Alert

Changing with the Times: The Cayman Islands' Trusts Law gets a Revamp

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Legislative amendments to the Cayman Islands' *Trusts Law* take effect from 14 June 2019. While the reforms do not represent a drastic overhaul of the Trusts Law, they introduce welcome improvements to ensure the Cayman Islands remains a leading offshore jurisdiction for the establishment, administration, and maintenance of trusts.

The legislative amendments[1] are the latest in a series of revisions to the Trusts Law (2018 Revision) (the "Trusts Law"), which is the main source of legislation concerning trusts in the Cayman Islands. The reforms take effect from 14 June 2019 and, as part of a continual process of fine-tuning the Trusts Law, effect the following key changes:

1. **codifying the *"Hastings-Bass"* principle**: providing a clear statutory framework to apply for relief where the trustee (or some other fiduciary) has made a mistake in the exercise of their powers;
2. **extra-judicial variation of trusts**: making it easier for the Grand Court to approve a variation to a trust on behalf of minor and unborn beneficiaries;
3. **compromise trust litigation**: making it easier for the Grand Court to approve a compromise to a trust dispute on behalf of minor and unborn beneficiaries;
4. **foreign element provisions**: extending the "firewall" or foreign element provisions which protect against a foreign law applying to a Cayman trust or foundation company; and
5. **trust corporations**: widening the definition of a "trust corporation" to include licensed trust companies' controlled subsidiaries and thereby widening the scope for such trustees to retire.

1 *Cayman Islands Trusts (Amendment) Law 2019*

Hastings-Bass: setting aside mistaken decisions

Where a trustee makes a mistake in the exercise of their powers, it stands to reason that innocent beneficiaries should have relief from the consequences of that mistake. Traditionally, common law courts had recognised wide powers in this regard, relying on the rule in "*Re Hastings-Bass*[2]", which concerns the validity or otherwise of a trustee's exercise of their powers in reaching a fiduciary decision.

In reliance on this principle, common law courts had held that trustees' exercise of their power was invalid not only where the power was exercised in bad faith or excessively, but also where the trustees, in exercising their powers, had taken into account irrelevant matters or failed to take into account relevant matters.

However, a recent line of authority (originating from a UK Supreme Court decision[3]) had severely restricted the Court's ability to correct such mistakes. If the UK authority was followed (and it had found some favour in the Cayman Islands[4]), it would require the applicant to prove a breach of fiduciary duty in order for a court to set aside a mistaken decision. This had the potential to set an unreasonably high threshold and deny relief in circumstances where the trustee had made their decision based on incorrect professional advice. As most exercises of dispositive powers by trustees in the Cayman Islands are based on professional advice, this could make it impossible for a court to exercise its corrective jurisdiction.

2 [1975] Ch 25
3 *Pitt -v- Holt and Futter -v- Futter [2011] EWCA Civ 197*

Fortunately, the reforms insert a new Section 64A in the Trusts Law to provide a statutory framework for the setting aside of mistaken decisions by trustees and other fiduciaries. Importantly, as a result of subsection 64A(4), it is not necessary to prove that the person who exercised the power (or their advisor) acted in breach of trust or duty. Rather, the focus (as in *Hastings-Bass*) is on:

a) whether in exercising their powers, the decision maker took into account irrelevant matters or failed to take into account relevant matters; and

b) but for that failure, the power would not have been exercised or would have been exercised in a different way or on a different occasion.

The Grand Court is empowered to set aside such "mistaken" decisions with the relevant exercise of power treated "*as never having occurred*". The Grand Court can also make such consequential orders as it considers necessary. However, protection is of course granted to ensure that any orders do not prejudice a *bona fide* purchaser for value of any trust property who did not have notice of the circumstances behind the mistaken exercise of power. As such, innocent third parties should not suffer as a result of any orders.

A range of interested parties including the trustee (or some other "holder" of the fiduciary power such as a delegate), a beneficiary of the trust, the enforcer of a purpose trust, or the Cayman Attorney General (where the trust is a charity), can make applications under Section 64A for a decision to be set aside. The Grand Court can also grant leave to allow any other person to apply.

Judicial variation of trusts

Prior to the reforms, where the Grand Court was asked to approve a variation of an established trust on behalf of any person (such as a minor or unborn beneficiary), it could only do so where it was satisfied that such variation was *"for the benefit of that person*".[5] This substantially restricted the type of variations that could be approved by the Court as, although a variation may be sensible, it could be difficult to show that it was specifically for the benefit of the relevant minor or unborn beneficiary.

The reforms amend the relevant provision (being Section 72 of the Trusts Law) to substitute the "*benefit test"* with a "*no detriment test*", thus lowering the threshold for the Court's approval to a trust variation. This means that rather than showing the variation would benefit the relevant person, it is now only necessary to show that it would not be to their detriment. The logical new standard will make it easier to vary a trust, while still offering the appropriate level of protection to minor and unborn beneficiaries.

4 *Schroder Cayman Bank and Trust Company Limited -v- Schroder Trust AG (2015) 1 CILR 239*
5 Section 72 Trusts Law (2011 Revision)

Resolution of disputes

Flowing from the above noted reforms, a new Section 64B is inserted into the legislation to apply a similar "*no detriment test*" where the Grand Court is asked to approve a compromise of a trust dispute on behalf of a beneficiary (such as minor or unborn who cannot otherwise be party to the compromise).

Until the amendments, the Grand Court relied on its inherent jurisdiction to approve such a compromise on a beneficiary's behalf (there being no relevant statutory provision in this regard). However, the test required the compromise to be "*for the benefit"* of that person. Consistent with the approach now taken to varying trusts, the new Section 64B of the Trusts Law substitutes the "*for benefit*" common law test with a statutory "*no detriment*" test. Thus allowing the Court to approve a compromise of trust dispute affecting minor or unborn beneficiaries, provided that such compromise is not to the detriment of the relevant beneficiary, notwithstanding that the Court may not be satisfied as to whether it actually benefits such person.

While modern disputes are increasingly resolved by compromise and alternative dispute resolution ("ADR"), there were (prior to this reform), long-acknowledged difficulties in seeking to follow such an approach in the trusts context (unless all beneficiaries were in existence and adults). Making it easier to resolve disputes is obviously an important modernisation for the Trusts Law, although such compromise will still involve the Court system.

The involvement of the Courts in resolving Cayman Islands' trusts disputes is likely to continue for the foreseeable future as the Cayman Islands takes the approach that court involvement is preferable to independent arbitration or ADR. To this end, it should be noted that the Grand Court already offers the resolution of trust disputes via confidential processes in chambers and with relatively minor fees compared to those normally associated with arbitration. As such the present dispute resolution regime may in any event be preferable to a separate ADR regime.

Extension of the "firewall" foreign element provisions

Cayman's firewall legislation (in Sections 90-93 of the Trusts Law) protects trusts which are governed by the laws of the Cayman Islands from being attacked because a foreign law confers a party with an interest in the trust's assets by virtue of their personal relationship with the settlor (for example persons claiming as a result of forced heirship). This "firewall" offers significant asset protection and estate planning benefits, especially from jurisdictions which do not allow a testator freedom as to how to dispose of their assets on death (which is defined as "forced heirship").

Questions had arisen as to the application of the provisions and the protection afforded to the settlor's descendants once the settlor was no longer living. In order to avoid any technical

difficulties in this regard, the relevant provision (being subsection 91(b)) has been amended by extending the reference to a "*personal relationship to the settlor*" to include a personal relationship to any beneficiary including a discretionary beneficiary. Thus, the reforms enhance the protection offered by the "firewall" so that it is clearly available to all beneficiaries in countering any potential claims against a trust's assets in a foreign jurisdiction.

"Trust corporation" definition

The definition of a "trust corporation" has been amended to include not just licensed trust companies, but also their controlled subsidiaries.[6] This minor amendment widens the scope for trustees to utilise the retirement provisions in the Trusts Law and also achieves consistency with the term's definition relating to Cayman STAR trusts at Section 105(2) of the Trusts Law.

Codification of trustees' duties

It is also of interest to note that the reforms did not include any measures to codify trustees' fiduciary duties. This was one of the topics considered by the Cayman Islands Law Reform Commission ("Commission") in the lead up to the Trusts Law revision.[7] However, the Commission appears to have maintained its initial view that such codification is unnecessary and that the proper approach is to leave the evolution of trustees' duties to the common law. This continues to set Cayman apart from jurisdictions such as UK, Jersey and Guernsey where certain duties are encased in statute.

Conclusion

The recent reforms are a positive step toward the ongoing and incremental modernisation of the Trusts Law in the Cayman Islands. It is comforting to see the commitment of the legislature to ensuring that the Cayman Islands remains an attractive and leading jurisdiction for wealth structuring and management well into the future.

6 the amendment relates to the definition contained in Section 2 of the Trusts Law

7 Cayman Islands Law Reform Commission, Trusts Law Reform: Discussion Paper (5 April 2017)

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