UPDATE

The P Trust and the R Trust

Update prepared by Jonathan Speck (Partner, Jersey)

Mourant Ozannes appeared recently *In the matter of the P Trust and the R Trust* [2015] JRC 196. The case demonstrates the power of the Royal Court to declare invalid the exercise of powers by fiduciaries.

The case involved a family for whose benefit two Jersey law governed discretionary trusts had been established by the father, a successful businessman. The father was also the protector of the trusts from their inception until the events which gave rise to these proceedings.

During the course of the hearing the Royal Court had to consider the duties of a person exercising a fiduciary power. Without purporting to assert an exhaustive list of such duties, it was held that a fiduciary exercising its powers shall:

- act in good faith and in the interests of the beneficiaries as a whole;
- reach a decision open to a reasonable power holder;
- take into account relevant matters and only those matters; and
- not act for an ulterior purpose.

When considering the exercise of fiduciary powers a distinction can be made between formal validity (ie the power was exercised by the correct power holder in accordance with the formal requirements of the trust deed) and essential validity (ie the power was exercised in breach of one or more of the duties set out above). The latter is a qualitative test which must also be met for the exercise of power to withstand challenge.

The purported appointment and removal of trustees

In this case both trusts contained powers to appoint and remove trustees which were vested in the protector. In 2014 the father, as protector, purported to exercise these powers and appoint as trustee an ostensibly thinly capitalised, unregulated, opaque private trust company in another jurisdiction to which none of the family had any connection. In the circumstances the trustees rightly became concerned that the appointments may not be in the best interests of the beneficiaries and they made various attempts to procure further information about the proposed new trustee and its qualifications and experience. Ultimately these attempts were unsuccessful and the trustees' concerns were exacerbated. Certain beneficiaries shared similar concerns and an application was made to the Royal Court for directions as to what the trustees should do next.

Evidence was heard of efforts made by the trustees to procure information about the purported new trustees, the unsatisfactory answers received and the flawed reasoning behind the father's decision to change trustees in the first place. The Royal Court held that the father, as protector:

- failed to take into account relevant matters, such as the expertise, experience and financial standing of the proposed new trustee of these substantial trusts; and
- took into account irrelevant matters, such as a suggestion that Jersey was not a 'whitelisted' jurisdiction

and therefore reached a decision at which no reasonable fiduciary could have arrived. It was therefore declared that the appointments of new trustees in relation to both trusts were invalid. All of the parties to the proceedings were content with this ruling.

The purported appointment and retirement of protectors

The second issue was more complex. A few months after the purported appointment and removal of trustees the father had retired and his sons were appointed as protectors of both trusts in his place. These appointments were made in accordance with the formalities prescribed by the relevant powers in the trusts. Crucially the daughter was not involved in the process and on learning of the appointments she issued a summons seeking a declaration that they be declared invalid or, in the alternative, the sons be removed as protectors.

In determining this issue, the Royal Court was required to review the history of the trusts and the events leading up to the appointments in question. Evidence was heard of difficulties in the relationship between the father and his daughter culminating in litigation being played out in a number of jurisdictions. This continuing litigation relates to companies controlled by the father and involves serious allegations of impropriety by the daughter against her father and brothers. Against this complex backdrop the daughter claimed that her brothers could not fulfil properly the functions of the office of protector because:

- they had a conflict of interest arising from the litigation;
- they were not sufficiently independent from the father; and
- the breakdown in relations would make it impossible for them to be seen to be acting fairly.

On the other hand, it was argued by the father than the appointments were appropriate not least because:

- his sons were highly qualified, experienced and successful professionals;
- all but one of the beneficiaries (ie the daughter) supported their appointments as protector; and
- as family members, the sons would provide to the trustees valued insight and perspective in the administration of the trusts.

Furthermore, the sons argued that they were merely peripheral participants in the litigation and the underlying conflict was actually only between the father and daughter. The sons' position was that they were essentially neutral and would remain so in fulfilling the functions of the office of protector.

The Royal Court applied the same qualitative test that it applied when determining the issue of the purported appointment of the new trustees and generally accepted the daughter's evidence in relation to the conflict of interest, hostility and lack of independence. In such circumstances it was held to be a breach of duty and irrational for the father as protector to appoint the sons as protectors of the trusts of which the daughter (and now her child) were beneficiaries.

Conclusion

This case is an excellent example of the distinction between formal and essential validity in the exercise of fiduciary powers - whether they be to appoint trustees, add beneficiaries, make distributions invest or any other type of power. A fiduciary may exercise a power under a trust in a manner which complies squarely with the formalities prescribed in the trust instrument and is therefore formally valid. However, the exercise of power could be impugned by a beneficiary or other person with *locus standi* if evidence can be brought that the power holder did not act reasonably, in good faith and take into account only relevant matters.

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