The Offshore Taxation Review

COUPE DE MONDE HALF TIME: JERSEY 1 - GUERNSEY 0

Dr Raymond Ashton[1]

1 Introduction

The recent case of *Lutea Trustees Ltd v Orbis Trustees Guernsey Ltd* (1997) SC LR 735 has attracted much attention in Guernsey if only because the company is a well known trust company and many people in the trust industry do not understand why the matter was litigated in Scotland rather than Guernsey. There is a further complication in that Lutea Trustees Ltd is a Jersey trust company. The case has other novel aspects as it is the first major case in which a Guernsey based company has been involved regarding the scope of indemnity clauses. It also remains partially undecided in that whilst the matter has been determined against the trustees by the Scottish Court of Appeal there is another action pending under which the trustees are, in turn, claiming relief against the beneficiary. What is not clear is why both actions were not heard together. The case is also of interest because it is only rarely that Scottish trust law is brought into such sharp focus and in a cross border context. In order to fully understand the findings of the case it will be necessary to summarise the main points of Scottish trust law which will be examined in the next section. The following section will discuss the main points in the case whilst the fourth will discuss the implications for trust practitioners, whether in Guernsey or elsewhere. The final section will summarise the main findings of the preceding four sections.

1 Dr Raymond Ashton, Carey Langlois, Advocates & Notaries, 7 New Street, St Peter Port, Guernsey GY1 4BZ. Tel: (01481) 700 300 Fax (01481) 716 485.

2 Scottish Trust Law

By definition this description will be a very summarised view of this topic. What follows is based on the influential text books of Gloag & Henderson[2] and Wilson & Duncan.[3] The common law of Scotland is mainly derived from the civil law but in some minor areas the cannon law. Whilst there was probably no period when civil law accounted for the law of Scotland it would be true to say that civil law, as promulgated and amended by the Dutch and French commentators of the sixteenth and seventeenth centuries, forms the basis of the Scottish law of contract and property. In this regard the leading text of Erskine, Institute (1773, edited by Nicolson 1871), is a very important jurisprudential source and is still a widely cited source of Scottish law. Whilst Scottish law has been heavily influenced by the civil law tradition which in turn has its origins in the Roman law tradition the development of trust law owes much to the English tradition and in this regard the Trusts (Scotland) Act 1921[4] and Trusts (Scotland) Act 1961 are very similar to the corresponding English provisions. In this context it follows that whilst there are some important jurisprudential differences between English and Scottish law for most practical purposes the statutory framework is the same.

Erskine thought of a trust as in the 'nature of a disposition by which a proprietor transfers to another the property of the subject intrusted, not that it should remain with him, but that it may be applied to certain uses for the behalf of a third party.'[5] Whilst trusts may arise by operation of law and a person may find himself bound as a trustee without his consent or even against his wishes, Erskine's statement is a useful starting point as to the nature of a trust and the role of the trustee: namely, that whilst he may be the legal owner of the property held in trust, he owes obligations to use his powers as legal owner for the benefit of some person other than himself.

Scottish law uses slightly different terms to describe the *dramatis personae* involved. In this regard the interest of the beneficiary is referred as *jus crediti.* The person referred to under English law as the settlor is known as the truster and as in England a trust may be constituted by the act of a truster or by operation of law as no technical language is required for the creation of a trust. Where the purposes of a private trust fund do not exhaust the trust estate the familiar English concept of a resulting trust

---

2 *The Law of Scotland*, Eds numerous, W Green/Sweet & Maxwell 1995.

3 *Trusts, Trustees and Executors*, Wilson, W A, and Duncan, A G M, W Green/Sweet & Maxwell 1995. This book is not dissimilar in status to Underhill & Hayton in England.

4 It should be remembered that the English Trustee Act 1925 was a consolidation of a number of earlier Acts.

5 Erskine, Ins, III i 32.

arises. A trust may be revocable or irrevocable but a declaration (referred to by the Latin term *undublio*) that it is irrevocable will almost certainly be decisive. There are also rules relating to the variation of trusts which are very similar to those that pertain in England.

The position with regard to the appointment and resignation of trustees (in this context the word used is assumption rather than appointment) is similar to England and a sole trustee is not entitled to resign unless he has "assumed new trustees" who are in office at the date of his resignation. Under the common law the court has power to remove a trustee but this is only exercised reluctantly unless the trustee has been guilty of malversation (*mal fides* or bad faith) of office or has shown by his conduct that he is unfit to discharge his duties. As in England the duty of the trustees is to administer the trust in accordance with the provisions in the trust deed in so far as they are lawful and possible. It is also possible for the trustees to exercise powers which are neither contained in the settlement deed nor permitted by statute by applying (again as in England) to the court for authority which is referred to as the exercise of the *nobile officium*. For this purpose, *nobile officium* has been exercised to remedy a deficiency where some administrative power is absent in order to enable the trust purposes to be effectually carried out[6] or where there was an obvious *casus improvisus* (unforeseen situation) under the trust deed or (in the context of the readers of this journal) to facilitate the carrying out of an order of a foreign court[7].

As in English law, it has long been recognised that a trustee must not be *auctor in rem suam*, that is, put himself in a position where his duties as trustee conflict with his own interests and similarly unless the trust instrument provides otherwise (which it will inevitably do) invest funds in a manner prescribed by the Trusts (Scotland) Act 1961. There is also a doctrine of *cy pres* so that where the intention of the truster cannot be carried out in the precise manner envisaged by the trust deed the court will sanction a scheme to benefit a closely related cause. The application of this doctrine is usually made in conjunction with the exercise of the power of *nobile officium* referred to above.

Where a trustee is guilty of a breach of trust the trustee, following English principles, will be liable to make good all the loss occasioned by the breach. In this regard all the usual tracing remedies are available although in the case where trust monies are mixed with the trustee's private funds and the trustee draws cheques for his own purpose in

---

6 *Anderson's Trustees* (1932) SC 226 - 226.

7 *Lipton's Trustees*, (1943) SC 521 and *Campbell-Wyndham - Long's Trustees* (1951) SC 685.

the first instance, purposes the rule in *Clayton's Case*[8] does not apply and the trustee is assumed to have drawn his own money rather than that belonging to the trust.

It is common to find a clause in all deeds alleviating, to a greater or lesser extent, the responsibility of the trustees for the management and administration of the trust. Such clauses are often referred to by appellations such as exculpation, indemnity and exemption clauses. In the leading case of *Knox v Mackinnon*[9] it was held that a clause to the effect that trustees should not be liable for omissions, errors or neglect of management, nor *singuli* in *solidium* but each be liable for his own actual intromissions[10] only and not protect the trustee against his own positive breaches of duty. It is also settled law that such clauses are ineffectual to protect a trustee against the consequences of gross negligence (referred to as *culpa lata*) or of any conduct which is inconsistent with *bona fides*. However, it is also provided that where a trustee has committed a breach of trust at the instigation or request (whether in writing or not) of the beneficiary the court may, if it thinks fit, order that any part of the interest of that beneficiary, be applied in indemnifying the trustee.[11] In such cases it must be shown that the beneficiary appreciated that what was done was a breach of trust and his concurrence must have been both clear and direct.[12] This point is developed further below in the context of the case which will be discussed in the next section.

3 *Lutea Trustees v Orbis Trustees Guernsey Ltd*

As stated in the introductory section this case concerned the scope of an indemnity clause and basically decides, as was previously always thought to be the case, that an indemnity clause cannot provide greater protection than the retiring trustee previously enjoyed in his role as trustee. It follows that it will not protect a retiring trustee who has been grossly negligent. This is why the case is of particular importance to both Guernsey and Jersey trust and estate practitioners.

In terms of the nomenclature of the case the plaintiffs are known as the pursuers and more conventionally the defendants the defenders in Scotland. The case is unusual

---

8 (1816) 1 Mer 572.

9 (1888) 15R (HL) 83, see also *Inglis* (1965) SLT 326.

10 Reference is also made in the Scottish judgments and books to the use of the word intromit and intromissions which in more familiar English terminology means deal with or dealing with.

11 *Section 31 Trusts (Scotland) Act 1921.*

12 *Henderson v Henderson's Trustees* (1900) 2 F 1295.

in that it was decided at first instance on the equivalent of an English motion[13] and without hearing any evidence and as a consequence this has had most unfortunate implications for the reporting of the case. The relevant portion of the trust deed provided, *inter alia*, that:

> "The trustees shall not be in any way liable for any loss suffered as a result of the exercise of any of the powers given to them by these presents or for any fall in value of or for the validity and sufficiency of investments, securities and others held by them or on their account whether made or retained by the trustees or for omissions or for neglect in their management or for one another or for factors, attorneys, solicitors, accountants, stockbrokers, agents or others appointed or employed by them except that they were habit and repute responsible at the time of their appointment or employment but each for his or her own actual personal intromissions only."

In relation to their discretionary power the deed provided that:

> "Whenever it shall be necessary in connection with the affairs of the trust hereby created for the trustees to exercise any discretionary power whatever decision or resolution they may act upon shall be final and binding on all parties interested either directly or indirectly and the acts of the trustees shall not be liable to be called in question upon any ground whatever except fraud."

In 1993 Orbis Trustees Guernsey Limited ("Orbis") ceased to be trustees and were replaced by Lutea Trustees Limited ("Lutea"), a Jersey trust company. However, in 1991 Orbis had, at the request of the settlor, lent $914,000 to a Mr W on terms that he would repay the money in twenty one days together with interest equal to the amount of the loan. The trustees obtained from W shares as security which ultimately turned out to be worthless. When Lutea took over as trustees they granted an indemnity to Orbis in familiar terms:

> .....that all liabilities, actions proceeding, claims.....whatsoever.....including all or any liabilities.....in connection with the loan of $914,000.....

The deed of indemnity concluded, again, in familiar terms that, *inter alia,* the liability of the new trustees shall extend only to liabilities in respect of which the old trustees

---

13 In Scottish terms this is referred to as a *decree de plano.* The English equivalent can be found in RSC Order 14 (Queen's Bench Division) and in the Chancery Division, Order 86 (Chancery Division).

would have been entitled to reimbursement out of the trust fund had they remained trustees under the said deed of trust on its present terms.[14]

At first instance and almost as a preliminary point, Orbis maintained that the action was irrelevant on the grounds that by virtue of the trust deed they were immune from action and in any event were entitled to reimbursement from the new trustees in any event. This was dismissed at first instance. A powerfully constituted Scottish Court of Appeal held:

1 The advancement of such a large sum of money to a company at an interest rate which exceeded 1,000 per cent and which was in financial difficulties was an abrogation of the trustees duties to preserve the trust estate and not to make unnecessarily hazardous investments. As such, irrespective of the fact that Orbis had not valued the investment and that it was valueless, there was a clear breach of duty by Orbis. This clear breach of duty amounted to *culpa lata dolo a equiparatur* (gross negligence[15]) and that the judge at first instance had been correct in granting a decree *do plano* (literally with ease).

2 There was nothing in the trust deed which could excuse Orbis in respect of the loss attributable to the loan as a result of the grossly negligent actions of the old trustees, following the leading Scottish case of *Knox v Mackinnon* (1888) 15R (HL) 83.

3 As a necessary corollary of (2) that the terms of the indemnity which the new trustees gave to the old trustees only extended to any liability which the former trustees would have been entitled to have made good by reimbursement from the trust fund; it did not cover acts of gross negligence by the old trustees.

---

14 Interestingly although somewhat tangentially in the result it was argued that in relation to the scope of the indemnity that it should be read strictly, following *Smith v UMB Chrysler* [1978] SC (HL) 1 and in the case of ambiguity, *contra proferentes.* The defenders, Orbis, were the *proferentes* regarding the terms of the indemnity but in terms of liabilities the plaintiffs were *proferentes.* This is a doctrine of interpretation which states that the construction least favourable to the person putting forward an instrument should be adopted against him. For more on this subject see the excellent article by Matthews, P (1989) Conv 42.

15 In the Oxford Companion to Law, Professor D Walker discusses *culpa lata* as gross neglect verging on deliberate or reckless harm; by contrast Millet LJ, in *Armitage v Nurse* [1997] 2 All ER 705 has described the term as negligence plus a vituperative element. Readers are also referred to the influential article of Nobles, R, Trustees Exclusion Clauses in Jersey and England, 10 Trust Law International, 3, 1996 p 65-69.

4 Interestingly and strictly obiter Lord McCluskey reserved his position on the point whether the standard of care is different for a professional as opposed to a lay trustee.

4. Implications for Trust Practitioners

The first point that should be made is that the decision arises mainly as a result of procedural considerations. It is also clear from the speech of Lord McCluskey at 748 that this is not the only litigation on this subject matter before the court. Indeed the author has been informed that there is litigation before the court in the form of a claim under section 31[16] Trusts (Scotland) Act 1921 which provides:

> "Where a trustee shall have committed a breach of trust at the instigation or request or with the consent in writing of the beneficiary, the court may, if it shall think fit, make such order as to the court shall seem just for applying all or any part of the interest of the beneficiary in the trust estate by way of indemnity to the trustee or person claiming through him."

It follows that whilst the case confirms the scope of the indemnity clause in that a retiring trustee can only receive what he would be entitled to receive had he not retired it is by no means clear that ultimately Orbis will incur any liability,[17] hence the reference to the football score in the heading of the article. Indeed it is the author's understanding that the discovery process (or Scottish equivalent) is under way. On this basis further actions may be appropriate such as an action for either or both accountability on the basis of the existence of a constructive trust liability to account.

The second point is why the litigation took place in Scotland. Whilst it is clear that the proper law of the trust must have been Scottish the forum for administration (at least before the changeover in trustees) must have been Guernsey. It could be that the Trust Deed contained a provision to the effect that exclusive jurisdiction in respect of the provisions of the trust deed was reserved to Scotland. In the absence of such a clause this author is surprised why the Royal Court of Guernsey was not seised of the matter on the basis of section 4(b) The Trusts (Guernsey) Law 1989 which gives jurisdiction to the Royal Court of Guernsey in respect of a foreign trust where a trustee is resident in Guernsey or where any property of which is situated or administered in Guernsey. Whilst the choice of venue is unlikely to affect the ultimate

---

16 This provision is very similar to the English provision contained in section 62 Trustee Act 1925, and in Guernsey section 51, The Trusts (Guernsey) Law 1989 and Jersey Article 42 Trusts (Jersey) Law 1984.

17 On the face of it if the truster is also a beneficiary which from the litigation seems to be the case it is likely that the trustees have, *prima facie*, a good case to be indemnified.

result it would, at the very least, have had the result that both actions would have been heard together. At the moment we are in danger of drawing overall conclusions about the case which might not be justified once all the results of the litigation are known.

The third point arises from the strictly procedural nature of the case. By definition the court has been mainly concerned with the content of the documents and representations that have been made in relation to the documents and not with the particular factual events leading up to the making of the loan. As a result, it is very easy to be misled by the decision in the reported case. For all those who have worked either with or in offshore jurisdictions it is not a shock that such large sums were advanced or that whilst the loan was secured the security was not, apparently, valued. In the late nineteen eighties and early nineties such large transactions and on such terms were common in offshore jurisdictions. In that sense Orbis have been unlucky! Settlors often identified (and still do in some cases) the trust fund as their own asset particularly where they have a life interest and cannot understand why such transactions are not automatically processed! It is submitted that the Scottish court, when deciding whether relief should be given under section 31 account should be taken of the customs and practices of the forum for administration at the time the loan was made.

The final point concerns the meaning of the words "gross negligence". Whilst assistance might be obtained from the jurisprudence relating to bailments, liability of municipal authorities for accidents attributable to snow and ice and to gratuitous passengers of drivers it must be borne in mind that there is a special relationship between the trustees and the beneficiaries. Thus, it is submitted, the trustees will have more onerous obligations than the persons involved in the other situations referred to in the preceding sentence. Notwithstanding this limitation the author is of the view that the decision[18] of Mance J, in a shipping case, provides a valuable insight into this term:

> "'gross' negligence is clearly intended to represent something more fundamental than failure to exercise proper skill and/or care constituting negligence. But, as a matter of ordinary language and general impression, the concept of gross negligence seems to me capable of embracing not only conduct undertaken with actual appreciation of the risks involved, but also serious disregard of or indifference to an obvious risk.....I see no difficulty in accepting that (a) the seriousness or otherwise of any injury that might arise, (b) the degree of likelihood of its arising and (c) the extent to which someone takes any care at all are all potentially material when considering whether particular conduct should be regarded as so abhorrent as to attract the epithet of 'gross' negligence."

---

17 *The Hellespoint Ardent* [1997] 2 Lloyds Rep 547, at p 586-588.

5 Conclusions

On a practical level before reading a Scottish law case it would be useful to have a Latin revision lesson or alternatively have a copy of Trayner's Latin Maxims & Phrases to hand. Indeed this is indispensable for the English legally trained lawyer. The latter book is now, unfortunately, out of print but, as stated, is indispensable to a full appreciation of a Scottish trust case and more generally to any case with what might be called a large Roman Law element.

The case does not advance matters much further other than to highlight the limited nature of the indemnity which a retiring trustee can receive from a new trustee which in turn is dictated by the constraints of general trust law. As a consequence it is not possible to contract out of gross negligence. However, (and more to the point) the case does not take us any further in terms of our understanding of the term gross negligence. A definitive statement on this issue is badly needed.

As indicated above, there is other litigation pending and it is hoped that account is taken of the custom and practice of the offshore industry at the time the facts giving rise to the case took place. This is necessary to put the case in context and to the extent that the Scottish court is not able to follow this custom and practice it does suggest that perhaps the trustees should have taken action in the Guernsey court on the basis that it is more likely that a more sympathetic hearing would have been given to such practices. This highlights an important tactical issue: the *forum conveniens* may be crucial to the determination of the outcome of the litigation. Often insufficient attention is given to this factor in cross border litigation. As trust litigation is gathering apace in offshore jurisdictions advisers should bear this point carefully in mind in the future.

The last point is concerned with the future. As indicated in the title the case is only part of the outstanding litigation. Readers of this journal should pay careful attention to the Law Reports for the final outcome as at the moment we are only at the half way stage. Whilst the litigation half time score is one nil in favour of the Jersey trustees, readers should be aware of the rivalry between the two jurisdictions and in particular the famous annual match between the two islands known as the 'Muratti' (the English equivalent of a local football 'derby'): a strong fight back, in terms of section 31 Trusts (Scotland) Act 1921 is expected by the Guernsey trustees in the second half.