Untangling the Webb: An offshore perspective on the Privy Council case of Webb v Webb

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In a recent decision the Privy Council has had the opportunity to consider the circumstances under which a trust may be declared invalid due to the reservation of powers by its settlor.

In Webb v Webb the Court determined that a trust was invalid because "*the trust deeds failed to record an effective alienation by [the Settlor] of any of the trust property*".

In essence, the Court held that the cumulative effect of the powers the Settlor reserved to himself under the trust deed were that "*in equity and in all of the circumstances of this case, he can be regarded as having had rights in the trust assets which were indistinguishable from ownership*".

Although this Privy Council decision relates to the Cook Islands, the principles set out will likely apply more widely to trusts in other offshore jurisdictions, such as BVI, Cayman and Guernsey.

The facts

Mr and Mrs Webb were married in December 2005. Shortly after their marriage Mr Webb settled a family trust (the Arorangi Trust). The beneficiaries were Mr Webb and Mr Webb's son from a previous marriage. The Arorangi Trust assets came to include: land in the Cook Islands; a leasehold interest in a property in the Cook Islands; and other assets in the Cook Islands jurisdiction.

Under the trust deed Mr Webb reserved a number of appointments and powers to himself. The ones of particular interest to the Privy Council included provisions which:

- Appointed himself as sole trustee; and pursuant to the trust deed, could exercise all powers and discretions conferred by the trust deed notwithstanding they may conflict with his duties as trustee to the beneficiaries.
- Appointed himself as consultant; whose role it was to assist the trustee in the administration and management of the trust and to advise the trustee on all matter relating to the trust's investments; at his absolute discretion to remove the trustee and appoint another; request with any beneficiary the early vesting of the trust property; and consent to any variation proposed by the trustee.
- As settlor reserved to himself the power to nominate himself as sole beneficiary in place of the existing beneficiaries.

In deciding whether the Arorangi Trust was valid the Privy Council considered that the question of validity could be approached in two ways, either:

- that the powers reserved to Mr Webb were so extensive that Mr Webb can be said never to have disposed of any of the property purportedly settled on or acquired by the trust, and in connection with that, whether the trusts lacked the irreducible core of obligations owed by trustees to the beneficiaries and enforceable by them which is fundamental to the concept of a trust; or

- that the powers reserved were so extensive he can be regarded as having rights which were tantamount to ownership.

The Privy Council agreed with the Court of Appeal that it made no difference to the outcome which of those analytical paths was taken.

It adopted the same path as the Court of Appeal and likewise agreed that, taken in the round, "*the bundle of rights which* [Mr Webb] *retained is indistinguishable from ownership*" and that the Court of Appeal was "*plainly entitled to find as it did that the trust deeds failed to record an effective alienation by Mr Webb of any of the trust property*".

O, what a tangled Webb we weave...

Since this judgment has been handed down, we have heard commentators opine that this is likely to be disregarded as a matter of trust jurisprudence on the basis that it was a judgment handed down in the context of matrimonial proceedings.

However, the Privy Council did not take the opportunity to caveat its determination by adding "for the purposes of the matrimonial law…" or other commentary to that effect. Moreover, by looking at the cases cited before the Privy Council, and the lower courts, they are cases all too familiar to trust practitioners dealing with fundamental aspects of trust principles, such as *Armitage v Nurse* (re: irreducible core of trust obligations); *Schmidt v Rosewood* (court's supervisory powers over a trust); *McPhail v Doulton* (certainly of objects). It is therefore far from clear that this judgment is only of relevance to those who practice exclusively in the Family Courts.

In fact, given the circumstances, this is of real interest to those who practice in an offshore jurisdiction.

Firstly, it is opining on common law trust law principles, based on English law precedent with which offshore common law jurisdictions tend to share principles.

Secondly, the basis for determination of the trust invalidity was the extent of reserved powers enjoyed by the settlor in whichever role; something directly enshrined in statute in a number of offshore jurisdictions, including Guernsey, Jersey, BVI and Cayman.

A previous high-profile case which attempted to wrestle with the effect of reserving powers that could be exercised by a settlor over a trust was the English High Court's determination in *Pugachev*.

In *Pugachev*, the High Court considered whether trusts set up by Mr Pugachev were "illusory". In doing so Birss J considered that when a court considers the extent to which a person has divested themselves of the assets purportedly settled into trust, the court is entitled to take as a whole the powers that have been reserved to them under the trust deed. Put simply: "*the analysis is concerned with what the effect of the deed truly is*". In undertaking this analysis, Briss J found that the trust deeds were not effective at divesting Mr Pugachev of his beneficial interests and so the assets were held on bare trust for Mr Pugachev and so available to his creditors.

Since the English High Court's determination in *Pugachev* there has been a lively debate as to whether its line of reasoning would be replicated in offshore proceedings, particularly in jurisdictions where reserved powers are enshrined in law. By way of example, in Guernsey at section 15 the Trusts (Guernsey) Law, 2007 expressly states:

"*A trust is not invalidated by the reservation or grant by the settlor (whether to the settlor or to any other person)* ***of all or any*** *of the following powers or interests…*" (emphasis added)

The Trusts Law goes on to name a range of powers that fall within this including: powers to revoke; vary or amend the terms of the trust; powers to advance; appoint; pay or apply the income or capital of the trust; investment manager-type powers; power to remove; power to give directions; change the law of the trust; and a power to restrict the function of a trustee by requiring it only be exercised with permission. In short, everything that the Privy Council and the High Court have relied on to determine that a person has failed to divest themselves of their assets.

The general consensus has been that the offshore courts are unlikely to follow *Pugachev* and find a trust is illusory, where not only are the reserved powers enshrined in statute, but there is an express statement to the effect that ***all*** may be reserved.

However, as a result of historical imperative, the Royal Court of Guernsey, in common with other offshore jurisdictions, often looks to England and other common law jurisdictions as those trust concepts have broadly grown from the same roots.

Now, whilst a single decision may prove an aberration, twice may start to look like a firmer rule, particularly where it is the Privy Council making such findings.

It leaves our offshore jurisdictions with an interesting conundrum as to the development of our trust laws.

The alienation of property is a fundamental tenet of trust law, without which a trust cannot be created. It is also a settled proposition that under English common law settlors may reserve to themselves certain powers within the trust deed. The development of English (and Cook Island) common law would indicate that whilst the ability to reserve powers does not, of itself, automatically invalidate a trust, where the settlor has reserved so much they cannot truly be said to have parted with the property, the trust would be invalid from the outset.

And so where does the offshore world choose to spin its web?

Should we argue that, as a result of the express reserved powers legislation, we should deviate from the developments in *Pugachev* and *Webb*? That as a result an express trust, such as that in *Webb*, would be upheld on the basis it is provided for by statute? To take this to its ultimate conclusion may result in some absurd decisions. Settlors could essentially draft trust instruments under which the trustee has as much control over the trust as a fly ensnared on a web of the settlor's design – who ceases to be able to independently act or take any substantive step in respect of the trust assets. To take it to its extreme could call into question the basis of trust foundations.

The alternative is equally unenticing for the trust world. The attractiveness of a trust is often that the settlor is able to still exercise some degree of influence with the trustees. Should the offshore trust world accept that the use of reserved powers is likely to result in an invalidity of the trust it would surely need to consider alternative mechanisms for settlor involvement - as well as wrestling with the potential implications of finding the assets they have been administered pursuant to reserved power trust deeds are actually held on bare trust for the settlor.

As ever, the outcome is likely to fall somewhere in between. The Trust Law offers statutory comfort of the common law position, namely that reserving powers in and of themselves will not be sufficient to invalidate the trust simply by their presence. But they won't provide a settlor with carte blanche to declare a trust whilst for all intents and purposes maintaining benefit and control over it. The courts can still

consider whether the combined effect of the reserved powers in the round mean that a settlor has truly parted with the assets intended to be settled into trust.

It has always been sensible practice when setting up trusts to consider the purposes for which it is being created, be it for generational wealth planning, wealth structuring or asset protection. However, as with anything, the more powers that settlors choose to reserve to themselves, the less effective the benefits or protections offered by a trust are likely to be. Now, there is another reason why settlors should hesitate before placing themselves in the centre of the web[b]...

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