

Privy Council clarifies the proper purpose rule – *Grand View Private Trust Co Ltd v Wong & Ors*

UPDATE

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The Privy Council has provided welcome clarification to trustees in relation to the equitable constraints on the exercise of their powers under broadly drafted trust instruments.

In *Grand View Private Trust Co Ltd and another v Wong and others* [2022] UKPC 47, the Judicial Committee of the Privy Council held that the exercise of a power by a trustee to add and exclude beneficiaries was void on the basis that it was inconsistent with the purpose for which that power was conferred. In this update, we look at the reasoning employed by the Privy Council in reaching this conclusion and consider the wider significance of the judgment to trust administrators in the British Virgin Islands.

Background

The *Grand View* case concerns two discretionary Bermuda law governed trusts settled simultaneously in 2001, known as the Global Resource Trust and the Wang Family Trust. Both trusts held valuable shareholdings in companies known as the Formosa Plastics Group, one of the largest business conglomerates in Taiwan.

The class of beneficiaries of the Global Resource Trust were the children and remoter issue of the settlors. The Wang Family Trust was something of a misnomer, in that it was a purpose trust conferring no benefit on members of the Wang family. Both trusts included a broadly drafted power to add or exclude beneficiaries or classes of beneficiaries.

In 2005, the settlors decided that there was no longer any need for a private trust for the benefit of their children, as they were already adequately provided for in the settlors' wills. The trustee of the Global Resource Trust accordingly exercised its powers of addition and exclusion to exclude all family members from the beneficial class of the Trust, add the trustee of the Wang Family Trust as the sole beneficiary, and appoint all of the Trust's assets to the trustee of the Wang Family Trust.

This decision was challenged by a number of the Wang family members in 2018. At first instance, the Supreme Court of Bermuda decided *inter alia* that the trustee of the Global Resource Trust invalidly exercised its powers in replacing the family members as beneficiaries with the trustee of the Wang Family Trust and declared the trustee's acts in those respects to be void and of no effect. An appeal against this decision was allowed by the Court of Appeal of Bermuda, who also granted leave to appeal to the Judicial Committee of the Privy Council (the **Board**). Following a three-day remote hearing in March 2022, the Board handed down its judgment on 8 December 2022.

The Decision

The Board held that the power of addition and exclusion was a fiduciary power and therefore subject to duties and restrictions imposed by equity. The Board agreed with the Court of Appeal that the following questions were relevant when considering the validity of the exercise of a power by a trustee:

- whether the way in which the power has been exercised is in accordance with the express or implied terms of the power (the 'scope of power rule');

- whether the trustee has given adequate deliberations as to whether and how it should exercise the power; and
- whether the use of the power by the trustee, although within its scope, was for an improper purpose ie a purpose other than the one for which it was conferred (the 'proper purpose rule').

The Board rejected an argument from the Wang family members that the trustee lacked the necessary power to exclude them and add the trustee of the Wang Family Trust as the sole beneficiary. The decision taken by the trustee of the Global Resource Trust fell within the scope of the power as drafted in the trust deed. The key issue in the appeal was whether the use of the power was consistent with its proper purpose.

The Board considered the trust instrument, and the circumstances surrounding its creation, and concluded that the purpose of the Global Resource Trust was to benefit the family members of the settlors and the trustee's decision to replace the family members as beneficiaries with the trustee of the Wang Family Trust was inconsistent with the purpose for which the power of addition and exclusion was conferred.

Takeaways

There are a number of takeaways from the Privy Council's judgment for BVI trust administrators:

- Identifying the proper purpose of a power involves an inquiry into the wording of the trust instrument and the circumstances in which it was created. Letters of wishes that post-date the trust deed are not relevant to that inquiry. While trustees can legitimately have regard to wishes later expressed by the settlor as to how the trustees should exercise their powers, such wishes are not admissible in determining the purpose of those powers.
- The Board agreed with the Court of Appeal that there is no absolute 'substratum' principle that precludes a trustee from exercising its powers in a manner which will change the very fabric of the trust. Courts in other offshore jurisdictions such as Jersey and the Cayman Islands have already reached similar conclusions.¹ The correct approach is to determine the proper purpose of the power, although there is a strong presumption that a power of amendment is not to be used to alter the purpose of the trust.
- The interests of the beneficiaries are relevant but not determinative factors when identifying the proper purpose of a power of exclusion and addition. The task is to discern the intended purpose of the power of exclusion and addition in the context of a particular trust – this is a more nuanced inquiry than merely assessing what is in the best interests of the beneficiaries. On the facts the Board found that the clear purpose of the Global Resource Trust was to benefit the Wang family members and that purpose had a decisive effect on identifying the purpose of the power of addition and exclusion. However, the Board rejected the notion that there is an overriding principle or rule that the exercise of a power by a trustee must be in the interests of some or all of the beneficiaries.
- HNWIs should be careful not to 'box themselves in' when setting up succession planning structures. Futureproofing a trust requires more than just broadly worded drafting. The original structures set up in 2001 did not provide sufficient flexibility to merge the two trusts in 2005 when the settlors decided to pass on their wealth to their children via inheritance as opposed to a trust. The Board noted that that the wording of the trust deed did not suggest that the interests of the family members were intended to terminate if the trustee took the view that the trust in their favour was no longer needed to meet the settlor's estate planning objectives. Amending a will is usually a straightforward task; making fundamental changes to an irrevocable discretionary family trust is often more difficult.
- Taking a momentous decision without first obtaining a blessing from the court is a dangerous business. A well-advised trustee will usually seek the court's blessing before taking a momentous decision, thereby protecting itself from complaints from the beneficiaries in the future. The trustee of the Global Resource Trust opted not to seek a blessing from the court, which left the door open to the family members to challenge the decision in 2018, some 13 years after it was taken. It will inevitably be disappointing to a trustee if the court declines to bless a proposed course of action; but the reputational, fiscal and financial consequences of a trustee decision being declared void years after it's been implemented is likely to be far more wide reaching.

¹ See *Representation of Rysaffe Fiduciaries Sarl* [2021] JRC 230 (Jersey) and *In the Matter of the Poulton Family Trust* (unreported, FSD 0121 of 2016 (IKJ), 18 February 2022) (Cayman Islands).

Conclusion

The *Grand View* decision confirms the importance of the proper purpose rule and illustrates its teeth. The judgment is a stark reminder to trustees of the inherent limits on the exercise of their powers, notwithstanding the wording of the trust instrument. The upshot is that trustees are more constricted in how they exercise their powers, not least because the purpose of a particular power may not always be easy to discern. However, the Privy Council's judgment provides welcome clarification and guidance as to how the purpose of a particular power can be identified, which should assist trustees with understanding the application of the proper purpose rule whilst giving comfort to beneficiaries whose interests are better protected.

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