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Exclusions and exemptions in onshore and offshore trusts

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FOLLOWING *SPREAD* V *HUTCHESON*, GUERNSEY AND JERSEY TRUSTS LAW HAS BEEN ALIGNED MORE CLOSELY WITH ENGLISH AND WELSH LAW WITH REGARDS TO DUTIES AND STANDARDS OF CARE. HOWEVER, A CLEAR LEGISLATIVE PROVISION IS REQUIRED IN ENGLAND AND WALES IN ORDER TO LIMIT EXCLUSIONS AND EXEMPTIONS

By Daniel Clarry

ABSTRACT

- The *en bon père de famille* obligation in Guernsey trusts law has effectively been translated in the *Spread* v *Hutcheson* litigation, in which it was uniformly accepted to be equivalent to the standard of care applicable to trustees in England and Wales and in Jersey, i.e. the 'prudent man of business'. This removes a latent uncertainty in Guernsey law.
- Despite difficulties in the reasoning of the Privy Council in *Spread*, the alignment of standards of care of trustees develops greater cohesion across these prominent trust jurisdictions and facilitates the coherent development of trusts jurisprudence.
- Unlike in England and Wales, the standards of care in Guernsey and Jersey are mandatory, rather than applicable by default, which ensures greater accountability in offshore trust administration.
- Guernsey and Jersey have also taken a more robust position on trustee exemption clauses, where liability for a trustee's own fraud, wilful default or gross negligence cannot be exempted; in England and Wales, all liability save actual fraud can be exempted.
- Despite leading trust precedents recommending against broadly drafted trustee-exemption clauses, and attempting to strike an appropriate balance between accountability and protection of trustees, trustees may nevertheless insist on lower standards of care being imposed, consonant with the general and statutory law.
- As a matter of public policy, the minimum standards of care that apply to trustees and any consequent liability ought to be clearly stated as a matter of law, irrespective of trust drafting. Trustees would not be unduly exposed as there remain internal mechanisms in trusts law that protect diligent trustees from liability, including obtaining legal advice, concurrence from beneficiaries and protection from the court, where necessary.

This article builds and reflects on an article published in the *Jersey & Guernsey Law Review*,[1] which was primarily concerned with *Spread Trustee Co Ltd* v *Hutcheson*.[2] In *Spread*, a preliminary question of law made its way to the Privy Council: could a trustee be exempted from liability for gross negligence in a trust instrument before 19 February 1991?[3] If a trustee could not be so exempted, the provisions in the relevant trust instruments were invalid and the beneficiaries could pursue their claim against the trustee.

Departing from the Royal Court of Guernsey and the Guernsey Court of Appeal judgments, and only by a slim majority (3:2), the Privy Council held that a trustee could be exempted from liability for gross negligence in a trust instrument under Guernsey customary law. Essentially, the Privy Council aligned the *Trusts (Guernsey) Law 1989* with Guernsey customary law such that, until 19 February 1991 when statutory amendment came into force, Guernsey customary and statutory law both allowed trustee exemption clauses that excluded liability for gross negligence.

There were three problems with that approach. First, the *Trusts (Guernsey) Law 1989* was not a codification of Guernsey trusts law and it should not have been treated as such by approaching the determination of Guernsey customary law as simply a matter of statutory construction. Second, the explanatory material that accompanied the relevant amendment to the *Trusts (Guernsey) Law 1989* to explicitly prohibit the exemption of liability for gross negligence in a trust instrument did not treat that amendment as a particularly momentous occasion, even though it was the first time that gross negligence could not be excluded by the terms of a trust instrument under Guernsey law, according to the majority of the Privy Council.[4] Third, although the Privy Council accepted that the statutory draftsmen in Guernsey followed a similar amendment in Jersey,[5] the prohibition on 'gross negligence' was also introduced in Jersey without any indication that it was a significant change to the pre-existing law.[6]

One interesting feature of the *Spread* litigation warrants further attention because it resolves a peculiar aspect of Guernsey trusts law. In determining the position of trustee exemption clauses under Guernsey customary law as a matter of statutory interpretation, the Privy Council did not consider that the unique obligation to act *en bon père de famille* in the *Trusts (Guernsey) Law 1989*, which was accepted to be declaratory of Guernsey customary law, had any particular role to play in the determination of the question of whether a trustee of a Guernsey trust could be exempted from liability for grossly negligent conduct. Instead, the Privy Council equated the obligation to act *en bon père de famille* with the standard of care expected of a trustee in English and Welsh law.

The consequence of doing so is that the standards of care in onshore and offshore trust administration are aligned, even though the law on trustee exemption clauses remains quite different. The duties of care applicable to trustees in England and Wales, Guernsey and Jersey are the subject of this article, as well as the law on exclusion and exemption clauses and the drafting practice that has arisen responsively. It will be shown that, while the duties of care are similarly framed in onshore and offshore trust administration, the mandatory nature of Guernsey and Jersey trusts laws ensures that duties of care cannot be excluded by the terms of a trust in the Channel Islands and trustees cannot be exempted from liability for gross negligence. This enhances the

1. Daniel Clarry, 'The Offshore Trustee *en bon père de famille*', *Jersey & Guernsey Law Review*, 5 (2014) 18(1)
2. [2012] 2 AC 194 (*Spread* (PC))
3. On 19 February 1991, an amendment to the *Trusts (Guernsey) Law 1989* came into effect that explicitly prohibited the exemption of liability for a trustee's grossly negligent conduct
4. States' Advisory and Finance Committee, 'Report on Amendments to the *Guernsey (Trusts) Law 1989*', 16 March 1990, *Billet d'État VIII of 1990*, article VI. See also *Spread Trustee Co Ltd* v *Hutcheson* (2009) 10 GLR 403 (*Spread* (GCA)), 35–38, per Martin JA
5. *Spread* (PC) at 216, per Lord Clarke
6. Finance and Economics Committee, Explanatory Note (lodged with the draft *Jersey Amendment Law au Greffe*), 31 January 1989

accountability of offshore trustees, relative to their onshore counterparts.

STANDARDS OF CARE IMPOSED ON TRUSTEES

A duty of care is a fundamental aspect of trust administration that regulates the manner in which a trustee executes the trust and performs their duties as trustee. The difficulty in defining the duty of care is in shaping an objective standard of care to be applied to the different persons that may occupy the office of trustee. Nevertheless, it is fundamental to ensuring that a trust will actually be performed.

Aside from active or positive breaches of trust (i.e. misapplication or misappropriation of trust property), trustees commonly commit passive breaches of trust by failing to act diligently – in particular, by failing to monitor trust investments that have not been diversified but simply comprise a concentrated shareholding in a particular company that declines in value. Three examples may be given of such cases. In *Re Lucking's Will Trusts*,[7] a trustee was held liable for failing to supervise the management of a company in which the trust had a controlling interest. In *Bartlett* v *Barclays Bank Trust Co Ltd (No.2)*,[8] a bank was held liable for failing to supervise two land development projects undertaken by a company of which the bank held 99.8 per cent of the shares as trustee. In *Spread*, the relevant conduct concerned the alleged failure by the trustee to monitor shares, the value of which plummeted over several years by some GBP50 million.[9]

Such cases give rise to the common complaint that trustees did not take appropriate steps to preserve the value of the trust fund and did not act diligently. Similarly, trustees who do not actively administer the trust may also be held liable for failing to monitor the performance of the trust by their co-trustees. In such cases, the difficulty is in setting the appropriate threshold for liability where the trustee has not actively breached the trust. For this reason, the framing of duties of care to regulate such conduct is especially important, albeit difficult to define in abstraction, and has given rise to shifting standards of care to take account of the circumstances.

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England and Wales

In England and Wales, a trustee's duty of care is expressed as, or likened to, that of the 'ordinary prudent man of business' or, in other words, it is the duty to act as a reasonable and prudent man would act in the conduct of his own affairs – that is,

7. [1967] 3 All ER 726
8. [1980] Ch 515
9. In *Spread*, the claim was met by an exemption clause that successfully relieved the trustee from liability except for 'wilful and individual fraud or wrongdoing...' See also Hildyard J, 'Prudence and Vituperative Epithets' (lecture given to the Chancery Bar Association's Annual Conference (London, 21 January 2012)), available at www.step.org/prudence-and-vituperative-epithets (estimating the loss to the trust fund to be some GBP50 million)

with reasonable care and skill.[10] In the general law, that formulation allows for a shifting standard depending on the care and skill that one would expect would be exercised by the trustee in question, since the test of what is 'reasonable' in the circumstances must reflect the qualities of the trustee in question.[11]

Similarly, in the statutory law, a trustee's duty of care is to 'exercise such care and skill as is reasonable in the circumstances, having regard in particular to the following: any special knowledge or experience that he has or holds himself out as having; and, if he acts as trustee in the course of a business or profession, to any special knowledge or experience that it is reasonable to expect of a person acting in the course of that kind of business or profession.'[12] Furthermore, the conduct of a trustee will be considered by having regard to the facts and circumstances known to, or that ought to have been known by, the trustee at the time, and not with the benefit of hindsight.[13]

By virtue of the *Trustee Act 2000* (TA 2000), the statutory duty of care is attached to a broad range of powers of a trustee, however conferred.[14] The statutory duty of care attaches to powers to:[15] invest and review such investments; acquire land;[16] employ agents, nominees and custodians and review the conduct of such persons;[17] compound liabilities, etc;[18] insure trust property;[19] and get in reversionary interests falling into possession, as well as ascertaining and fixing the value of trust property.[20] However, the statutory duty of care only applies in the circumstances specified by the TA 2000.[21] As such, it is important to consider not only when the duty of care does apply, but when it does not: 'The duty of care does not apply if or in so far as it appears from the trust instrument that the duty is not meant to apply.'[22] In so providing, the TA 2000 makes the statutory duty of care a default, rather than mandatory, rule of English and Welsh trusts law. It is, therefore, left to settlors, and especially those advising them, to choose to exclude the statutory duty of care by the terms of the trust.

Despite extensive consultation and statutory reform, the TA 2000 failed to grapple with the difficult public policy question of setting the limits on lawful exclusion of a trustee's duty of care and what base standard must apply. Thus, trust instruments will either exclude the statutory duty of care altogether, thereby rendering the core aspect of the TA 2000 inoperative, or reduce the higher standard of care applicable to professional trustees down to that of lay trustees.[23] This manipulation of a trustee's duty of care means that professional trustees often only owe a duty to act honestly and in good faith or, put another way, not to act dishonestly or fraudulently.

Despite the vulnerability of beneficiaries to the mismanagement of trustees, the rules of English and Welsh trusts governance are weak relative to those applicable to other fiduciary office-holders, such as directors and certain trustees, where duties of due or reasonable care and skill cannot be excluded by the terms of a constitutive document.[24] The approach taken in the statutory law of setting the duty of care merely as a default rule permits the perverse result that those who are

10. *Re Speight; Speight* v *Gaunt* [1883] 22 Ch D 727 per Sir George Jessel MR (CA), affd sum nom *Speight* v *Gaunt* [1883] 9 App Cas 1; *Learoyd* v *Whiteley* [1887] 12 App Cas 727 (HL); *Re Godfrey* [1883] 23 Ch D 483; *Re Chapman* [1896] 2 Ch 763 (CA); *Re Lucking's Will Trusts* [1967] 3 All ER 726, [1968] 1 WLR 866; *Bartlett* v *Barclays Bank Trust Co Ltd (Nos.1 and 2)* [1980] 1 Ch 515, 531 and 534 per Brightman J; *Henderson* v *Merrett Syndicates Ltd* [1995] 2 AC 145; *Bristol & West Building Society* v *Mothew* [1998] Ch 1. See also Getzler, 'Duty of Care', in Birks & Pretto (eds), *Breach of Trust* (2002) 41

11. *Bartlett* v *Barclays Bank Trust Co Ltd (Nos.1 and 2)* [1980] Ch 515, 531–534 per Brightman J. See also *Re Waterman's Will Trusts* [1952] 2 All ER 1054

12. TA 2000, s1

13. *Re Hurst* [1892] 67 LT 96 (CA), 99 per Lindley LJ; *Re Chapman* [1896] 2 Ch 763, 777–78 (CA); *Nestle* v *National Westminster Bank* [1994] 1 All ER 118 (CA), 134 per Staughton LJ

14. TA 2000, s2 and Schedule 1

15. TA 2000, sections 4 and 5, and Schedule 1, s1

16. TA 2000, s8, and Schedule 1, s2

17. TA 2000, sections 11, 16, 17, 18 and 22, and Schedule 1, s3

18. TA 2000, Schedule 1, s4; *Trustee Act 1925* (UK), s15

19. TA 2000, Schedule 1, s5; *Trustee Act 1925* (UK), s19

20. TA 2000, Schedule 1, s6; *Trustee Act 1925* (UK), s22(1) and (3)

21. TA 2000, s1(1) and (2)

22. TA 2000, Schedule 1, s7

23. Reed and Wilson, *The Trustee Act 2000 – A Practical Guide* (Jordan Publishing, 2001), page 154

24. See, for example, *Companies Act 2006*, s174 (as to directors), s750 (as to debenture trustees); *Pensions Act 1995*, s33 (as to pension trustees); *Financial Services and Markets Act 2000*, s253 (as to unit trustees)

> The majority of the Board of the Privy Council interpreted the *en bon père* obligation as 'the duty... to act as a reasonable and prudent trustee would act – that is, with reasonable care and skill'

entitled to charge professional fees for trust administration and hold themselves out as having certain skills often owe no duty to take any reasonable care, or the same standard applicable to trustees receiving no remuneration at all.

Guernsey

In Guernsey, a trustee's duty of care is reduced to the expression that 'a trustee shall, in the exercise of his functions, observe the utmost good faith and act *en bon père de famille*'.[25] In terms of what that, at least superficially distinctive, language means in practical terms, we have authoritative guidance from the Privy Council in *Spread*.[26] Indeed, this was one of the points that was upheld *per curiam* on appeal at an intermediate and final appellate level and is, therefore, an important aspect of *Spread*.

Martin JA (with whom Vos and Montgomery JJA agreed) considered there to be 'no doubt the obligation to act *en bon père de famille* implies a standard of care similar to that required of trustees in England, namely that of a prudent man of business...'[27] On appeal, Lord Clarke (with whom Lord Mance and Sir Robin Auld agreed) also considered that it is 'no doubt the duty of a trustee under [the relevant provision of the *Guernsey (Trusts) Law 1989* codifying the *en bon père de famille* obligation] to act prudently and thus to exercise all reasonable care and skill to be expected of a trustee.'[28] The majority of the Board of the Privy Council went on to endorse that approach by interpreting the *en bon père* obligation as 'the duty... to act as a reasonable and prudent trustee would act – that is, with reasonable care and skill.'[29] In his leading opinion, Lord Clarke considered that the trustee's duty of care is 'the same' in Guernsey as it is in England and Wales and also in Scotland.[30]

However, the content of the duty of care in Guernsey law to act *en bon père de famille* was not the issue that split the Board of the Privy Council. Indeed, Lady Hale similarly held that 'the duty to act *en bon père de famille* [was] clearly equivalent to the duty adopted by English law to act as a prudent man of business...'[31] Rather, the key issue was whether the *en bon père de famille* obligation carried with it some particular quality, such that a prospective exemption of liability for gross negligence in a trust instrument would be inimical to a Guernsey trust.

On that question, no peculiar meaning was given to the *en bon père* obligation, even though the dissenting opinions, especially that of Lord Kerr, highlighted the obvious difference between the two duties, in that the English and Welsh duty of care did not embody the concept of fiduciary loyalty, whereas the duty to act as a *bon père* plainly was fiduciary in nature.[32] Leaving that dissent aside, the unique obligation to act *en bon père de famille* was authoritatively translated in *Spread* and equated with English and Welsh trusts law.

Eliding those jurisdictions together on a central feature of trust law serves to develop greater cohesion and coherency across those different jurisdictions, whereas a different approach that

25. *Trusts (Guernsey) Law 2007*, s22(1)
26. *Spread* (PC) at 213 per Lord Clarke (with whom Lord Mance and Sir Robin Auld agreed)
27. *Spread* (GCA) at 421, citing *Bartlett* v *Barclays Bank Trust Co Ltd (No.2)* [1980] 1 Ch 515
28. *Spread* (PC) at 209
29. *Spread* (PC) at 209, 213
30. *Spread* (PC) at 209, 218 per Lord Clarke (with whom Lord Mance and Sir Robin Auld agreed), citing *Bartlett* v *Barclays Bank Trust Co Ltd (No. 2)* [1980] 1 Ch 515 and *Lutea Trustees Ltd* v *Orbis Trustees Guernsey Ltd* (1998) SLT 471, 473 per Lord Justice Clerk (Cullen)
31. Spread (PC) at 245
32. Spread (PC) at 255 per Lord Kerr

lent weight to the distinctiveness of the obligation to act *en bon père de famille* in Guernsey trust law may have isolated Guernsey from the prominent trusts jurisdictions upon which it typically draws in developing its trusts jurisprudence. Guernsey would have been alone in fashioning its trust law around the *en bon père de famille* obligation.

Although the mixed legal system of Quebec has known the trust for a long time, the *en bon père de famille* obligation was not adopted in the recodification of the Quebec *Civil Code* in 1994.[33] France has also recently purged the *en bon père de famille* expression from its general law.[34] As such, a distinctive interpretation of a Guernsey trustee's obligation to act *en bon père de famille* would have created uncertainty in advising on Guernsey trusts and increased the likelihood of litigation to resolve those uncertainties. For that reason, even though the obligation for a Guernsey trustee to act *en bon père de famille* does look superficially distinct, there are good policy reasons behind equating that obligation with the prudent man of business in English and Welsh trust law. In any event, no indication was given in the explanatory report that accompanied the passage of the *Trusts Guernsey Law 1989* as to what was meant by the obligation to act *en bon père de famille*, and little appears to have been known in the profession, more generally.[35]

Jersey

In contrast with Guernsey, Jersey mirrors the English and Welsh trustee's duty of care much more closely in providing that a 'trustee shall in the execution of his or her duties and in the exercise of his or her powers and discretions... act... with due diligence... as would a prudent person... to the best of the trustee's ability and skill; and observe the utmost good faith.'[36]

As in England and Wales, shifting standards apply in each case, depending on the particular circumstances, especially the individual trustee's ability and skill. However, like in Guernsey, and unlike in England and Wales, the duty of care is not excludable by the terms of a trust instrument in Jersey, thereby making it a mandatory rule of Jersey trust law and part of the irreducible core of a Jersey trust, which cannot be excluded when creating such a trust. Jersey has, therefore, taken a more robust approach than England and Wales in fixing the duty of care in Jersey trust administration.

TRUSTEE EXCLUSION AND EXEMPTION CLAUSES

Trustee exemption clauses are closely connected with the trustee's duty of care because such clauses curtail the consequences that would ordinarily arise from the breach of the trustee's duty of care. It also follows, therefore, that a distinction must be drawn between trustee exemption clauses, which purport to exempt a trustee from liability arising from a breach of trust, and trustee exclusion clauses, which attempt to exclude the underlying duty itself.

That conceptual difference translates, in practical terms, into the kinds of remedies that might be available to correct a breach of trust.[37] Equitable compensation, for example, is one remedy that may be available, but other remedies may be more appropriate depending on the circumstances of the case. While a trustee exemption clause might restrict the personal liability of a trustee in terms of paying equitable compensation, and thereby provide adequate protection for a trustee, other remedies ought to

33. A Popovici, *'Le bon père de famille'*, in *Mélanges Adrian Popovici: Les couleurs du droit*, Générosa Bras Miranda et Benoît Moore, (Montréal : Éditions Thémis, 2010), page 125

34. J Parienté, '*Le "bon père de famille" va disparaître du droit français*', *Le Monde*, 20 January 2014, available at www.lemonde.fr/politique/article/2014/01/20/le-bon-pere-de-famille-menace-de-disparition-du-droit-francais_4350949_823448.html

35. States' Advisory and Finance Committee, 'Report on the *Guernsey (Trusts) Law*', 12 February 1988, *Billet d'État IX of 1988*. No further indication was given as to the meaning of the *en bon père de famille* expression with the amendments to the *Guernsey (Trusts) Law 1989* in 1990 nor in the re-enactment of that Act in 2007 – see States' Advisory and Finance Committee, 'Report on Amendments to the *Guernsey (Trusts) Law 1989*', 16 March 1990, *Billet d'État VIII of 1990*; Commerce and Employment Department, 'Review of Trust Law in Guernsey', *Billet d'État XXI* (reported 13 December 2006, reviewed 27 October 2006), 2398–413

36. *Trusts (Jersey) Law 1984*, s21(1)

37. Compare *Futter* v *HMRC; Pitt* v *HMRC* [2013] 2 AC 108, [2013] UKSC 26, 89 per Lord Walker

be available to beneficiaries, such as injunctive relief and the ancillary liability of third parties. Trustee exclusion clauses risk destabilising other remedial relief and ought to be avoided, despite the possibility of excluding a trustee's duty of care in English and Welsh law.

Here, we are concerned with the different approaches to trustee exemption clauses in onshore and offshore trust administration – again, a more robust position has been taken in the Channel Islands than England and Wales on the ability of trustee exemption clauses to exempt trustees of liability.

England and Wales

In England and Wales, *Armitage* v *Nurse* remains the leading authority on the lawful scope of trustee exemption clauses. In the case, the Court of Appeal upheld a clause exempting any trustee 'for any loss or damage... to [the Trust]... unless such loss or damage shall be caused by his own actual fraud'.[38] There, Millett LJ held that 'actual fraud' meant dishonesty and that, as the clause was not void on the grounds of public policy, the trustee would only be liable for dishonesty. If the trustee breached the trust, but did so with the honest intention of furthering the interests of the trust, then the trustee would be exempted from personal liability, according to Millett LJ.

That subjective approach to dishonesty has subsequently been pared back by the Court of Appeal in *Walker* v *Stones*, in which Sir Christopher Slade rejected the subjective approach for dishonesty and preferred a more objective test for determining whether an 'honest belief' of the trustee was 'reasonable'.[39] As such, a trustee exemption clause 'would not exempt the trustees from liability for breaches of trust, even if committed in the genuine belief that the course taken was in the best interests of the beneficiaries, if such belief was so unreasonable that no reasonable solicitor-trustee could have held that belief.'[40] That adds a preferable gloss to Millett LJ's approach.

As to the possibility of excluding a trustee's duty of care, Millett LJ clearly stated:[41]

> 'I accept the submission made on behalf of [the beneficiary] that there is an irreducible core of obligations owed by the trustees to the beneficiaries and enforceable by them which is fundamental to the concept of a trust. If the beneficiaries have no rights enforceable against the trustees, there are no trusts. But I do not accept the further submission that these core obligations include the duties of skill and care, prudence and diligence. The duty of the trustees to perform the trusts honestly and in good faith for the benefit of the beneficiaries is the minimum necessary to give substance to the trusts, but in my opinion it is sufficient.'

To be absolutely clear, Millett LJ went further in stating:[42]

> 'In my judgment [the relevant clause in the trust instrument] exempts the trustee from liability for loss or damage to the trust property no matter how indolent, imprudent, lacking in diligence, negligent or wilful he may have been, so long as he has not acted dishonestly.'

From a public policy perspective, that view is unsatisfactory.[43] Indeed, the prevalence of broadly drafted trustee exemption clauses in the trust industry has caused the perverse situation that the very trustees that ought to have higher standards apply to their conduct in administering trusts are the very persons who insist on the lowest standards of care and fullest exemptions.[44]

38. *Armitage* v *Nurse* [1998] Ch 421
39. *Walker* v *Stones* [2001] QB 902, 939 per Sir Christopher Slade
40. *Walker* v *Stones* [2001] QB 902, 941 per Sir Christopher Slade. For a subsequent interpretation of the objective assessment of reasonableness, see *Fattal* v *Walbrook Trustees (Jersey) Ltd* [2010] EWHC 2767 (Ch), paras 78–82 per Lewison J; *Madoff Securities International Ltd* v *Raven* [2013] EWHC 3147, paras 323–26 per Popplewell J. On the test for dishonesty, compare *Barlow Clowes International Ltd (in liquidation)* v *Eurotrust International Ltd* [2006] 1 All ER 333 and *Twinsectra Ltd* v *Yardley* [2002] 2 AC 164
41. *Armitage* v *Nurse* [1998] Ch 421, 253–54 per Millett LJ (with whom Hirst and Hutchison JJA agreed)
42. *Armitage* v *Nurse* [1998] Ch 421, 251 per Millett LJ (with whom Hirst and Hutchison JJA agreed)
43. Dal Pont, 'The Exclusion of Liability for Trustee Fraud', 6 APLJ 41 (1998)
44. Compare Law Commission, *Trustee Exemption Clauses* (No.171, 2002), para 3.31; Law Commission, *Trustee Exemption Clauses* (No.301, 2006), para 4.10

> The prevalence of broadly drafted trustee exemption clauses in the trust industry has caused the perverse situation that the very trustees that ought to have higher standards apply to their conduct in administering trusts are the very persons who insist on the lowest standards of care and fullest exemptions

Following extensive consultation and reporting by the Law Commission, which only produced soft recommendations and a 'rule of practice',[45] that position is unlikely to change in England and Wales unless a suitable case is taken to the UK Supreme Court to test the correctness of *Armitage* v *Nurse*, key aspects of which have been subsequently questioned.[46] It may be that the UK Supreme Court may consider that a clause which purports to prospectively exempt a trustee from all forms of liability for loss or damage caused to a trust 'no matter how indolent, imprudent, lacking in diligence, negligent or wilful [the trustee] may have been, so long as [the trustee] has not acted dishonestly' is unacceptable and is not to be borne by the beneficiaries. In the interim, English and Welsh trustees are likely to insist on broad trustee exemption clauses to avoid liability for gross negligence.[47]

Guernsey

Since 19 February 1991, Guernsey has provided greater protection to beneficiaries in the offshore administration of Guernsey trusts than that provided in England and Wales. Specifically, this was achieved by prohibiting the exemption or indemnification of liability for a breach of trust arising from the trustee's 'own fraud, wilful misconduct or gross negligence.'[48] For the avoidance of doubt, Guernsey trusts law also invalidates *pro tanto* any term of a trust that purports to relieve or indemnify a trustee of liability for a breach of trustee arising from his own fraud, wilful misconduct or gross negligence.[49] A trustee will be personally liable, irrespective of the existence of a trustee exemption clause for 'any loss or depreciation in value of the trust property resulting from the breach', as well as for 'any profit which would have accrued to the trust had there been no breach'.[50]

Liability is, however, appropriately limited where there are multiple trustees and only some of the trustees have participated in the breach of trust. In such cases, the innocent trustee will not be liable unless 'he becomes or ought to have become aware of the breach or of the intention of his co-trustee to commit the breach', and 'he actively conceals the breach or intention, or fails within a reasonable time to take proper steps to protect or restore the trust property or to prevent the breach.'[51] A similar situation arises where a newly appointed trustee discovers past breaches of trust, in which case the new trustee 'shall take all reasonable steps to have the breach remedied.'[52]

45. Law Commission, *Trustee Exemption Clauses* (No.301, 2006), paragraphs 7.1–7.2. See also STEP, 'Guidance Notes: STEP Practice Rule to Trustee Exemption Clauses', available at www.step.org/guidance-notes. See Kenny, 'Conveyancer's Notebook: The Good, the Bad and the Law Commission' [2007] Conv 103, 103–08

46. E.g. *Spread* (PC) 46–52 per Lord Clarke (with whom Lord Mance and Sir Robin Auld agreed), 129 per Lady Hale; Law Commission, *Trustee Exemption Clauses* (No.171, 2002), paragraph 2.54; Hildyard J, 'Prudence and Vituperative Epithets', available at www.step.org/prudence-and-vituperative-epithets

47. E.g. *Re Clapham's Estate; Barraclough* v *Mell* [2006] WTLR 203; [2005] EWHC B17

48. *Trusts (Guernsey) Law 2007*, s39(7)

49. *Ibid*, s39(8)

50. *Ibid*, s39(1)

51. *Ibid*, s39(4)

52. *Ibid*, s39(3) and (6)

Jersey

In functionally equivalent terms to Guernsey, Jersey has taken a similarly robust position with respect to trustee exemption clauses, in providing that 'nothing in the terms of a trust shall relieve, release or exonerate a trustee from liability for breach of trust arising from the trustee's own fraud, wilful misconduct or gross negligence.'[53] The potential liability of a trustee is similarly broad, including 'the loss or depreciation in value of the trust property resulting from such breach' and 'the profit, if any, which would have accrued to the trust property if there had been no such breach.'[54]

The strictness of the rules on trustee liability are moderated by a trustee only being 'liable for a breach of trust committed by the trustee or in which the trustee has concurred' and not being liable for a breach of trust by a co-trustee, 'unless the trustee becomes aware or ought to have become aware of the commission of such breach or of the intention of his or her co-trustee to commit a breach of trust... and the trustee actively conceals such breach or such intention or fails within a reasonable time to take proper steps to protect or restore the trust property or prevent such breach.'[55] As is the case in Guernsey, 'a trustee shall not be liable for a breach of trust committed prior to the trustee's appointment, if such breach of trust was committed by some other person', although a new trustee must 'take all reasonable steps to have such breach remedied'.[56]

BALANCING ACCOUNTABILITY AND PROTECTION OF TRUSTEES

It is a widely held view that professional trustees and possibly, although it is less likely, well-advised lay trustees will draft trustee exemption clauses to the fullest possible extent as a matter of course. In Australia, one leading trust commentary notes it to be 'a melancholy fact that [trustee exemption] clauses are usually insisted on by highly paid professional trustees (like trustee companies), who hope to gain immunity from the consequences of departing from their own advertised standards of expertise'.[57] In England and Wales, a similar, seemingly inescapable, melancholy pervades trusts discourse. Indeed, one need look no further than the leading case of *Armitage* v *Nurse*, in which Millett LJ said '... it must be acknowledged that the view is widely held that these [trustee exemption] clauses have gone too far, and that the trustees who charge for their services and who, as professional men, would not dream of excluding liability for ordinary professional negligence should not be able to rely on a trustee exemption clause excluding liability for gross negligence'.[58]

Kessler QC said in an earlier edition of his popular trust drafting book: 'The problem with exemption clauses, it is considered, is not one of trust law but of trust draftsmanship. The solution is not law reform, but a drafting solution; to require appropriate use of such clauses in trust drafting. A strengthening of the rules of professional conduct – or to a greater recognition of the implications of existing rules – would be the best solution to the problem.'[59] In the latest edition of that text, Kessler QC and Sartin go on to rightly acknowledge that they really have no idea whether such an approach has been a success or not and that an empirical study would be required to provide some indication of the measure of success.

However, the melancholy fact that trustee exemption clauses have gone too far in practice is not an inescapable reality. It is a matter for each jurisdiction to ensure minimal standards of care in the administration of trusts by setting mandatory rules that reflect the underlying public policy imperatives behind competent trust administration. To that end, it is far better to set the limits up to which a settlor can prospectively exempt a trustee from the

53. *Trusts (Jersey) Law 1984*, 30(10)
54. *Ibid* at 30(2)(a) and (b)
55. *Ibid* at 30(5)(a) and (b)
56. *Ibid* at 30(4) and (9)

57. *Jacobs' Law of Trusts in Australia*, 7th edn (LexisNexis, 2006), paragraphs 1619–20
58. *Armitage* v *Nurse* [1998] Ch 241, 256 per Millett LJ (with whom Hirst and Hutchison JJA agreed)
59. Kessler QC, *Drafting Trusts and Will Trusts*, 7th edn (Sweet & Maxwell, 2004). See also Kessler QC and Pursall, *Drafting Cayman Islands Trusts* (Sweet & Maxwell, 2006), page 94

> The answer to the 'problem' of trustee exemption clauses is not optimistic recommendations and soft law but statutory reform to define exactly what is the minimum standard of care that a trustee is required to take in the administration of a trust

financial consequences of their misconduct, as is the case in the Channel Islands.

Furthermore, if it is so widely regarded that trustee exemption clauses have gone too far then the answer to the 'problem' of trustee exemption clauses is not optimistic recommendations and soft law but statutory reform to define exactly what is the minimum standard of care that a trustee is required to take in the administration of a trust. Such an approach has the benefit of certainty and would not require any empirical study to determine the measure of its success.[60]

Interestingly, the melancholy fact with respect to the onshore trust industry is not the result of trust draftsmen following precedent texts from leading practitioner guides, but from the insistence by trustees either acting on advice or from an awareness of the lower standard of care imposed on them in the general and statutory law.

In the modern trust precedents, we find an encouraging shift away from the inclusion of broad trustee exemption clauses. Thus, in relation to the 'liability of trustees', the second edition of the *STEP Standard Provisions* recommends the inclusion of the following provision into trust instruments: 'a Trustee shall not be liable for a loss to the trust fund unless that loss was caused by his own actual fraud or negligence'.[61] The detailed guidance to that provision confirms the linking of that exemption with the default standard of care in trust administration, in providing that 'trustees are not liable for breach of trust when they have acted honestly and with reasonable care.'[62]

Another welcome sign that STEP has attempted to grapple with the difficult public policy issue over higher standards applying to professional trustees is found in the delineation between the exemptions applicable to different kinds of trustees. Thus, in the *STEP Standard Provisions*, STEP recommends the inclusion of a further provision as follows:

> '12.2 A Trustee shall not be liable for a loss to the Trust Fund unless that loss or damage was caused by his own actual fraud, provided that:
> 12.2.1 the Trustee acts as a lay trustee...; and
> 12.2.2 there is another Trustee who does not act as a lay Trustee.'

Again, the 'detailed guidance' to that draft clause relevantly provides that 'this clause... relieves a lay Trustee, even if negligent, unless guilty of fraud and as long as there is a professional Trustee... Thus a lay Trustee may, if they choose, broadly leave the Trust administration to a professional co-Trustee.'[63]

The failure to include such a clause may lead to serious financial exposure for a lay trustee who entrusts the administration to another trustee. But it is not all lay-trustee-sided, as there is a safeguard in the requirement for there to be at least one other trustee, who is not a lay trustee (i.e. a professional trustee). The potential uncertainty in delineating between lay and professional trustees is resolved by reference to the relevant trust legislation.[64] Thus, 'a person acts as a lay trustee if he – (a) is not a trust corporation, and (b) does not act in a professional capacity'.[65]

60. Kessler QC and Leon Sartin, *Drafting Trusts and Will Trusts: A Modern Approach* (Sweet & Maxwell, 2012), page 108

61. *STEP Standard Provisions*, 2nd edn, clause 4, available at www.step.org/step-standard-provisions

62. *Ibid* at 11

63. *Ibid* at 11

64. *Ibid* at 4 (clause 12.2.1 further provides that a 'lay trustee' falls 'within the meaning of s28 *Trustee Act 2000*')

65. TA 2000, s28(6)

For the purposes of the TA 2000, 'trust corporation' has the same meaning as that provided for in the *Trustee Act 1925*.[66] As such, '"Trust corporation" means the Public Trustee or a corporation either appointed by the court in any particular case to be a trustee, or entitled by rules made under subsection (3) of section four of the *Public Trustee Act 1906*, to act as custodian trustee...' and, therefore has a much narrower meaning than what might be thought is meant by a 'trust corporation'. Thus, the second limb (i.e. a trustee acting in a professional capacity) is more likely to apply in most cases. To alleviate the shortcomings of allowing professional trustees to be exempted for liability for a breach of trust, the Law Commission's rule of best practice requires 'professional trustees' (i.e. trustees who receive remuneration for administering a trust) to bring any clause purporting to limit liability to the attention of the settlor.[67]

Elsewhere, Kessler QC has, with Sartin, recommended against the drafting of broad exemption clauses and advised that a clause be included in trust instruments in the same terms as he proposes in the *STEP Standard Provisions*.[68] In doing so, they hope that 'there is still a marketplace in which some firms will undertake the duties of trustee on terms that they undertake to use reasonable care and accept responsibility if they fail to do so.'[69]

Further, they suggest that the adoption of narrow trustee exemption clauses may confer a competitive advantage over other professional trustees that routinely insist on exempting themselves for negligent trust administration.[70] Their plea is overly optimistic, as it is unlikely that such trustees would advertise their services in this way. A better approach would be to state the minimum standards of care that apply to trustees as a matter of law irrespective of trust drafting. This would not expose trustees unduly as there remain internal mechanisms in trusts law that protect diligent trustees from liability, the main three of which are considered below.

Advice

First, trustees can and ought to seek advice in relation to a broad range of administrative and dispositive matters in order to discharge their duty of care. To make that clear, a provision may be drafted into a trust in the terms provided for in the *STEP Standard Provisions*, that:[71]

> 'A Trustee shall not be liable for acting in accordance with the advice of counsel, of at least five years' standing, with respect to the Trust. The Trustees may in particular conduct legal proceedings in accordance with such advice without obtaining a court order. A Trustee may recover from the Trust Fund any expenses where he has acted in accordance with such advice.'

However, according to the *STEP Standard Provisions*, the exoneration of trustees by means of obtaining advice does not apply in certain, entirely sensible circumstances, including where the trustee knows or suspects that counsel's advice was incomplete, court proceedings are pending on the matter or where the trustee either has a personal interest in, or has committed a breach of trust relating to, the subject matter of the advice.[72]

A somewhat odd aspect of the UK Supreme Court's decision in *Futter* v *HMRC*; *Pitt* v *HMRC* was that the court upheld the view that 'if the trustee has in accordance with his duty identified the relevant considerations and used all proper care and diligence in obtaining the relevant information and advice relating to those considerations, the trustee can be in no breach of duty and its decision cannot be impugned merely because in fact that information turns out to be partial or incorrect' as

66. TA 2000, s39(1)
67. Law Commission, *Trustee Exemption Clauses* (No.301, 30 July 2006), paragraph 7.1; STEP, *Guidance Notes: STEP Practice Rule to Trustee Exemption Clauses*, available at www.step.org/sites/default/files/Comms/STEPGuidanceNotes.pdf. See also Kessler QC and Sartin, *Drafting Trusts and Will Trusts: A Modern Approach* (Sweet & Maxwell, 2012), pages 102–3
68. Kessler QC and Sartin, *Drafting Trusts and Will Trusts: A Modern Approach* (Sweet & Maxwell, 2012), 109 ('a Trustee shall not be liable for a loss to the Trust Fund unless that loss was caused by his own actual fraud or negligence')
69. *Ibid* at 106
70. *Ibid*
71. *STEP Standard Provisions*, 2nd edn, clause 12.3
72. *STEP Standard Provisions*, 2nd edn, clause 12.4 and 11

a correct statement of the law and that 'apart from exceptional circumstances... only breach of fiduciary duty justifies judicial intervention.'[73] Given that represents a modern view, it is worthwhile addressing the point in trust drafting, as it remains possible for a trustee to be liable for a breach of trust despite obtaining professional advice.[74]

Beneficiaries

Second, trustees may seek the concurrence of beneficiaries in order to relieve or indemnify themselves from liability for a breach of trust.[75] In some cases, such as in trusts of land to which the *Trusts of Land and Appointment of Trustees Act 1996* (TLATA) applies, a statutory duty may be imposed on trustees to consult the beneficiaries with respect to 'the exercise of any function relating to the land subject to the trust' and to 'give effect to the wishes of those beneficiaries' accordingly.[76] Like the duty of care in the TA 2000, the duty to consult and obey the wishes of the beneficiaries in the TLATA is not mandatory, but excludable by the terms of the trust.[77]

The trustee's duty to consult beneficiaries is somewhat vague and empty in any event – it is also potentially problematic in that it may place the trustee in a difficult position where the particular duty to consult and obey the beneficiaries conflicts with the general duty to perform the trust.[78] In such cases, the general duty to perform the trust ought to prevail.[79] For these reasons, any duty to consult beneficiaries is expressly excluded by the trust instrument in favour of an 'absolute discretion clause'.[80] Here, the concern is not with a general duty to consult beneficiaries, which does not arise except from the terms of the trust or some statutory provision in any event,[81] but with the ability of the trustee to minimise the risks associated with trust administration by avoiding liability and securing indemnification by means of such consultation.

As such, trustees may be able to avoid liability for a breach of trust where the trustee has sought and obtained the concurrence of the beneficiary as to the proposed course of action, irrespective of whether the beneficiary is actually aware that the relevant conduct would constitute a breach of trust.[82] Of course, proper disclosure must be made by a trustee and fully informed consent must be obtained from the beneficiaries. Once the trustee has done so, it will be difficult for a beneficiary to make a successful claim for personal liability for breach of trust arising out of a course of action in which the beneficiary consented, with virtually identical provisions in England and Wales, Guernsey and Jersey codifying this position.[83]

Court

Third, trustees are in the enviable position of being able to approach the court for advice and directions as to how to perform their duties and will obtain a prospective indemnity if they have made full disclosure of all material matters pertaining to that advice and act accordingly.[84] That is a better working model for trust administration, as well as the coherent operation of trust law, than the inclusion of broadly drafted trustee exemption clauses in trust instruments.

In addition to the ability of trustees to be able to approach the court for advice and directions concerning any matter of doubt arising in the administration of the trust, there is also a statutory power for the court to relieve a trustee from

73. *Pitt* v *HMRC*; *Futter* v *Futter* [2013] 2 AC 108, 131, 139–141 per Lord Walker, approving *Abacus Trust Co (Isle of Man)* v *Barr* [2003] Ch 409, 23 per Lightman J and 178 and *Pitt* v *Holt; Futter* v *Futter* (2012) Ch 132, 178 per Lloyd LJ
74. *Pitt* v *HMRC; Futter* v *Futter* [2013] 2 AC 108, 140 per Lord Walker. See also *Stott* v *Milne* (1884) 25 Ch D 710, 714 per Lord Selborne LC, approved in *Re Beddoe* [1893] 1 Ch 547, 558 per Lindley LJ; *Re Dive* [1909] 1 Ch 328, 342 per Warrington J
75. *Trusts (Guernsey) Law 2007*, s40; Trusts (Jersey) Law 1984, s30(6) and (7)
76. *Trusts of Land and Appointment of Trustees Act 1996* (UK), s11(1)
77. *Trusts of Land and Appointment of Trustees Act 1996* (UK), s11(2), (3) and (4)
78. E.g. a trustee of land may owe a duty to consult with, and obey the wishes of, the life tenants, but the wishes of the life tenants may commonly conflict with those of the remainderman, who may not yet be born or cannot be consulted for some other reason
79. E.g. *Trusts of Land and Appointment of Trustees Act 1996* (UK), s11(1)(b)
80. *STEP Standard Provisions*, 2nd edn, clause 19. See also Kessler QC and Sartin, *Drafting Trusts and Will Trusts*, 11th edn (2012), 142
81. *X* v *A* [2000] 1 All ER 490, 496 per Arden J
82. *Re Pauling's Settlement Trusts*, *Younghusband* v *Coutts & Co* [1961] 3 All ER 713, 729–30 per Wilberforce J
83. *Trusts (Guernsey) Law 2007*, s56; *Trusts (Jersey) Law 1984*, s46; *Trustee Act 1925* (UK), s 62(1)
84. In England and Wales, see *Administration of Justice Act 1985*, s48; *Civil Procedure Rules 1998*, Part 64, Practice Direction 64A and 64B. In Guernsey, see *Trusts (Guernsey) Law 2007*, sections 68 and 69. In Jersey, see *Trusts (Jersey) Law 1984*, s51

personal liability for a breach of trust where the trustee has acted honestly and reasonably, and ought fairly to be excused for the breach of trust and for omitting to obtain the directions of the court.[85]

Plainly, it is more desirable for trustees to seek advice and directions from the court before undertaking any legally uncertain course of conduct in the administration of a trust – indeed, the statutory provision conferring power to relieve trustees from personal liability refers not only to a trustee being excused from the breach of trust, but also to failing to obtain directions from the court. Given the bias toward proactivity by trustees, and prospective directions being given by the court for trustees to obtain indemnification, the statutory power is often seen by trust practitioners as a 'false friend' of trustees that cannot be relied upon to justify past conduct *ex post facto*, but only as a defence of last resort against allegations of maladministration.[86]

CONCLUSIONS

The conclusions drawn in this article are threefold.

First, the peculiar obligation to act *en bon père de famille* in Guernsey trust law has effectively been translated in the *Spread* litigation and equated with the English and Welsh, and Jersey duties of care. Although that approach fails to give any weight to Guernsey legal heritage, it does have the benefit of certainty and cohesion. One key difference, however, is that the Guernsey and Jersey trusts laws adopt the duty of care as mandatory rules and prohibit the exemption of a trustee's liability for fraud, wilful default or gross negligence, rather than leaving those matters (save fraud) as matters of trust drafting, which remains the case in English and Welsh law. The clear statutory position taken in the Channel Islands is to be preferred, as it promotes prudent trust administration.

Second, leading precedent texts and drafting manuals attempt to fill gaps left in onshore trust administration by recommending against the inclusion of broad trustee exemption clauses, and attempt to approximate onshore trust administration with the minimum standard expected of offshore trustees as a matter of law. Again, the better approach would be for a clear legislative provision to provide for the minimum standards that apply to trust administration irrespective of trust drafting.

Third, there is no need for broad exemptions of liability for trustees who conduct themselves with reasonable diligence, as existing mechanisms within trusts law serve to protect prudent trustees, especially by indemnifying trustees by the taking of advice, concurrence with beneficiaries and directions from the court. Aside from the duty of care, which itself can be excluded by the terms of a trust, the mandatory rules of English and Welsh trust law are too trustee-biased when compared to Guernsey and Jersey, both of which have struck a more appropriate balance between beneficiaries and trustees and furthered the public policy incentive of promoting prudent trust administration.

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85. *Trusts (Guernsey) Law 2007*, s55; *Trusts (Jersey) Law 1984*, s45; *Trustee Act 1925* (UK), s61

86. See Waterworth, *A Practitioner's Guide to Drafting Trusts*, 2nd edn (2007), 115. See also, Thurston, *A Practitioner's Guide to Trusts*, 9th edn (2011), 151 (questioning 'what is reasonable conduct in this context?'); Kessler QC and Sartin, *Drafting Trusts and Will Trusts*, 11th edn (2012), 108–09 (recommending additional drafting in the trust instrument to properly protect trustees from personal liability)