

Investec v Glenalla: Privy Council defines the limits of a trustee's liability and the rights of creditors

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The Judicial Board of the Privy Council released its important judgment in *Investec Trust (Guernsey) Ltd & Anr. v Glenalla Properties Ltd. & Ors* [2018] UKPC 7 on Monday (23 April), sitting on appeal from the Court of Appeal of Guernsey. The case concerned claims by BVI companies as creditors under loan agreements entered into by trustees of a Jersey law trust.

The Board had to consider the effect of Article 32(1) of the Trusts (Jersey) Law 1984 (as amended) (the **TJL**) which provides as follows:

"Where a trustee is a party to any transaction or matter affecting the trust –

- if the other party knows that the trustee is acting as trustee, any claim by the other party shall be against the trustee as trustee and shall extend only to the trust property;
- if the other party does not know that the trustee is acting as trustee, any claim by the other party may be made against the trustee personally (though, without prejudice to his or her personal liability, the trustee shall have a right of recourse to the trust property by way of indemnity).

The majority of the Board (Lords Mance and Briggs dissenting) confirmed that the effect of Article 32(1) TJL is to limit the liability of a trustee to third parties to the trust assets and safeguard a trustee's personal assets from claims where the other party to a transaction knows that the trustee is acting in the capacity of trustee.

It does not impose a monetary cap on third party claims, however; nor does it confer a right on creditors to make direct claims against trust property. The majority were willing to hold that Article 32(1) TJL would have this effect irrespective of the proper law of the transaction (e.g. governing law of the contract) or of the law of the forum in which the litigation was taking place.

Third party creditors are therefore limited to a claim against the person of the trustee which can then only be executed against the trust assets indirectly. This execution is achieved by way of subrogation to the trustee's equitable lien over the trust assets, which survives any retirement of that trustee from office and vesting of assets in the new trustee. The equitable lien, based on the trustee's rights of indemnity and reimbursement from trust assets, only applies where the trustee has incurred a liability "reasonably", in accordance with the terms of Article 26(2) TJL.

The Board clarified (Lord Mance again dissenting on this point) that whether or not a liability has been reasonably incurred is to be judged at the date on which it was incurred and not with the benefit of hindsight at the point in time when a trustee (or creditor by

way of subrogation) seeks to rely on their right of reimbursement. Allegations of breach of trust brought by beneficiaries relating to an unreasonable continuation of a liability previously incurred were therefore irrelevant to the analysis.

Personal exposure of trustees in litigation

As a note of caution for any trustees who may become involved in litigation, the Privy Council determined that Article 32(1) TJJ did not serve to limit the liability of a trustee to the trust assets in relation to the costs of legal proceedings. Such a limitation would otherwise restrict the Court's wide discretion to award costs under Article 53 TJJ. Furthermore, a Beddoe-type order blessing the trustee's participation in proceedings would not of itself relieve a trustee from the consequences of its unreasonable behaviour in the conduct of the litigation, leaving the way open for future courts to award indemnity costs against a trustee personally in appropriate circumstances.

A legal step too far?

In a powerful dissenting judgment, Lord Mance criticised the interpretation of Article 32(1) TJJ favoured by the majority of the Board, observing that it would mean that trustees would have a separate, quasi-corporate status or capacity when contracting with third parties, despite the fact that a trust is not a separate legal entity. In circumstances where there was no direct right of recourse to trust assets for a creditor, he considered that there was an "evident unfairness" in leaving a creditor to rely on a claim through the trustee which would be defeated where a trustee acted in breach of trust.

While it is right that this is the inevitable consequence of the majority decision, it is difficult to see how this is commercially unfair given that any third party has the opportunity to evaluate the risks and rewards of entering into a transaction with a trustee acting openly in that capacity. It is no different in substance to the scenario which Lord Mance found acceptable whereby a trustee entering into a contract can limit its liability simply by stating that it contracts in its capacity "as trustee only".

In the commercial world there is also nothing to prevent mitigation of such risks by taking security over trust assets, for example, as any arms-length lender would expect to do. The problem in this case only arose because the trustee had accounted for flows of money between companies which were all trust assets as unsecured, interest-free loans. Following the financial crash and collapse of Kaupthing Bank which had acted as external lender to the BVI companies, those companies had gone into liquidation and the liquidators had called in the intra-group loans.

Takeaway points

Trustees of Jersey law trusts should be comforted by the decision for a number of reasons. Provided they deal openly with third parties in their capacity as trustees, they will not attract any personal liability to creditors.

Equally, if they indemnify or reimburse themselves out of the trust assets in respect of a liability that was reasonable at the time it was incurred, they will not be personally liable to their beneficiaries for doing so even if with hindsight there have been negative consequences resulting from the liability. However, caution will still be required where allegations of breach of trust are made in relation to entering into the particular transaction concerned as there may be a duty to account for losses arising.

The Board has confirmed that the trustee's rights of indemnity and lien extend to and continue to subsist in trust assets in the hands of successor trustees. These rights reinforce the typical contractual chain indemnities required from successors.

Finally, trustees engaging in litigation should note that even if they obtain Beddoe-type relief which should mean that the decision to participate in the proceedings is not open to an allegation of breach of trust, their conduct in the litigation must be reasonable

or there will be a risk of a personal costs order being made against them, including on the indemnity basis. On a practical note, if there are difficult tactical decisions to be made along the way such as whether to bring or defend interlocutory applications, then the prudent course will be to reconvene the Beddoe court and take urgent directions.

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