Scottish Law Commission

promoting law reform

(DISCUSSION PAPER No 148)

Discussion Paper on Supplementary and Miscellaneous Issues relating to Trust Law

discussion paper

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April 2011

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The Scottish Law Commission was set up by section 2 of the Law Commissions Act 1965[1] for the purpose of promoting the reform of the law of Scotland. The Commissioners are:

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The Commission would be grateful if comments on this Discussion Paper were submitted by Friday 1 July 2011.

Please ensure that, prior to submitting your comments, you read notes 1-3 on the facing page. Comments may be made on all or any of the matters raised in the paper. All non-electronic correspondence should be addressed to:

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[1] Amended by the Scotland Act 1998 (Consequential Modifications) (No 2) Order 1999 (SI 1999/1820).

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Abbreviations

DCFR,

> Draft Common Frame of Reference: Principles, Definitions and Model Rules of European Private Law (Full Edition: Christian von Bar, Eric Clive (eds), 6 vols, 2009; Outline Edition: Christian von Bar, Eric Clive and Hans Schulte-Nölke (eds), 2009)

DP on Accumulation,

> Discussion Paper on Accumulation of Income and Lifetime of Private Trusts (DP No 142, 2010)

DP on Breach of Trust,

> Discussion Paper on Breach of Trust (DP No 123, 2003)

DP on Trust Administration,

> Discussion Paper on Trustees and Trust Administration (DP No 126, 2004)

DP on Trustees' Liability,

> Discussion Paper on Liability of Trustees to Third Parties (DP No 138, 2008)

Lewin,

> *Lewin on Trusts*, John Mowbray, Lynton Tucker, Nicholas Le Poidevin, James Brightwell, Edwin Simpson (eds) (18th ed, 2008)

Panico,

> Paolo Panico, *International Trust Laws* (2010)

Thomas and Hudson,

> Geraint Thomas and Alastair Hudson, *The Law of Trusts* (2nd ed, 2010)

PART 1: INTRODUCTORY ISSUES

Chapter 1 Introduction

Background to the project

1.1 The Commission has been giving consideration to aspects of the law of trusts for some time. The first area examined, jointly with the Law Commission for England and Wales, was trustees' powers of investment. This resulted in a joint Report, Trustees' Powers and Duties.[1] The Scottish recommendations in that Report were confined to the investment powers of trustees and their ability to purchase land, whether for investment or otherwise. The recommendations for England and Wales went further, and considered the powers and duties of trustees generally. The English provisions in the Report were implemented by the Trustee Act 2000. The Scottish provisions were implemented some five years later, in Part 3 of the Charities and Trustee Investment (Scotland) Act 2005. The technique adopted was to amend the Trusts (Scotland) Act 1921, the basic statute that still, after nearly 90 years, regulates Scottish trust law.

1.2 Thereafter the Commission has issued seven further Discussion Papers and one Report. The Discussion Papers are as follows:

- Breach of Trust (DP No 123, 2003),
- Apportionment of Trust Receipts and Outgoings (DP No 124, 2003),
- Trustees and Trust Administration (DP No 126, 2004),
- Variation and Termination of Trusts (DP No 129, 2005),
- Nature and Constitution of Trusts (DP No 133, 2006),
- Liability of Trustees to Third Parties (DP No 138, 2008),
- Accumulation of Income and Lifetime of Private Trusts (DP No 142, 2010).

One Report has been published, on the Variation and Termination of Trusts.[2]

The current state of trust law in Scotland

1.3 The trust is a very versatile legal institution, and in the modern legal and financial world it can fulfil many different functions, especially in the investment and commercial fields. Consequently it is important the law of trusts should be accessible to a wide range of users and their advisers. This means that the law should be expressed clearly and coherently in modern statutory language. In recent years there has been increasing competition among jurisdictions to attract trust business on an international basis. This is important not only for the legal profession but also for the financial and investment community as the existence of

[1] Law Com No 260, Scot Law Com No 172 (1999).
[2] Scot Law Com No 206 (2007).

modern, flexible legal vehicles is essential to enable them to provide a service that will attract international business. Consequently jurisdictions that wish to attract international financial and investment business have in recent years reformed their trust law in a major fashion, to bring it into line with modern requirements.

1.4 Numerous examples can be cited. One is Jersey. Trusts in Jersey are governed by the Trusts (Jersey) Law 1984. This has been revised by statutes passed in 1984, 1989, 1991, 1996 and 2006. The amendments have been worked into the basic legislation in a coherent and easily accessible form. The result is trust legislation that is clear and up-to-date. In any attempt to obtain international trust business, there can be little doubt that the Jersey legislation is much more attractive than that in Scotland. Many other examples could be cited. In New Zealand, another jurisdiction that attempts to attract international trust business, the main statute is the Trustee Act 1956. This Act has been amended by further acts or other legislation passed in 1957, 1960, 1968, 1974, 1982, 1986, 1988, 1999, 2001, 2006 and 2010. The result is still reasonably coherent, but the New Zealand Law Commission has recently begun a full review of the 1956 Act; in their Introductory Issues Paper[3] they state that a full review of the Act is long overdue, and that it needs modernisation and that some provisions need clarification and anomalies should be removed. Even in England and Wales, where basic legislation is frequently permitted to remain in force for very long periods, the Trustee Act 1925 has been significantly amended by the Trustee Act 2000, and other aspects of the law of trusts have been altered by the Perpetuities and Accumulations Act 2009.[4]

1.5 These jurisdictions stand in sharp contrast to Scotland. The basic statute regulating trusts in Scotland is the Trusts (Scotland) Act 1921.[5] That Act is now 90 years old, and it looks very dated in both style and substance. Much of it is redolent of an age when trusts were used to hold landed estates or, through the marriage contract trust, to deal with weaknesses in the law relating to the property of married women. Today, while trusts of that nature can be encountered, it is much more common to find trusts used for the purposes of tax and estate planning or to regulate a family's business interests or for commercial purposes. The use of trusts for commercial purposes can take many forms, including investment vehicles, pension trusts, securitisation trusts and many others. Those changes have not been reflected in Scottish trusts legislation.

1.6 Apart from the Trusts (Scotland) Act 1921, other legislation has been passed subsequently: the main statutory provisions are the Trustee Investments Act 1961, the Trusts (Scotland) Act 1961, the Law Reform (Miscellaneous Provisions) (Scotland) Act 1966 and, as mentioned above, the Charities and Trustee Investment Act 2005. In part these Acts amend the 1921 Act; in part they provide further free-standing provisions. The result is that the trusts legislation is complicated in form and difficult to access. Because of the economic significance of trusts it is important that the legislation should be accessible to all users, not

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[3] Review of Trust Law in New Zealand: Introductory Issues Paper (Issues Paper 19, Nov 2010: http://www.lawcom.govt.nz/project/review-law-trusts?quicktabs_23=issues_paper).

[4] Both of the latter statutes were the result of reports by the Law Commission for England and Wales: the Trustee Act 2000 implemented, with minor modifications, the recommendations of the Report by the Law Commission and the Scottish Law Commission on Trustees' Powers and Duties (Law Com No 260, Scot Law Com No 172, 1999) and the Perpetuities and Accumulations Act 2009 implemented the recommendations of the Law Commission's Report on the Rules against Perpetuities and Excessive Accumulations (Law Com No 251, 1998).

[5] Much of the 1921 Act is derived from earlier legislation, notably the Trusts (Scotland) Act 1867 and the Trustees (Scotland) Act 1861; often the Victorian provisions are copied verbatim.

merely to lawyers who specialise in the field. The existing legislation appears to us to be clearly deficient in this respect. Moreover it is, as we have stated, seriously outdated in both form and substance.

1.7 In the course of the trusts project we have examined the law in numerous other jurisdictions. It is fair to say that in all of these the basic legislation is more up-to-date and accessible than in Scotland, in most cases very plainly so. We have also examined the relevant provisions of the Draft Common Frame of Reference, particularly those in Book X on Trusts.[6] Moreover, in the course of our recent consultations with advisory groups, it has been suggested that, because of the present state of the law in Scotland, in particular the statutory provisions, Scots law does not appear attractive to persons considering setting up trusts. This is especially when it is compared with other jurisdictions. This seems to us to indicate that the statutory provisions governing trusts are in urgent need of reform, so that international trust business may be attracted to Scotland and Scottish trust business may be retained. In this connection, it is not merely the legal profession that benefits; as mentioned above, the existence of a modern trust law is important to the investment and financial community, and should be of great assistance in generating investment and financial business in Scotland.

The present state of the project on the law of trusts

1.8 We received detailed responses to all of our discussion papers from a substantial range of interested parties. Generally speaking, these were supportive of the proposals that we made. We have also had very useful comments at different stages of our project from members of our Advisory Groups.[7] We greatly appreciate the input from each of these sources. Our present intention is that we should now proceed to publish a report with an accompanying Bill on the basis of the discussion papers and the responses. The result will be a comprehensive statement of the statutory provisions that affect trusts in Scots law, with significant updating.[8] In particular, we envisage that there will be important new provisions in areas such as the lifetime of trusts, the alteration of trust purposes, the provision of information to beneficiaries and, possibly, the extent to which private purpose trusts may be set up. This will, we hope, deal with the problems discussed above, that Scots law in its existing state is seriously outdated and inaccessible.

1.9 If this course is followed, we are of opinion that it will not be necessary to implement the proposals contained in the Discussion Paper on the Nature and Constitution of Trusts. The matters covered by that Discussion Paper were as follows:

- The definition and nature of a trust in Scots law;
- The rules for the creation of *inter vivos* trusts;
- The effectiveness of a trust against creditors of the truster;

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[6] The Draft Common Frame of Reference: Principles, Definitions and Model Rules of European Private Law ("DCFR") was published in 2009. For a general introduction to the DCFR project and why it is of interest to the work of law reform at the Scottish Law Commission see our recent Discussion Paper on Interpretation of Contract (DP No 147, 2011), paras 1.2-1.7. Where relevant, we cite the DCFR in footnotes to the current paper.

[7] We list the members of our Advisory Groups in Appendix C.

[8] In effect this will involve the updating and re-statement of the Trust (Scotland) Act 1921, the Trustee Investments Act 1961, the Trusts (Scotland) Act 1961, the Law Reform (Miscellaneous Provisions) (Scotland) Act 1966 and the Charities and Trustee Investment (Scotland) Act 2005, so far as relating to powers of investment.

- The requirements of writing;
- The rules on the constitution of *mortis causa* trusts;
- The validity of truster-as-trustee trusts;
- The validity of latent trusts of moveable property;
- The validity of latent trusts of heritable property, and in particular whether there should be a requirement that such trusts should be registered in the Land Register.

1.10 The reason for excluding those matters from an updating and restatement of the trust legislation is that they are areas that have historically been left to the common law or other legislation such as the Requirements of Writing (Scotland) Act 1995. Our current view is that the common law has generally been satisfactory in setting out the essential structure and legal effects of a trust, and the legislation governing requirements of writing is also satisfactory so far as trusts are concerned. The responses to our consultation did not indicate any serious need for reform in this area.[9] We will, however, state our reasons for excluding these areas in our forthcoming report.

1.11 Nevertheless, it is possible that the form of restatement of the law that is required is not merely an updating of the existing legislation but a fully comprehensive restatement such as is found in jurisdictions such as Jersey and Malta. We discuss this matter in Chapter 2. If we were to follow that course the matters considered in our Discussion Paper on the Nature and Constitution of Trusts would be relevant, because the basic nature of a trust and the manner in which trusts can be created would require to be stated in the legislation.

Further consultation

1.12 In giving detailed consideration to the responses to our discussion papers, we have changed our views to some extent on certain matters. In addition, we have taken account of developments since the earlier discussion papers were published, and these have affected our thinking in some areas. Because of the significance of some of these changes, we are of opinion that we should conduct a further limited consultation on the more important matters where we think that the treatment in the earlier discussion papers was inadequate. This exercise will be limited, in that it is confined to matters where the Commission's views have changed to a significant extent. Those matters are discrete, and there is no common theme to them. Nevertheless, the overall context should be apparent from the references to our earlier discussion papers.

1.13 In addition, our researches have indicated a number of important statutory developments in other jurisdictions that we think should be considered in Scotland. We are of opinion that we should also consult on these matters. The law of trusts is of great practical significance. Over the last 20 to 30 years its scope has increased greatly, and trusts are now of fundamental importance in a large number of commercial contexts. In addition to the traditional commercial applications such as pension funds and unit trusts, trusts are now frequently found playing a vital part in complex corporate and property

[9] A minority view was expressed questioning whether truster-as-trustee trusts should be recognised, although the majority supported them and they are widely used in commercial agreements.

transactions. They also serve as the basis for a wide range of financial and investment vehicles. Thus trusts are important not merely in the traditional legal world; they are also fundamental to the commercial world. We are firmly of the view that the law of trusts must be updated in order that the institution can properly fulfil this role.

1.14 We have become aware that in a number of jurisdictions new forms of trust have been developed to cater for modern commercial and financial needs. Prominent among these are the STAR trusts developed in the Cayman Islands[10] and the VISTA trusts developed in the British Virgin Islands.[11] Broadly similar forms of trust are now available in many other jurisdictions including, within Europe, Jersey, Guernsey and the Isle of Man. New Zealand is now giving active consideration to the adoption of such forms of trust. If Scotland were to follow a similar course, we think that that could give an important competitive edge to the Scottish financial services industry, which is of course of great importance in the Scottish economy.

1.15 This Discussion Paper is divided into three Parts. The first is made up of this Chapter and Chapter 2, where we raise the possibility of enacting a comprehensive statement of trust law in Scotland. In Part 2, consisting of Chapters 3 to 9, we re-consult on a number of matters considered in the earlier discussion papers in the trusts project, with a view to addressing specific issues which have arisen within the following discrete topics. In Chapter 3 we consider the basis on which trustees, as a body and individually, are liable in delict to third parties. In Chapter 4 we discuss the liability of trustees, both individually and as a body, for litigation expenses, and suggest a new scheme to deal with the problem of the personal liability of trustees. In Chapter 5 we consider certain aspects of the position of nominees and custodians. Nominees have come to assume great importance in practice, as shares held under the Crest system are held by them and they are extensively used to hold quoted and unquoted securities. Consequently we think that the law in this area merits further examination. In Chapter 6 we reconsider an issue that has arisen in relation to our discussion of breach of trust, namely the standard of care that a trustee is required to demonstrate in his or her dealings with the trust. In Chapter 7 we discuss the jurisdiction of the court and the procedures that might be put in place to deal with cases where an application to the court is required: our guiding principle is that the procedures should be straightforward and easy to use. In Chapter 8 we consider certain problems that have come to our attention regarding the position of *ex officio* trustees, in particular the appointment, removal or replacement of such trustees in cases where the office holder cannot or does not want to act. In Chapter 9 we discuss the statutory power of advancement that applies in default of any provision in the trust deed.

1.16 In Part 3, consisting of Chapters 10 to 14, we consider five other new matters which have not previously been covered in the trusts project but where we think that legislation may be desirable. We begin in Chapter 10 by considering the obligations of trustees to provide information to beneficiaries of a trust. This is an important area of the law in practice but it has received very little consideration by the Scottish courts, and in other jurisdictions a number of different, and contradictory, approaches have been taken. Consequently we think that this topic merits detailed consideration.

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[10] See ch 12.
[11] See ch 13.

1.17 In Chapters 11-13 we consider three legal institutions that are found in other jurisdictions which we think might usefully be introduced into Scots law. These are all institutions designed to increase the usefulness of trusts as investment and financial vehicles. They have all been welcomed in commercial and investment circles, and they appear to have been successful in attracting significant amounts of legal business to the jurisdictions in which they operate. We are very conscious of the importance of the law of trusts to the financial and investment community in Scotland, and we think that there might be significant benefits to the Scottish financial services industry if Scotland were to adopt one or more of these institutions. The first of these, considered in Chapter 11, is the protector. This is a person appointed by the truster to make sure that his or her wishes are properly carried through by the trustees. On occasion a protector may be given power to appoint or remove trustees, or to give directions to the trustees as to how they should exercise discretionary and other powers. Evidence from other legal systems indicates that protectors are fairly popular, and we ask whether this might be so in Scotland.

1.18 The second institution that might prove useful in Scotland is the private purpose trust.[12] In Chapter 12 we ask whether Scots law should make express provision to authorise the creation of such trusts. Private purpose trusts are permitted in a number of jurisdictions that attract international trust business, and public purpose trusts are encountered in existing Scots law. The main practical problem with purpose trusts is enforcement of the trust purposes in the absence of named beneficiaries. In Scottish public trusts the Lord Advocate fulfils that role, and jurisdictions that permit private purpose trusts usually provide for the appointment of an enforcer, a person whose responsibility it is to ensure that the trust purposes are duly performed. We accordingly devote some attention to the institution of the enforcer. In general, our discussion of private purpose trusts and enforcers is informed by the STAR trusts legislation of the Cayman Islands[13] and, to some extent, the purpose trusts provisions of the Guernsey Trusts Law.[14]

1.19 The third institution that we consider is a type of trust similar to the VISTA trusts permitted in the British Virgin Islands.[15] This is a very specific form of trust designed to hold a controlling interest in a company where the truster wishes to ensure that the interests of the company and its business are placed before the interests of beneficiaries. That involves important modifications to trustees' general obligation to invest prudently, since that obligation may require trustees to take a view contrary to the interests of the company. In Chapter 13 we consider whether Scots law should make express provision for trusts of this nature. We should point out that, if private purpose trusts were permitted, it would be possible to use them to fulfil the same function as a VISTA trust, although the precise terms of the trust would require careful drafting in each case. To that extent, permitting private purpose trusts might render legislation for VISTA-type trusts redundant. It is possible, however, that making specific provision for this highly specialised form of trust might itself prove attractive, in that the basic requirements of the trust are expressly set out in the legislation.

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[12] A purpose trust is a trust that does not have defined beneficiaries but rather exists to achieve a defined purpose, frequently of a philanthropic or business nature.
[13] Special Trusts (Alternative Regime) Law 1997, now contained in Pt VIII of the Cayman Islands Trusts Law (2009 Revision) (reproduced in Appendix B).
[14] Trusts (Guernsey) Law 2007, s 12 (reproduced in Appendix B).
[15] Virgin Islands Special Trusts Act 2003 (reproduced in Appendix B).

1.20 Finally, in Chapter 14 we discuss the issue of what might be done in the case of error or other defect in the exercise of trustees' discretionary powers. In planning this over recent months, we intended to raise the question of whether there is any support for or opposition to the statutory enactment of a Scottish rule along the lines of what we understood to be the English rule in *Hastings-Bass*[16] (which would enable the exercise of trustees' discretionary powers to be reduced or otherwise altered if the trustees were in error as to the considerations that ought to have been taken into account by them in the exercise of their power). However, very shortly before this paper was ready to be published the Court of Appeal issued its decision in *Pitt v Holt; Futter v Futter*,[17] which reviewed this area of the law and greatly restricted what had previously been understood to be the *Hasting-Bass* principle. It is too early to know whether this decision will be appealed to the Supreme Court but, whilst the principle has been the subject of litigation in most of the major trust jurisdictions, it has never come before the Scottish courts. Nevertheless, we are aware of suggestions in a recent article that the rule "has been vitally important in the protection of beneficiaries from tax charges arising from the acts of trustees".[18] In the same article, it is said that "[t]he offshore trust industry is highly competitive, and a jurisdiction that is perceived to have no *Hasting-Bass* principle will lose business to another which is more accommodating".[19] Against that background, we think that it is important that this general topic is considered for possible reform of the law. We have yet to reflect fully on the very recent Court of Appeal's decision mentioned just above, but we see value at the present time in asking whether there is support for a statutory rule under which errors or other defects in trustees' exercise of their discretionary powers can be challenged.

1.21 Finally, we are conscious that many of those who consider this Discussion Paper will have very extensive practical experience of the law of trusts. We are anxious at this stage to identify any further problems that we have not yet considered that might merit inclusion in our final report and draft Bill. We accordingly ask the following question:

1. **Are there any further matters, beyond those considered in this and earlier discussion papers in the trust project, that we ought to consider in our report and draft Bill? In this connection, we are particularly concerned to know whether there are any recent developments in the commercial and investment world that should be reflected in Scottish Trusts legislation. This applies both to commercial and financial developments within the United Kingdom and to the position internationally, where new forms of trust or new procedures may be appearing that could usefully be replicated in Scotland.**

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[16] *Re Hastings-Bass* [1975] Ch 25.
[17] [2011] EWCA Civ 197, 9 March 2011.
[18] Joseph Howard, "Hastings-Bass – oceans apart?" 2011 Private Client Business 1, 23 at p 26.
[19] Ibid.

Chapter 2 A possible comprehensive statutory statement of trust law in Scotland

2.1 It has been suggested to us that it might be desirable to go further than an updating and restatement of the existing trusts legislation and to enact a fully comprehensive statement of trust law. Legislation of that sort has long existed in India,[1] and a recent example is to be found in Jersey, where the Trusts (Jersey) Law 1984 provides a detailed and comprehensive statement of the principles of trust law.[2] Yet another example is found in Malta, where the Trusts and Trustees Act 1988 provides a comprehensive statement of the law including, at section 3, a definition of a trust, and extensive provisions about the validity of trusts and the manner in which a trust can be set up.[3] This is in addition to the matters that have traditionally been covered by trust legislation in the English-speaking world. The availability of a comprehensive statement might be particularly significant if the potential truster is from a jurisdiction where trusts have not traditionally been found, and might therefore be uncertain as to precisely what a trust achieves. For such trusters and their advisers, it might be helpful to set out the fundamental nature of a trust and its legal effects in primary legislation.

2.2 On the other hand, the drafting of such legislation would not be especially easy, as a number of basic concepts that are at present contained in the common law would have to be set out in definitive statutory form. Uncertainties would have to be resolved, and a number of important policy issues would have to be decided, on which further consultation would almost certainly be necessary. Moreover, it is likely that further areas of doubt would be discovered even after such legislation was enacted. A common criticism of comprehensive statements of the law is that flexibility may be reduced. While this has been true in some legal systems that have resorted to extensive codification, it is not inevitable; indeed, comprehensive statutes may be drafted that permit the courts to develop the institutions that are created in a practical manner to meet changing economic and social conditions. Ultimately, the advantage of a comprehensive statement of the law is that it promotes greater certainty as to what the law is. This may be of importance in a field such as the law of trusts, where those who make use of the law are concerned to make detailed plans for the future of their families, their businesses or their investments.

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[1] The Indian Trusts Act 1882, as subsequently amended, and which is available, for instance, at http://www.helplinelaw.com/docs/THE%20INDIAN%20TRUSTS%20ACT,%201882.

[2] The Trusts (Jersey) Law 1984, as subsequently amended, and which is available at http://www.jerseylaw.je/law/lawsinforce/consolidated/13/13.875_TrustsLaw1984_RevisedEdition_1January2007.pdf. (Certain provisions are reproduced in Appendix B.) In the USA, the Uniform Trusts Code provides States with a nearly comprehensive set of default rules on the regulation of trusts: see http://www.law.upenn.edu/bll/archives/ulc/uta/2005final.htm. A further example of a comprehensive statement of trust law is found in the Quebec Civil Code at Bk 4, Titles XI-XII, Arts 1260-1370.

[3] The Trusts and Trustees Act 1988 is reasonably modern, and has been amended in 1989, 1994, 2004, 2006, twice in 2007 and in 2009. This illustrates the way in which trust legislation ought to be kept up-to-date.

2.3 If a comprehensive statutory statement of Scottish trust law were favoured, the scope of the legislation would be significantly greater than we propose at present. If there is a clear demand for such a step, however, it is likely that we would complete the trusts project by publishing a discussion paper and in due course a report on a comprehensive statement. Because of the relatively radical nature of such a step, we think that it would be appropriate to publish a draft Bill for comment prior to preparing the final report. Consequently, it is likely that we would publish a discussion paper in which the major policy issues were considered but which also contained a draft Bill, based on the proposals in the discussion paper. We would invite comments on the draft Bill, and in due course our intention would be to publish a report with a final Bill, taking account of comments received during the consultation period.

2.4 In the meantime, even if such a step were thought desirable, a restatement and updating of the existing legislation would be an important step in that direction, and is in any event clearly necessary as a matter of urgency. For that reason we are minded at this stage to proceed with an updated version of the trusts legislation with some additions. Nevertheless, we invite comments on the following question:

2. Would there be an advantage in Scotland's having a comprehensive statutory statement of trust law along the lines of, for example, the Trusts (Jersey) Law?

PART 2: RE-CONSULTATION

Chapter 3 Liability for delict

Proposals in our earlier Discussion Paper

3.1 The delictual liability of trustees was considered in Part 3 of our Discussion Paper on Liability of Trustees to Third Parties.[1] Ordinary delictual liability was considered at paragraphs 3.2-3.9. We pointed out the lack of authority in this area. The most recent case[2] indicated that, in making payment of a delictual claim, trustees are *prima facie* liable as individuals. They are entitled to relief out of the trust estate.[3] That is the *prima facie* rule, but it can be modified by the form of decree, and if the trust estate is insufficient, the form of decree becomes important: if the decree is against the trustees "as trustees", it is limited to recovery out of the trust estate; if it is against the trustees as individuals, it is not so limited and recovery is possible from the trustees' own property. Finally, if the trustees have themselves been negligent, it is possible for damages to be awarded against them personally without relief from the trust estate.

3.2 We suggested that it was clear that trustees should be responsible for delicts committed by them, their agents or employees, and that the important question was to what extent damages should be payable from the trust estate or from the trustees' own assets. We expressed the view that it was wrong that trustees should be personally liable in all situations where their employees or agents had been negligent, and noted that there was evidence that people were becoming increasingly reluctant to act as trustees because of the financial risks involved. We expressed a preference for the rule found in the American Uniform Trust Code[4] whereby trustees are only personally liable if they have been personally at fault. If on the other hand a person suffers loss without any trustee's being personally at fault, the trustees should be sued in a representative capacity, with the result that damages would only be payable out of the trust estate. We further thought that the court should have power to apportion damages between the trust estate and the personal assets of a trustee who has been personally at fault. That might be appropriate where, for example, the damage was caused partially by the trustee's own fault and partly by the fault of an employee of the trust. Finally, we expressed the opinion that a trustee who is at fault and therefore personally liable should not be entitled to seek relief or indemnity from the trust estate; a trustee who was at fault could not be said to have behaved reasonably and within his or her powers. Against that background we made the following proposal:

> "(1) Where a person suffers loss as a result of some act or omission of the trustees (or anyone for whom they are responsible) in the course of administering the trust, damages should generally be payable from the trustees' trust patrimony. Damages should be payable from a trustee's

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[1] DP No 138, 2008. We refer to this as the "DP on Trustees' Liability".
[2] *Mulholland v MacFarlane's Trs* 1928 SLT 251. In that case, the defenders had been designated as trustees and so damages were payable only from the trust estate.
[3] Mackenzie Stuart, *The Law of Trusts* (1932).
[4] Section 1010(b): "A trustee is personally liable for torts committed in the course of administering a trust, or for obligations rising from ownership or control of trust property, including liability for violation of environmental law, only if the trustee is personally at fault."

private patrimony only if, and to the extent that, he or she was personally at fault.

(2) It should be competent for the court to award damages partly from the trustees' trust patrimony and partly from the private patrimony of a trustee who was at fault."[5]

3.3 In our DP on Trustees' Liability we went on to discuss the delictual consequences arising out of the ownership and occupation of property.[6] Trustees may incur civil liability in respect of contaminated land, either as actual polluters or as the owners or occupiers of contaminated land. This can represent a major potential liability. The relevant legislation[7] defines the owner in such a way as to cover trustees, but is silent as to the capacity in which the trustees are liable. We noted that the American Uniform Trust Code[8] excludes personal liability of trustees except in cases where a trustee is personally at fault. The official comment on the relevant section states that protection from personal liability for environmental law violations had been specifically included as that was of particular concern to trustees. We agreed with that approach, that personal liability should require some element of personal fault, and that ownership or occupation of property should be insufficient by itself for personal liability.

3.4 We also considered the Occupiers' Liability (Scotland) Act 1960, which imposes a duty of care on those occupying or controlling premises towards persons entering the premises. The Act does not deal expressly with trustees, and it is not clear whether they are liable personally or only in a representative capacity. We thought that a similar approach should be taken as in the case of environmental liability.

3.5 Against that background we made the following proposal:

"(1) Where liability arises out of the trustees' ownership or control of trust property or under environmental legislation only the trustees' trust patrimony should generally be liable. A trustee's private patrimony should be liable only if, and to the extent that, he or she was personally at fault.

(2) It should be competent for the court to award damages partly from the trustees' trust patrimony and partly from the private patrimony of a trustee who was at fault."[9]

Consultation responses

3.6 On public consultation, we received broad support for the proposals reproduced in paragraphs 3.2 and 3.5 above. Certain of the comments made, however, caused us to reconsider the details of our proposals. At a general level, the Faculty of Advocates thought that the limitation that we proposed on trustees' personal liability could be considered unfair in that it would give trustees greater protection than individuals, partners and members of

[5] DP on Trustees' Liability, proposal 7.
[6] DP on Trustees' Liability, paras 3.10-3.14.
[7] Environmental Protection Act 1990, s 33; Pollution Prevention and Control (Scotland) Regulations 2000; Control of Pollution Act 1974, s 30F.
[8] Section 1010(b).
[9] DP on Trustees' Liability, proposal 8.

unincorporated associations. This, they suggested, "might have the effect of opening up the trust vehicle to abuse because the liability of a trust would be limited to the extent of the trust patrimony unless a trustee was 'personally' at fault". As an alternative, the Faculty suggested that a provision modelled on section 1157 of the Companies Act 2006 might be appropriate;[10] this allows the court to grant an officer of a company relief against the company if the officer acted honestly and reasonably and ought fairly to be excused. This would mean that trustees should be liable personally in the first instance, with relief only at the court's discretion.

3.7 By contrast, STEP[11] considered that fixing liability on trustees who were "personally" at fault might go too far: the word "personal" was, they thought, unhelpful. STEP considered that the personal liability of trustees should be confined to three cases:

(i) where the trustee was the actual wrongdoer;

(ii) where the trustee was a supervisor of the wrongdoer and failed to take reasonable care to devise, institute or maintain a safe system; or

(iii) where the trustee "failed to show the prudence of an ordinary man of business".

The last of these cases, it was suggested, would cover the possibility that trustees failed to take out adequate insurance. The latter point was also made by the Faculty of Advocates.

3.8 We have given careful consideration to the submissions received, and we think that on balance our original suggestions are broadly correct, subject to the further matters discussed below. In relation to the Faculty's comments, it is true that trustees will be given a degree of protection that is not accorded, for example, to partners. Nevertheless, such protection is available to those who carry on business through the vehicle of a limited company, or indeed a limited liability partnership. Abuse might occur, but the existence of personal liability where a trustee is personally at fault will, we think, deal with nearly all such cases. We are also concerned at the suggestion that potential trustees may be discouraged from accepting an appointment because of the risk of personal liability. That point was reinforced by STEP's comments.

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[10] Section 1157 (Power of court to grant relief in certain cases) provides as follows:
"(1) If in proceedings for negligence, default, breach of duty or breach of trust against–
(a) an officer of a company, or
(b) a person employed by a company as auditor (whether he is or is not an officer of the company),
it appears to the court hearing the case that the officer or person is or may be liable but that he acted honestly and reasonably, and that having regard to all the circumstances of the case (including those connected with his appointment) he ought fairly to be excused, the court may relieve him, either wholly or in part, from his liability on such terms as it thinks fit.
(2) If any such officer or person has reason to apprehend that a claim will or might be made against him in respect of negligence, default, breach of duty or breach of trust–
(a) he may apply to the court for relief, and
(b) the court has the same power to relieve him as it would have had if it had been a court before which proceedings against him for negligence, default, breach of duty or breach of trust had been brought.
(3) Where a case to which subsection (1) applies is being tried by a judge with a jury, the judge, after hearing the evidence, may, if he is satisfied that the defendant (in Scotland, the defender) ought in pursuance of that subsection to be relieved either in whole or in part from the liability sought to be enforced against him, withdraw the case from the jury and forthwith direct judgment to be entered for the defendant (in Scotland, grant decree of absolvitor) on such terms as to costs (in Scotland, expenses) or otherwise as the judge may think proper."

[11] The Society of Trust and Estate Practitioners.

3.9 In relation to STEP's suggestion as to how the circumstances in which personal liability arises should be defined, we incline to the view that we should retain the concept of personal fault in the legislation, but that our report should indicate the sort of circumstances where personal liability is likely to be incurred. Cases where the trustee is the actual wrongdoer are clear. In cases where a safe system is required and a particular trustee is responsible for devising such a system, we think that personal fault would be established. A trustee who was not personally responsible for devising such a system, however, would not be subject to personal liability. The third of STEP's suggested categories, a trustee who "fails to show the prudence of an ordinary man of business", perhaps goes to the standard of care, a matter that we discuss below, rather than the incurring of personal liability. In a case where a trustee is personally responsible for a particular aspect of a trust's activities, however, failure to exercise the ordinary standard of care would on our approach give rise to personal liability. We would envisage a somewhat fuller discussion of these matters in the report.

Further issues

3.10 We are of opinion, however, that our recommendations should deal with the precise manner in which proceedings for delict can be raised against trustees. Two separate issues arise: the basis on which the injured party can raise proceedings, and the manner in which the trustees as a body and the individual trustees can settle their liability *inter se*.

3.11 So far as the first of these issues is concerned, two possibilities exist:

(i) The injured party sues the trustees as a body, and they have a right of relief against any individual trustee who is personally at fault;

(ii) The injured party has a right to sue either the trustees as a body or any trustee who is averred to be personally at fault or the body of trustees and the individual trustee jointly and severally; in effect this would involve full joint and several liability on the part of the body of trustees and any trustee who is shown to be personally at fault.

The advantage of the second of these approaches would be that the injured party was able to obtain a remedy against the trustee who was personally at fault at the outset, without the need to sue the trustees as a body first. In a case where the trust estate was inadequate to meet the award of damages, it would enable an effective remedy to be obtained at the outset, although obviously only in cases where a trustee was personally at fault. Such a procedure would in addition enable the court to apportion damages between the trustees as a body and any delinquent trustee who is personally liable. The advantage of the first approach would be to shield trustees more fully from claims by a third party. On balance, we are inclined to favour the second approach, on the basis that it is procedurally a more effective remedy, leading to a speedier and fuller resolution of the substantive issues.[12] We accordingly invite comments on the following proposal:

[12] It is also in accordance with DCFR Book X.7-401, which provides for solidary liability between trustees.

3. **Where a person suffers loss as a result of some act or omission of the trustees (or anyone for whom they are responsible) in the course of administering the trust, the trustees as a body will be liable to make reparation for such loss. In addition, any individual trustee who is personally at fault will be liable jointly and severally with the trustees as a body, and in that event any damages awarded against the individual trustee will be payable out of his or her private patrimony. In all such cases, however, it should be essential that the claim, so far as directed against an individual trustee, is on the basis that he or she was personally at fault.**

In a case where averments of personal fault are found by the court not to be justified, it can obviously be expected that a sanction in expenses will be imposed.

3.12 In view of the comments made by STEP about the definition of the circumstances in which a trustee will incur personal liability, we invite comments on the following proposal and question:

4. **It is not necessary to provide a statutory definition of "personal" liability, or of the circumstances in which personal liability is incurred. That matter should be left to the judgment of the court, but our report should contain a more detailed discussion of the circumstances in which such liability will be incurred.**

5. **We further ask if, contrary to the foregoing proposal, it is thought that a statutory definition of the circumstances in which a trustee incurs personal liability should be provided, what criteria might be used in such a definition?**

3.13 The second issue that arises is how the trustees as a body, and any individual trustee who is at fault, can settle their liability *inter se*. Two questions arise here, both involving rights of relief: can the trustees as a body recover any sum that they are compelled to pay from the trustee who is personally at fault, and can a trustee who is personally at fault and found liable to pay damages recover from the trust estate the sum that he or she has paid? These questions were not addressed expressly in our DP on Trustees' Liability. It seems to us, however, that the normal consequences of joint and several liability should apply: the trustees as a body and the individual trustee who is personally at fault are joint wrongdoers, and each should have a right of relief against the other. In addition, in the enforcement of those rights of relief, the provisions of section 3(1) of the Law Reform (Miscellaneous Provisions) (Scotland) Act 1940[13] should apply, so that the court can apportion liability as between the body of trustees and the individual trustee. We therefore propose:

[13] Section 3(1) provides:
"Where in any action of damages in respect of loss or damage arising from any wrongful acts or negligent acts or omissions two or more persons are, in pursuance of the verdict of a jury or the judgment of a court found jointly and severally liable in damages or expenses, they shall be liable inter se to contribute to such damages or expenses in such proportions as the jury or the court, as the case may be, may deem just:
Provided that nothing in this subsection shall affect the right of the person to whom such damages or expenses have been awarded to obtain a joint and several decree therefor against the persons so found liable."

6. The body of trustees and any individual trustee who is personally at fault should each have a right of relief against the other, that right being subject to the power of apportionment in section 3(1) of the Law Reform (Miscellaneous Provisions) (Scotland) Act 1940.

3.14 Another matter raised by consultees on which we wish to consult further is the question of insurance. This may be relevant in two distinct contexts. The first of these is the general duty of trustees to take out insurance in respect of trust property. This is a duty that is owed to the beneficiaries as part of the trustees' general duty to use the care and skill of a person of ordinary prudence in looking after the trust property. It is not a duty owed to third parties who may be injured by the trustees' delicts. The second context is where the trustees incur delictual liability but the assets of the trust are not sufficient to satisfy any resulting award of damages. In such a case it may be claimed by the injured party that the trustees were at fault in failing to obtain insurance, and should in consequence satisfy the award out of their own personal assets. For such a claim to be of use to the injured party, it must be made against the trustees personally, in their private capacity, because the trust assets have *ex hypothesi* been exhausted.

3.15 It is the second of those contexts that is relevant to delictual claims made by third parties against trustees. We are of opinion that the result of such a claim would depend upon whether insurance is compulsory. Insurance is compulsory in respect of the operation of motor vehicles and employers' liability. In other cases, such as property insurance, there is no obligation to take out a policy, even in respect of liability to third parties. In the cases where insurance is compulsory, the duty to insure is imposed by statute on the operator of the vehicle or the employers of a person,[14] and we think it likely that that would amount to a personal statutory duty on each trustee.[15] Consequently, in the event of a failure to insure we consider that each of the trustees would be personally liable for the failure. Nevertheless, this might be subject to an exception in cases where, for example, the trustees had expressly instructed one of their number to obtain insurance. Whether there would be personal liability in such a case would depend on circumstances. Where an outsider, such as a solicitor or an insurance broker, was instructed to obtain insurance but failed to do so, the trustees as a body would obviously have a claim against him based on breach of contract. By contrast, in cases where insurance is not compulsory, we think that it is unlikely that trustees would be personally liable to a third party for failure to insure.[16]

3.16 The other contexts in which insurance may be relevant, the general duty to take out insurance, is as we have already said an aspect of the trustees' general duty to beneficiaries

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[14] See, eg, s 143(1)(a) and (b) of the Road Traffic Act 1988; and s 1 of the Employers' Liability (Compulsory Insurance) Act 1969.

[15] It has previously been held that a failure to insure will give rise to civil liability on the part of the operator of a vehicle: *Monk v Warbey* [1932] I KB 75 (interpreting s 35 of the Road Traffic Act 1930, the statutory predecessor of s 143 of the Road Traffic Act 1988). This construction of the 1988 Act was approved in *Houston v Buchanan* 1940 SC (HL) 17, with Lord Wright acknowledging (at 38-39) that such a failure to insure will give rise to not only criminal liability under the Act, but also personal delictual liability to any injured person also. In respect of employer's liability insurance, it has been held that the directors of a company were personally liable for failure to insure (breach of their statutory duty under the Act): *Quinn v McGinty* 1999 SLT (Sh Ct) 27 per Sheriff Principal Bowen QC at 29.

[16] We note that DCFR Book X.-6:205(1) provides that a trustee will have a right to reimbursement or indemnification out of the trust fund in respect of expenditure or debt reasonably incurred in order to obtain insurance. This right does not, however, apply where the trustee is remunerated for performing obligations under the trust, nor where insurance is taken out against a liability arising from non-performance of an obligation, which is in itself intentionally or grossly negligent (DCFR Book X.-6:205(2)).

to use appropriate care and skill in the management of the trust property. So far as we can discover, the only authority in this area is *Glover's Trustees v Glover*,[17] where it was held that trustees who own heritable property are obliged to obtain fire insurance in respect of that property. At present the question of whether a duty to obtain insurance arises in any particular case, and if so the content of that duty, is a matter left to the common law. Because the question of insurance has been raised by professional bodies, however, we think that at this stage we should raise the question of whether the legislation governing trusts should make express provision for insurance. We accordingly ask the following question:

7. Is it appropriate to make provision in legislation for the obtaining of insurance by trustees? If so, how might such an obligation be formulated?

[17] 1913 SC 115.

Chapter 4 Liability for litigation expenses

Previous consultation

4.1 We considered the liability of trustees for litigation expenses in Part 4 of our Discussion Paper on Liability of Trustees to Third Parties.[1] We pointed out that the nature of trustees' liability depends on the form of the interlocutor awarding expenses. If the award is against the trustees "as trustees", the trustees are liable in their representative capacity only and the expenses are payable out of the trust estate. If that is insufficient, it is impossible to recover the balance from the trustees personally. Alternatively, the interlocutor may award expenses against named trustees personally. The effect of this is that the trustees must pay the expenses out of their private patrimonies without any right of reimbursement or relief from the trust estate. We gave examples of cases where trustees were found personally liable;[2] these include cases where trustees engage in unnecessary litigation, or unsuccessfully oppose their removal or replacement, or where litigation arises as a result of the trustees' neglect of duty. The normal form of award, however, is an interlocutor against named trustees without any further qualification. This has the effect of making the trustees personally liable to pay the expenses to the successful opponents but preserves their right of relief against the trust estate. The general rule is that they have such a right of relief provided that the expenses are necessarily, properly and reasonably incurred in the discharge of their duty.[3] If trustees litigate following the advice of counsel, they will normally be entitled to reimbursement of legal expenses from the trust estate.

4.2 We pointed out that the advantage of an award of expenses made against trustees without further qualification is that the trustees' right of relief against the trust estate is left open and can be resolved at a later date, with further proceedings if necessary. The rule also discourages trustees from indulging in rash litigation, in that they might then be personally liable for the expenses. The existing rules also benefit successful litigants who raise or defend proceedings against trustees, in that they will have a right to recover from the trust estate and if it is insufficient from the trustees' own private patrimonies.

4.3 We thought, however, that it was arguable that the present system is too discretionary and potentially onerous for trustees.[4] Normally trustees litigate responsibly, and should not have to put their private patrimonies at risk when they are simply performing their duties properly. On that basis we considered that it might be appropriate to set out the rules regarding expenses in legislation, to lessen the risk that trustees will be personally liable for expenses and to create a more certain climate. We thought that the basic rule should be that trustees who litigate as such should not be personally liable; the trust estate

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[1] DP No 138, 2008. We refer to this as the "DP on Trustees' Liability".
[2] DP on Trustees' Liability, at para 4.5.
[3] DP on Trustees' Liability, at para 4.6; see in particular *Gibson v Caddall's Trs* (1895) 22 R 889 at 893 per Lord McLaren. We note generally the differing position of DCFR Book X.-10:201-203 on this matter, which suggests that trustees will usually be personally liable to satisfy the claims of creditors in all cases, not the trust fund. The DCFR suggests that creditors can only have recourse against the trust fund to satisfy such claims if the trustee does not satisfy the debt: DCFR Book X.-10:101 et seq.
[4] DP on Trustees' Liability, para 4.9.

would be liable, and there would be no right to recover any balance from the trustees' private patrimonies other than in specified cases. Those cases would be listed, the list being based on existing categories where awards of expenses are made against trustees personally.[5] A final provision would give the court discretion to depart from the rules in exceptional circumstances.

4.4 On that basis we asked the questions:

> "(a) Should trustees' liability for litigation expenses be set out in new legislation along the lines of the scheme outlined [above]?
>
> (b) If not, what other changes, if any, to current practice should be made?"[6]

Consultation responses

4.5 On consultation, we found considerable support for the proposal, but two important respondents, the Faculty of Advocates and STEP, disagreed with it. The Faculty opposed general personal immunity on the basis that it would give an unfair advantage to trustees of insufficiently funded trusts: they would be able to avoid personal liability and the successful opponents would not recover their expenses in full. The solution suggested was the trustees should either seek an indemnity from the beneficiaries or should be required to obtain caution. In exceptional circumstances, the court could grant personal indemnity without an obligation to obtain caution.[7]

4.6 STEP argued on similar lines. They suggested that as a general rule, if the trust patrimony is unable to meet an award of expenses, the trustees' personal patrimony should be exposed to liability. Any alternative would place trustees at an advantage over other litigants. Like the Faculty, STEP noted the current power of the court to make a protective order for expenses, at least in matters of general public importance.[8]

Further proposals

4.7 In view of the comments by STEP and the Faculty of Advocates, we have reconsidered this issue in detail. If the general rule were as we proposed, that an award of expenses will normally only be enforceable against the trust estate with no personal liability on the part of the trustees, the main difficulty would arise when a trust had insufficient assets to meet an award of expenses. In such a case, a successful litigant would be left without any payment of expenses. In addition, if there was any doubt about the propriety of the

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[5] These were listed as follows (in para 4.5 of the DP on Trustees' Liability):

> "(a) where [the trustees] engaged in unnecessary litigation, either as pursuers or defenders;
> (b) where the trustees unsuccessfully opposed their removal or replacement by a judicial factor;
> (c) where the litigation has arisen due to the trustees' neglect of duty;
> (d) where a minority of the trustees unsuccessfully pursued an action in the name of the trustees without consulting their co-trustees. Where a minority defends, relief is allowed against the trust estate only if the trust has benefited from the intervention;
> (e) where the trustees have unsuccessfully opposed the reduction of the trust deed, but relief may be allowed where the character of the trustees has been impugned or where they defended the deed in good faith, particularly if they acted on the advice of counsel." (footnotes omitted)

[6] DP on Trustees' Liability, questions 9(a) and (b).

[7] This is as outlined in *McArthur v Lord Advocate* [2005] CSOH 165, 2006 SLT 170.

[8] *McArthur v Lord Advocate*, *supra*.

trustees' litigating, there might as the litigation proceeded be uncertainty on the part of the trustees as to their ultimate position.

4.8 We think that a helpful analogy can be drawn with proceedings raised by companies. If a company that has raised an action has inadequate assets, the same problem arises: a successful litigant who obtains an award of expenses is unable to satisfy it from the company's own assets and has no right of recourse against the shareholders or directors. This problem is dealt with by section 726(2) of the Companies Act 1985.[9] Essentially, if there is a significant doubt about a company's ability to pay any award of expenses, it is competent for the other party to the litigation to apply to the court for an order that the company should be ordered to find caution or other security for expenses. This provision is frequently used in practice, and appears to be effective in ensuring that awards of expenses against unsuccessful pursuers can be met. It also serves to prevent companies from being used as a vehicle for litigating without fear of the financial consequences. The section only applies to pursuers, and not company defenders. The mischief aimed at is the raising of an action by a company that lacks adequate assets, and the purpose of the section is to protect a party against whom such an action is raised. Where an action is raised against a company, by contrast, that is the voluntary act of the pursuer, and it is up to the pursuer to ascertain whether the company is worth suing.

4.9 There is, however, one important difference between a company and trust in this respect. Companies are obliged to lodge annual accounts, and these can readily be used to determine whether there is reason to believe that the company will be unable to meet an award of expenses. If it is clear, for example, that the company has a very small paid up capital and its last published accounts disclose little in the way of assets, the defender will be in a strong position in arguing that the requirements of section 726(2) are met. If, on the other hand, the company has substantial net assets and is trading at a profit, at least as disclosed in the published accounts, the defender's argument will be much weaker. Even in a case where the published accounts disclose a weak financial position, it is of course possible for the company to produce more up-to-date financial information to suggest that it will be able to meet an award of expenses. The fallback position is that the directors or shareholders or some other party agree to provide security of some sort for the expenses. If necessary this can be ordered in instalments, to meet the expenses of the action as it proceeds.

4.10 When litigation is raised by trustees, it is obviously impossible to use published accounts as a starting point.[10] Thus a defender will have no obvious source of knowledge of the trust's financial position. No doubt in some cases the Land Register can provide some information, but this will inevitably be partial at best and we do not think that it is reasonable to expect a defender to search the Land Register for the purposes of determining a trust's financial ability to meet awards of expenses. We are of opinion that the most satisfactory solution to this problem is to have a basic rule that trustees who raise an action are personally liable for the expenses of a successful defender but to entitle them to apply to the

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[9] Section 726(2) provides: "Where in Scotland a limited company is pursuer in an action or other legal proceeding, the court having jurisdiction in the matter may, if it appears by credible testimony that there is reason to believe that the company will be unable to pay the defender's expenses if successful in his defence, order the company to find caution and sist the proceedings until caution is found". In practice, security other than caution is regarded as acceptable.

[10] This is subject to an exception for charitable trusts, which are obliged to lodge their annual accounts with OSCR: s 44(1)(d) of the Charities and Trustee Investment (Scotland) Act 2005.

court for an order that they should not be so liable. To obtain such an order, they would require to establish by credible testimony that the trust estate would be sufficient to pay the defender's expenses if the pursuers were unsuccessful in the action. To that end, the trustees would normally require to lodge the trust accounts, possibly supported by valuations of trust assets or certificates relating to trust liabilities. The problems, however, are essentially evidential, and we think that the basic structure should be quite workable in practice; section 726(2) provides a useful precedent so far as evidence is concerned.

4.11 We should draw attention to one further matter. Although we have made use of section 726(2) as an analogy in considering how trustees might be liable for expenses, we do not propose that there should be any statutory power in the court to order pursuer trustees to find caution or other security. Instead, the sanction used to prevent trusts from litigating without adequate resources is the personal liability of the trustees, which will be removed only if they satisfy the court that the trust has adequate resources to finance the litigation. Personal liability might be removed, however, if the trustees provide some other form of security for the payment of expenses; for example, a company connected with the trust which had adequate resources might provide caution. The critical point is that, if the personal liability is to be removed, adequate resources must exist to pay for the litigation.

4.12 Where an action is raised against trustees, we are of opinion that the scheme set out in our DP on Trustees' Liability[11] should apply; that is the scheme described at paragraph 4.3 above. That would mean that trustees would only be personally liable in cases where they engaged in unnecessary litigation, or unsuccessfully opposed their removal or replacement, or where the litigation had arisen due to their neglect of duty. Personal liability might also be imposed where trustees unsuccessfully opposed the reduction of the trust deed, although there might be exceptions to that.[12] In all such cases, whether there is personal liability would be a matter for the discretion of the court. The reason for treating defenders differently is the same as for companies. The mischief that is aimed at is the raising of an action by the trustees with inadequate trust assets, and the purpose of the liquidation is to protect the defender who has been brought involuntarily into the action. Where an action is raised against trustees, by contrast, that is the voluntary act of the pursuer, and there is no compelling reason to make the trustees personally liable. In practice, if proceedings are raised against trustees who do not have substantial trust assets, it is likely that the trustees would point this out to the pursuer, with vouching if necessary, because the lack of assets is obviously an disincentive to continuing with proceedings. The pursuer would reach a decision in the light of that information.

4.13 We accordingly invite comments on the following proposals:

8. (a) Where trustees are pursuers in an action or other legal proceedings, they should be personally liable for any award of expenses made in favour of the defender, but they should be entitled to apply to the court for an order excluding such personal liability. In order to do so, they would require to satisfy the court that the assets of the trust were sufficient to pay the defender's expenses if successful in his or her defence, or alternatively that other security exists for payment of such expenses.

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[11] At its para 4.9.
[12] See our DP on Trustees' Liability, para 4.5.

(b) Where trustees are defenders in an action or other legal proceedings, any award of expenses in favour of the pursuers should be enforceable against the trust estate, with no recourse against the trustees' private patrimonies.

(c) The foregoing provisions should be without prejudice to the court's power to impose personal liability in cases where the trustees have engaged in unnecessary litigation or have behaved improperly, in the situations set out in footnote 5 above.

We should emphasise that the power to impose personal liability referred to in proposal 8(c) would be exceptional.

4.14 Finally, we think that the court should have a residual power to dispense with the rule stated in proposition 8(a) in exceptional cases. We have in mind a case where the trustees of a trust that lacks significant assets raise proceedings against a party who is alleged to have defrauded the trust of its assets or to have embezzled those assets; in such a case it might be quite unfair to expect the trustees to assume personal liability for expenses as a condition of raising proceedings. We accordingly propose:

9. The court should have power to dispense with personal liability as set out in proposal 8(a) in any case where such liability would be inequitable or unfair.

Chapter 5 Nominees and custodians

Background: some chronology

5.1 This section of the paper is best approached through a brief chronology because, with the benefit of hindsight, our original consultation became sandwiched between various relevant legislative reforms:

- In 1999 the Law Commission and the Scottish Law Commission published a joint Report entitled Trustees' Powers and Duties.[1] Amongst other topics it deals with nominees, but only in respect of England and Wales.[2] The recommendations relating to Scotland are confined to trustees' powers of investment.

- In 2000 the joint Report's recommendations were enacted in English law by the Trustee Act 2000. The Act contains provisions on nominees.

- In December 2004 we consulted on the use of nominees by Scottish trustees, in Part 3C of the Discussion Paper on Trustees and Trust Administration.[3] Part 3D deals with custodians.

- In 2005 the investment powers recommended in the joint Report of 1999 were inserted by the Charities and Trustee Investment (Scotland) Act 2005 into the Trusts (Scotland) Act 1921. They form section 4(1)(ea) and (eb).[4]

- The 2005 Act also contained provisions on nominees. It inserted sections 4A to 4C into the 1921 Act.[5] Sections 4B and 4C deal, respectively, with trustees' power to appoint nominees and their power to delegate investment management functions. These sections did not appear in the 2005 Bill as it was introduced into the Scottish Parliament, but were inserted at stage 3. They were drafted in consultation with the SLC.[6] The Stage 1 Report from the lead committee – the Communities Committee – set out the reasons for the inclusion.[7]

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[1] Law Com No 260, Scot Law Com No 172.
[2] This was deliberate, for reasons set out in para 1.16 of the Report (which were, essentially, that the our Fifth Programme of Law Reform contained a review of trust law – a review of which the present paper forms a part).
[3] Discussion Paper No 126. We refer to this as the "DP on Trust Administration".
[4] See s 93 of the 2005 Act.
[5] See s 94 of the 2005 Act.
[6] Official Report, 9 June 2005, col 17864.
[7] "In evidence to the Committee, Simon Mackintosh of the Charity Law Association noted that difficulties might arise 'when a trust deed contains no specific power or a trust deed's general terms are not wide enough to allow delegation' of investment management. He elaborated: 'The risk for trustees is that if they do not have a specific power and the general powers are not wide enough, they commit a breach of trust if they undertake sensible financial management by giving an investment manager a policy to act within and the requirement to report to trustees quarterly or every six months. That is a perfectly sensible way to manage a trust fund's investments, but the concern is that Scots law prevents trustees from acting in that way. The general principle of extending investment powers—which a joint report of the Law Commission and the Scottish Law Commission suggested and which has been applied in England—is to be supported.'": SP Paper 301, Communities Committee, 1st Report, 2005 (Session 2), para 231.

5.2 On one view, the fact that legislation on trustees' use of nominees and custodians followed so soon after our consultation means that further consideration of the topic is no longer necessary. While this view has merit, doubts remain about certain aspects of the legal relationship between trustee and nominee, doubts which have been fuelled in particular by recent litigation in England arising out of the collapse of Lehman Brothers. We consider that there are matters which would benefit from further consultation and reform.

Nominees

5.3 The central issue is whether the trustees' use of a nominee creates a further relationship of trust or whether it is a relationship of a different sort (such as agency or another form of contractual relationship).[8] This is especially relevant in the event of the nominee's insolvency. There was support for the first of these views in the responses to our DP (with, for example, the Faculty of Advocates saying that nomineeships "should be permitted only on the basis that they are constituted as express trusts").[9]

5.4 In the light of the changes brought about by the 2005 Act we felt that further work was needed. We therefore convened an *ad hoc* advisory group in April 2010.[10] Our understanding that there are many benefits (and some drawbacks)[11] in using nominees for certain types of investment was confirmed. We also learned that, broadly, there are two types of nominee which trustees would typically use, depending on the situation. One is the "in house" nominee company set up by a firm of solicitors or other professional firm. It will generally hold only assets of the parent organisation's clients, and the main reason for establishing such a nominee is convenience. The other type is a commercial nominee company (which may also be a subsidiary of a bank, for instance), which is run as a commercial operation in its own right.

5.5 The "in house" nominees set up by a professional firm generally present no problem. The nominee acts as trustee in relation to the assets (and where the assets are transferred to the nominee by trustees, it is they who become the beneficiaries of the new trust). We were informed that the Law Society of Scotland's master insurance provider wrote, some time ago, to solicitors' firms requiring that any nominee company owned by the firm must pass a resolution stating that it holds all assets on trust. As we are of the view that client money held by a firm, typically in its client account, is itself held on trust,[12] this would mean that where such money is transferred to an "in house" nominee it is the firm which is the beneficiary of the trust which arises on that transfer. In practice, given the use to which it is typically put, the risk of such a nominee becoming insolvent is minimal.

5.6 The position in relation to commercial nominees is less straightforward. The insolvency of Lehman Brothers has shown that (in English law, at any rate) it is far from clear whether, and if so to what extent, a nominee holds assets on trust for the client.[13] The

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[8] We note that the DCFR Book X.-5:206 categorises this practice as a "power of delegation", entrusting performance of an obligation to another individual.

[9] There was also unanimous support for a default power permitting trustees to use a nominee (proposal 6 of our DP on Trust Administration), which has now been implemented by amendment to the 1921 Act.

[10] The members are listed in Appendix C. We are very grateful to them all for their assistance.

[11] See our DP on Trust Administration, para 3.23.

[12] We discuss this issue at para 5.10 below.

[13] See, eg, *Re Lehman Brothers International (Europe) (In Administration)* [2009] EWHC 3228 (Ch), whose appeal is at [2010] EWCA Civ 917. The CA agreed with Briggs J at first instance that a trust had arisen and had done so at the point of receipt of the client's money by the nominee.

problem is compounded by the variety of sources of the various regulatory rules which nominees must follow: some are European in origin, some are domestic and others are promulgated by the Financial Services Authority in the FSA Handbook, which in turn is made up of mandatory rules and guidance. It is hardly surprising that muddles arose.

5.7 Not only did the Lehman litigation indicate that the nominee relationship is unclear, but it also led us to uncover a particular issue in relation to Scots law, which would be of relevance for an insolvent Scottish nominee. We have already alerted the Advocate General for Scotland to the issue,[14] as any legislation relating to financial services is for the Westminster Parliament. Section 139(1)(a) of the Financial Services and Markets Act 2000 provides the FSA with the power to make rules which result in "clients' money being held on trust in accordance with the rules". However, subsection (3) reads:

> "In the application of subsection (1) to Scotland, the reference to money being held on trust is to be read as a reference to its being held as agent for the person who is entitled to call for it to be paid over to him or to be paid on his direction or to have it otherwise credited to him."

The impact of this, for trust law, is that there is yet further uncertainty, in Scots law, about the nature of a client–nominee relationship to which the FSA Handbook applies. It may be, though, that this will be rectified in the relatively near future: we were recently contacted by officials in the Treasury who are working on a forthcoming Bill changing the regulation of financial services, and there is the possibility that the Bill will address this issue. We have made it clear that our firm view is that Scots law in this area should be brought into line with English law, requiring client money held by a nominee to be held on trust.

5.8 Our view, supported by the consensus view at our *ad hoc* advisory group meeting and by responses to our original consultation, is that the relationship between a trustee and a person called a nominee should always be one of trust. This is implicit in the very name "nominee". In other words, any nominee described as such should in all cases be regarded as holding the relevant assets as trustee. This should not be capable of being altered by agreement between the parties. (This will apply whether the assets are shares or other moveable property or heritage.[15]) If, however, trustees wish to transfer trust assets to a third party, for investment or other purposes, and the relationship with the third party is intended to be contractual rather than one of trust, this should continue to be possible;[16] but in such a case the third party ought not to be called a nominee.[17] Agency is a common example of this kind of contractual relationship. The distinction drawn here is essentially terminological rather than substantive. Nevertheless, we think that it would clarify the legal position significantly if use of the term "nominee" were confined to cases where assets are held on trust rather than under a purely contractual arrangement.

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[14] See Appendix A for the letter. Financial services are reserved by Head A3 of Pt II of Sch 5 to the Scotland Act 1998.

[15] This is the existing position: see s4(1)(ea) and s4B(1)(a) of the 1921 Act.

[16] This is, of course, subject to the trustees' fiduciary and other obligations. If they transfer assets to a person in circumstances where it is customary to use a nominee, the trustees may become liable to the beneficiaries if that person becomes insolvent and the full value of the assets is not returned to the trustees.

[17] We are not to be understood as saying that the word "nominee" must not appear in the third party's name. The regulation of business names is a separate matter and we do not wish to change it. The point is that the third party's role cannot be described as one of nominee if a relationship other than a trust-based one is intended.

5.9 In order to ascertain wider opinion on this matter we ask the following question:

10. Do you agree with the view expressed in paragraph 5.8 above?

5.10 In the course of our work in this area a separate but related question has arisen: does a solicitor's firm hold client money on trust or in another way, for example as agent? We have already indicated that, in our view, the money is held on trust.[18] This is the view reached by the Scottish courts.[19] We also note that a trust-like device has been incorporated into the Dutch civil law to deal with money held by a notary, despite trusts generally not being incorporated into the legal system.[20] The reason is to protect the clients if the notary becomes bankrupt. Similar protection appears to us to be of central importance in Scotland. In order to gauge views as to whether this ought to be made explicitly clear we ask the following question:

11. Should it be set out in statute that client money held by a solicitors' firm (or other professional firm) is held on trust?

5.11 The scenario we considered in paragraph 5.8 is that in which trustees transfer assets to a nominee. That is the situation with which we are directly concerned. If a rule is framed in those terms, however, it may be unclear what impact (if any) it has when a nominee is used by a person who is not a trustee. In our view, the status of the transferor should be irrelevant, and a trust relationship should be established whenever a person called a nominee receives assets and holds or deals with them on behalf of the transferor. In view of the question we ask below about any practical impact which reforms in this area may have, we ask for views:

12. If you answer yes to question 10, should the rule apply regardless of whether the relevant assets were held by trustees immediately before being transferred to the nominee (as opposed to being held by a person in his or her own right)?

5.12 The final issue concerns the possible impact of any change on the market. From what we understand, there will be no effect at all on "in house" nominees, for the reasons we have already outlined. But we are uncertain about the outcome for commercial nominees. They have a clear profit motive, and we understand that there has been a move on the part of some of them away from regarding themselves as trustees in favour of establishing the relationship with the client on a more contractual basis. In this way, they seek to set up the relationship in a way which suits their commercial interests; in part, this may take them away from a strict client–trustee model.[21] It may be that their business model would require to be

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[18] See para 5.5 above. The Law Society of Scotland, whom we consulted for an initial view, is in agreement. In addition, we see no reason why this should not also apply to client money held by other professional firms.

[19] Eg *Jopp v Johnston's Tr* (1904) 6 F 1028 and *Council of the Law Society of Scotland v McKinnie* 1991 SC 355; 1993 SLT 238.

[20] See art 25 of the Law on the Notarial Profession and also Reinout Wibier, "Can a Modern Legal System Do without the Trust?", L&FMR 2011, 5(1), 37-45 and available at SSRN: http://ssrn.com/abstract=1677810.

[21] In saying this, we are aware that, even if the relationship is required by law to be that of trust, there is the possibility that matters will take a different course in practice. The Lehman litigation is a prime example, as Briggs J makes clear in paras 3-4 of his decision in *Re Lehman Brothers International (Europe) (In Administration)* [2009] EWHC 3228 (Ch):

"3. In an ideal world, the flawless operation of the scheme created by the CASS7 rules [ie the relevant rules of the FSA Handbook] would ensure first, that the clients' money could not be used by the firm for its own account and secondly, that upon the firm's insolvency, the clients would receive back their money in full, (subject only to

adapted slightly if the law clearly and unambiguously required a nominee described as such to hold assets on trust. We would welcome views on this matter, which will be helpful for us not only in formulating our recommendations but also in gauging any impact in practice which they may have.

13. What is the likely impact on the market of a rule requiring a nominee to hold on trust assets transferred to it by another person? Any supporting evidence would be welcomed. Would the impact be lessened if the rule were restricted to cases in which the transferor of the assets is a body of trustees?

Custodians

5.13 We consulted on this topic in our DP on Trust Administration.[22] Respondents generally agreed with our view that no change in the law was needed. We have also been told by our *ad hoc* advisory group that custodians are rarely used in practice nowadays and also that if assets require to be held in custody by a third party it is not uncommon for that third party to require title to be transferred to it – in which case the distinction between a custodian and a nominee is elided.[23] However, in the light of the questions we have asked in relation to nominees we think it appropriate to ask for views on custodians, to make sure that we have a complete picture. We therefore ask:

14. Do you consider the existing law relating to the custody of trust documents and assets to be satisfactory? If not, what changes should be made?

Consultation responses to our DP on Trust Administration revealed very little appetite to change the current law, and our *ad hoc* advisory group told us that where custodians are used, which is declining, they generally require title to be transferred into their name, making them all but a nominee for our purposes.

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the proper costs of its distribution) free from the claims of the firm's creditors under the statutory insolvency scheme. The rules would achieve those twin objectives by ensuring that, promptly upon receipt, client money was held by a firm as trustee, separately and distinctly from the firm's own money and other assets, and therefore out of the reach both of the firm (for the conduct of its business) and of the firm's administrator or liquidator upon its insolvency (for distribution among its creditors).
4. In the imperfect and hugely complex real world occupied by LBIE [Lehman] and its numerous clients, there has on the facts which I am invited to assume for present purposes been a falling short in the achievement of both of those objectives on a truly spectacular scale."

[22] At paras 3.32-3.33.

[23] The DCFR categorises this practice as transferring physical control of trust assets to a "storer": see Book X.-5:205 and, more generally, Book IV.C, ch 5 ("storage").

Chapter 6 Breach of trust

6.1 In our Discussion Paper on Breach of Trust[1] we discussed the issue of *intra vires* delictual breach of trust in Part 3, and the standard of care to be exhibited by a trustee.[2] We pointed out that the general rule in Scots law is that a trustee is required to exhibit "the same degree of diligence that a man of ordinary prudence would exercise in the management of his own affairs".[3] We further stated that there is some uncertainty as to whether trustees who act as such in the course of their business or have relevant special skills are expected to show a higher standard of diligence and knowledge than the basic objective standard of an ordinary prudent person.

6.2 We went on to suggest that a higher standard of care should be required of "professional" trustees, and that legislation would be required to achieve this as the existing position in Scots law was uncertain. We expressed the view that a minimum standard applicable to all trustees was necessary; without that beneficiaries would be at the mercy of lazy, ignorant or incompetent trustees. That minimum standard must be objective; a subjective standard, based on the way trustees would act in relation to their own private affairs would be potentially too low and would present great difficulties in determining whether a breach of trust had occurred. We considered various standards that were available, and favoured one that is used in South Africa: a trustee should use the same care and diligence as an ordinary prudent person would use in managing the affairs of others.[4] That formula seemed to us to emphasise the fact of trusteeship: trustees administer the trust estate not for themselves but for the beneficiaries. Conscientious people are generally more careful and diligent in relation to the affairs of others than they are in relation to their own, and would be likely to adopt a more cautious and careful approach with other people's property.

6.3 In relation to "professional" trustees, we pointed out that solicitors, accountants and banks put themselves forward for trusteeship on the footing that they offer a superior standard of service to that of untrained amateurs. It is therefore not unreasonable for the law to hold them to a higher standard. In such a case, the standard would be the appropriate professional standard of care: negligence would be established only if the trustee followed a course of action that no ordinarily competent member of that profession would have adopted if acting with ordinary care.[5] We considered a number of formulations of the duty used in other jurisdictions, and concluded that a higher, professional standard should only apply where the trustee acts in the course of business; in this respect we attached some significance to the formulation in section 1(1) of the Trustee Act 2000 in

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[1] Discussion Paper No 123. We refer to this as the "DP on Breach of Trust".
[2] See DP on Breach of Trust, paras 3.2-3.11.
[3] *Raes v Meek* 1889 16 R (HL) 31 at 33 per Lord Herschell; see also *Knox v Mackinnon* 1888 15 R (HL) 83 at 87 per Lord Watson; and *Tibbert v McColl* 1994 SLT 1227.
[4] Trust Property Control Act 1988, s 9(1): "A trustee shall in the performance of his duties and the exercise of his powers act with the care, diligence and skill which can reasonably be expected of a person who manages the affairs of another."
[5] *Hunter v Hanley* 1955 SC 200.

England and Wales.[6] We did not favour using the criterion of payment for the imposition of a higher standard of care; it was sufficient that a professional person acted in the course of his or her business, even if no remuneration were charged. In addition, in cases where a trustee is left a modest legacy or gift as a token of appreciation for services to be rendered, that should not result in any higher standard.

6.4 In the light of these considerations we made the following proposal:

"Unless otherwise provided by statute, in carrying out their trust duties –

(a) Every trustee should have to use the same care and diligence that a person of ordinary prudence would use in managing the affairs of others.[7]

(b) A trustee who acts as such in the course of his or her business or profession should in addition have to use any special knowledge or expertise that it is reasonable to expect of a member of that business or profession."[8]

6.5 Those who responded to our Discussion Paper agreed generally with the first of these proposals. They were divided on the second, however. One view was that Scotland should, broadly speaking, follow the English rule in section 1(1) of the Trustee Act 2000; it was suggested that major differences between the two systems could undermine the provision of professional trustee services in Scotland. Another view was that, if a trustee was appointed on the basis that he held himself out as having particular knowledge or expertise, the standard of a person having such knowledge or expertise should apply, whether or not he was acting in the course of a business. That is close to the rule in section 1(1)(a) of the English Act. Yet a third view was expressed by the Law Society of Scotland, who stated that it could become increasingly difficult to find persons willing to take on the burden of becoming a trustee unless obligations were kept to reasonable levels. This was particularly relevant to pension trustees and trustees of private trusts.

6.6 On discussing the consultation responses, we were concerned by two matters relating to professional people who act as trustees. First, it seemed to us to be very important not to discourage such persons from accepting office as trustees. There is evidence that the fear that trustees are subject to excessively onerous duties already discourages many people from acting as trustees. That fear is of course compounded by uncertainties about the present state of the law. Following on from those considerations, our second concern relates to the position of a trustee who happened to have professional qualifications but did not act as trustee in a professional capacity. Such trustees are commonly asked to provide professional advice on an informal basis, without proper instructions and without payment. This is an obvious hazard for such trustees, as the legal status of such advice will often be far from clear.

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[6] This section provides that a trustee:

"… must exercise such care and skill as is reasonable in the circumstances, having regard in particular –

(a) to any special knowledge or experience that he has or holds himself out as having, and

(b) if he acts as trustee in the course of a business or profession, to any special knowledge or experience that it is reasonable to expect of a person acting in the course of that kind of business or profession."

[7] This is largely in line with the provisions of the DCFR Book X.-6:101 and 6:102(1).

[8] DP on Breach of Trust, proposal 3; see likewise DCFR Book X.-6:102(2).

6.7 On the other hand, we are conscious that some types of professional trustees are frequently appointed on the basis that they offer a superior standard of service; this applies in particular to professional corporate trustees and banks' trustee departments. In some cases it may apply to solicitors or accountants, where, for example, they market their services as professional trustees. In the latter category of case, it seems to us to be appropriate to hold the trustee to a professional standard of service, namely that of a specialist professional trustee.

6.8 With other trustees, however, we are of opinion that they should be subject only to the general standard of care, ie the standard of care and diligence of a person of ordinary prudence managing the affairs of others.[9] That should apply whether or not the trustee is a member of a profession. Thus in the ordinary case of a solicitor who accepts office as a trustee his or her actings qua trustee should be subject only to the general standard of care. That would apply to informal legal or other professional advice given by such a trustee in the course of the administration of the trust. The higher, professional, standard of care would only apply to such a trustee if he were expressly instructed to provide professional advice to the trust. In this way, we think that the hazards arising from informal requests for professional advice can be reduced. This seems to us to be fair, because trustees are normally unremunerated, and it does not seem reasonable to expect a gratuitous trustee to employ full standards of professional diligence in a case where there are no proper instructions and no remuneration.

6.9 The position is obviously different if professional work is instructed by the trust. In that case it seems to us that the ordinary standard of professional skill and care should apply. In such a case there is obviously the possibility that the trustee providing the professional services will receive remuneration, but we would not regard remuneration as an essential criterion for such liability; instead, we think that the existence of professional instructions should be the criterion. We note further that, in cases where proper instructions are given, the trustees' professional indemnity insurance will normally operate. By contrast, it may well not cover advice that is given on an informal basis.

6.10 The other category of cases where a higher standard of care should in our opinion apply relate to trustees who provide professional trustee services and charge for those services. As we have remarked, such trustees usually market their services on the basis that they provide a superior standard of service. Because they are paid for acting as trustees, we think that they should be subject to the appropriate professional standard of care and skill.

6.11 We accordingly make the following proposal:

15. Unless otherwise provided by statute, in carrying out their trust duties –

(a) Every trustee should have to use the same care and diligence that a person of ordinary prudence would use in managing the affairs of others.

(b) An unremunerated trustee who has professional qualifications or business experience should be subject only to the foregoing duty

[9] See proposal 3(a) as set out in para 6.4 above.

unless he or she is instructed to provide professional or other specialised advice to the trust. In the latter event, the trust will be required to use any special knowledge or expertise that it is reasonable to expect of a member of his or her profession or business.

(c) A trustee who provides professional trust services and is remunerated for doing so should be required to exercise the level of skill and care that it is reasonable to expect of a member of his or her profession or business.

In addition, we would welcome comments on the very common situation where one of the partners in the firm of solicitors who act for the trustees is appointed a trustee. Would the foregoing proposals deal adequately with that situation?

Chapter 7 Jurisdiction of the court

Court's entitlement to interfere with trustees' discretion

7.1 We considered the role of the court in the administration of trusts in Part 5 of our Discussion Paper on Trustees and Trust Administration.[1] We first considered the extent to which the court should be entitled to interfere with trustees' discretion,[2] concluding that the existing law was satisfactory. In summary, the court will only interfere with the discretionary powers of trustees if it can be shown that trustees considered the wrong question, or did not properly apply their minds to the right question, or perversely shut their eyes to the facts, or did not act honestly or in good faith or acted unreasonably. We remain of the view that the existing law is satisfactory and that there is no need to recommend any legislation in this area. Our proposal that there should be no change to the law met with universal support from those responding to the consultation.

Court's power to give directions to trustees

7.2 We then considered the power of the court to give directions to trustees.[3] We reviewed three procedures of importance to trustees: the petition for directions under section 6(iv) of the Court of Session Act 1988, the special case under section 27 of the Court of Session Act 1988, and the action of multiplepoinding. We expressed the view that the current procedures seemed broadly satisfactory. In particular, the petition for directions provided a useful and relatively informal mechanism to give trustees advice on any administrative difficulties that they might encounter. We gave consideration, however, to whether a procedure should be introduced, akin to *Benjamin* orders in English law, whereby trustees can be authorised by the court to distribute the trust estate on a particular footing, for example, that a particular person predeceased the testator without issue.[4] Obtaining the authority of the court in this way protects trustees against personal liability if it later turns out that the true situation was not as presumed by the court. Such an order does not of itself affect the beneficiaries' rights, but merely provides immunity to the trustees. We also gave consideration to whether there is a need for a procedure to deal with contingencies.[5] It can happen that a trust estate must remain undistributed to the current beneficiaries because of a remote possibility that some other person will become entitled to it and the trustees are not prepared to take the risk of personal liability should the contingency arise. Special cases have been used in this area, and in some cases authority to distribute has been given where the contingency was extremely unlikely to occur. The Inner House has in fact been willing to authorise distribution in cases involving Lloyds Names on the basis that contingencies are too remote to prevent distribution.[6] We accordingly suggested that it would be useful to

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[1] Discussion Paper No 126. We refer to this as the "DP on Trust Administration".
[2] Ibid, paras 5.2-5.8.
[3] Ibid, paras 5.9-5.29.
[4] Ibid, para 5.25.
[5] Ibid, para 5.26. Contingencies take two main forms: those relating to contingent debts due by (or occasionally to) the trust estate and those affecting the future rights of beneficiaries. A good example of the former is found in the cases relating to Lloyds' Names, where the contingency is whether the estate's liability to indemnify a Lloyds syndicate will be called up as a result of insurance claims made against the syndicate in future. An example of the latter is a case where the distribution of the estate depends on survivance by one beneficiary of another.
[6] *Neilson's Exrs, Petrs*, Extra Division, 25 June 2002, unreported.

introduce a procedure giving the courts an express power to authorise distribution of the trust estate and relieve the trustees from personal liability. Such a power would be framed in general terms and would be available where it was very likely but not certain that a particular event had or had not happened or where there was some remote chance of the present beneficiaries' entitlements being defeated by a future event. We therefore invited views on the following proposal and question:

> "(1) The court should be empowered, on application by the trustees or others with an interest in the trust estate, to grant an order authorising the trustees to make payments from the estate on the footing that a specified event has or has not happened or will not happen. The court may make an order subject to such conditions as it thinks fit.
>
> (2) Trustees who act in accordance with the authorising order should not be personally liable should the footing on which the court made the order turn out not to be correct, unless they concealed facts or acted fraudulently in the application. The freeing of the trustees from personal liability should not prejudice any right of the true beneficiaries to recover the trust estate from those to whom it had been distributed.
>
> (3) Should any other changes be made to the law or procedure relating to petitions for directions or special cases, and if so what changes should be made?"[7]

7.3 With the exception of the Faculty of Advocates, all of those who responded to our consultation on these matters were in favour of the proposals found at (1) and (2) above. The Faculty of Advocates suggested that at present trustees who are of the view that a contingency is so remote as to be not worth any serious consideration may, if they act on the basis of evidence and advice, defend a claim for breach of trust under section 32 of the Trusts (Scotland) Act 1921. The present proposal would, in their opinion, enable trustees to evade their obligation to act without negligence towards the trust's creditors or potential creditors, in circumstances where a contingency was known to exist, albeit its gravity was uncertain.

7.4 In view of the general tenor of the responses, we are inclined to favour the proposals that we made. So far as the Faculty's point is concerned, it seems to us that the court would consider as a matter of course whether there was any likely prejudice to actual or potential creditors, and would take that into account in deciding whether to grant the application. Clearly the degree of likelihood that a creditor will emerge can vary enormously, and if need be the court could obtain a report on the level of risk in the case under consideration. That is in fact what happened in the early cases on Lloyds Names.

7.5 The trustees and trust administration group of the Law Society made a number of interesting points in response to the foregoing proposals and question. They stated that the major complaint in relation to court proceedings is the time that it takes to obtain a decision. The group had considered the possibility of establishing some method of expediting trust cases. While they would be unlikely to fall within the remit of the fast track procedures available in the commercial court, in some trust cases, especially those involving pension

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[7] DP on Trust Administration, question 22.

funds, there is frequently a commercial impact. Nevertheless, there is a commercial requirement for pension cases to be dealt with expeditiously. Further concerns were expressed that there was a lack of sufficient understanding of trust law at shrieval level. It was suggested that a possible solution would be to create a procedure similar to the commercial court with similar case management procedures. In fact case management procedures are in practice used in trust cases in the Outer House, albeit on an informal basis. We think, however, that it would be useful to have those procedures formalised to some extent in the Rules of Court. We accordingly invite comments on the following proposal:

16. Provision should be made in the Rules of Court for case management procedures in trust cases in the Outer House. These should be modelled on the existing procedures used in the Commercial Court.

Court's power to confer powers in relation to a trust

7.6 We then considered the question of whether the court should be empowered to confer additional administrative and managerial powers in relation to a trust.[8] At present trustees' powers of administration are partly statutory and partly conferred by the trust deed. Sections 3 and 4 of the Trusts (Scotland) Act 1921 grant trustees a number of administrative powers. Those in section 4 are permitted provided that they are not "at variance with the terms or purposes of the trust". Section 5 of the Act empowers the court to authorise the trustees to do any act specified in section 4 notwithstanding that it would be at variance with the terms and purposes of the trust, provided that it is satisfied that carrying out the act would be expedient for the execution of the trust. In practice, however, modern trust deeds generally confer extremely wide management powers. This renders the statutory powers redundant in most cases. Moreover, investment powers are now essentially unrestricted as a result of the amendments effected to section 4 by the Charities and Trustee Investment (Scotland) Act 2005. We took the foregoing developments into account in Part 4 of our DP on Trust Administration, where we proposed that, unless the trust deed provides otherwise, trustees should have the same wide powers of management in relation to the trust estate that a capable person has in relation to his or her own property. If that were implemented, the significance of the powers of the court would be substantially reduced.

7.7 We then reviewed the current law, and in particular the power of the court under its *nobile officium* and the power to vary trust purposes under the Trusts (Scotland) Act 1961. The latter jurisdiction is dealt with further in our Report on Variation and Termination of Trusts;[9] we intend to incorporate the Bill annexed to that Report into the Trusts Bill annexed to our forthcoming report on the law of trusts generally. In addition, in our Discussion Paper on the Accumulation of Income and Lifetime of Private Trusts[10] we proposed a new jurisdiction in the court to alter trust purposes where there had been a material change of circumstances. That proposal met with a favourable response on consultation, and it is our intention to incorporate it into our forthcoming report.

7.8 Against that background, we nevertheless expressed the view in our DP on Trust Administration that it may still be necessary for the court to provide for additional administrative and managerial powers. Useful powers might have been inadvertently

[8] Paras 5.30-5.38.
[9] Scot Law Com No 206.
[10] Discussion Paper No 142. We refer to this as the "DP on Accumulation".

omitted, or powers that seemed unnecessary when the trust was set up might have been rendered necessary by changes in the legal or factual background. The existing jurisdictions were not wholly satisfactory. In particular, the jurisdiction under the *nobile officium* is not clear, and the variation of trusts jurisdiction is designed to deal principally with the variation of trust purposes rather than the enlargement of powers. In addition, that jurisdiction requires the consent of all beneficiaries who are living and capax. Our proposed jurisdiction for the alteration of trust purposes to deal with a change of circumstances is also limited in certain respects. It is designed to deal with the purposes of the trust rather than its administrative powers. In addition, it requires that a change of circumstances should be demonstrated, and we intend to recommend that, unless the trust deed provides otherwise, the jurisdiction can only be exercised 25 years after a trust has been created. For these reasons neither the variation of trust jurisdiction nor the jurisdiction to alter trust purposes provides a satisfactory means of conferring additional powers of an entirely administrative nature.

7.9 Against that background, we made the following proposal:

> "(1) The court should be empowered, on application by the trustees, to grant an order conferring additional administrative and managerial powers in relation to the trust estate on them, if satisfied that the order would be of benefit to the future administration of the trust estate.
>
> (2) The application should be intimated to all the beneficiaries, who would have an opportunity to object. An order should be capable of being granted notwithstanding the objections of some beneficiaries.
>
> (3) The court should have power to attach such conditions to the order as it thinks fit."[11]

On consultation, those proposals met with universal support.

7.10 The significance of the totality of the foregoing proposals (those found at paragraphs 7.2 and 7.9 above) is that they reveal a clear need for a jurisdiction in trust cases that is straightforward and efficient.

Jurisdiction of the Court of Session and Sheriff Court

7.11 In our DP on Trust Administration we reviewed the existing jurisdiction of the Court of Session and expressed the view that it should be possible for the sheriff courts to play a greater role in trust litigation, and that within the Court of Session trust business could usefully be re-directed from the Inner House to the Outer House.[12] We made the following proposal:

> "(1) The Outer House of the Court of Session and the sheriff courts should have concurrent jurisdiction in relation to applications:
>
> (a) under the Trusts (Scotland) Act 1921;

[11] DP on Trust Administration, proposal 23.
[12] See its Pt 5D.

(b) relating to endowments under Part VI of the Education (Scotland) Act 1980;

(c) dealing with the administration of trusts or the office of trustee, including *cy-près* applications; and

(d) by trustees for directions in relation to their administration of the trust.

(2) Petitions under section 1 of the Trusts (Scotland) Act 1961 (variation of trusts) should be presented to the Outer House rather than, as at present, to the Inner House.

(3) The part of section 26 of the Trusts (Scotland) Act 1921 which requires the Inner House to settle a draft scheme by the Lord Ordinary for administration of a charitable or permanent endowment should be repealed."[13]

7.12 Since December 2004, when our DP on Trust Administration was published, important developments have occurred in this area. First, the Scottish Civil Courts Review, carried out by Lord Gill and published in September 2009, proposed very major changes to the allocation of work among the courts in Scotland. In particular, it is proposed that the privative jurisdiction of the sheriff courts should be greatly increased in actions for damages and payment. The transfer of this business will be accompanied by a major reorganisation of the courts, in particular the sheriff courts, to enable new case management procedures to be used there. We note further that the Report recommends[14] that the Court of Session should retain exclusive jurisdiction in relation to more complex corporate matters, patents, exchequer cases, actions under the Hague Convention and devolution issues. Nothing is said expressly about trusts. Nevertheless, it is clear that trusts involve issues of some complexity, requiring a specialised knowledge of the law, and in that respect they are analogous to corporate and exchequer cases.

7.13 Secondly, under the Charities and Trustee Investment (Scotland) Act 2005, applications for reorganisation of a charitable trust are to be made only to the Office of the Scottish Charities Regulator ("OSCR"). Neither the Court of Session nor the sheriff court has any jurisdiction. The original draft of the Bill put forward for consultation by the Scottish Executive in June 2004 provided, at section 56, that applications for re-organisation of a charitable or public trust might be made to OSCR, to the Court of Session, or to the sheriff court. In our DP on Trust Administration[15] we noted that section 56 of the draft Charities and Trustee Investment (Scotland) Bill continued what was perceived as the current policy of extending jurisdiction to the sheriff courts by subordinate legislation. For reasons we explain below, the policy that underlay section 56 of the Bill was, however, departed from in the version of the Bill introduced to Parliament, and section 39 of the resulting Act provides that applications for reorganisation are to be made only to OSCR or, where OSCR itself is the applicant, to the Court of Session.[16] The reason for the change in policy is explained in the policy memorandum that accompanied the 2005 Act when it was introduced as a Bill. Paragraph 71 of that memorandum is as follows:

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[13] DP on Trust Administration, proposal 24.
[14] At ch 4, para 138.
[15] At para 5.29.
[16] See s 40 of the Charities and Trustee Investment (Scotland) Act 2005. Sections 39 and 40 have been subsequently amended (by s 124 of the Public Services Reform (Scotland) Act 2010) but not in a way which materially affects the present issue.

> "The consultation version of the draft Bill set out a common graduated regime for the reorganisation of all charities and public trusts. Hence a body wishing to reorganise would have had to apply to either OSCR, the Sheriff Court or the Court of Session, depending on its size. However, in response to comments from the court services and in a move to simplify the proposed regime even further for charities, the Executive has decided that OSCR, rather than the courts, should consider and determine all reorganisation schemes, whatever their size. Hence the Bill now provides that charities not having a power to amend their constitution themselves will have to apply to OSCR for approval of a proposed reorganisation scheme. This simplifies the regime, especially for the larger charities which would otherwise have had to apply to the Court of Session. Decisions on reorganisations by OSCR may be appealed to the Scottish Charity Appeals Panel by applicants, with a further appeal to the Court of Session."[17]

On reconsidering this issue, we think that there is considerable force in the arguments that simplification is important and that there should, generally speaking, be a single court to which all applications relating to trusts are made.

7.14 Thirdly, some of the jurisdictions contemplated in our discussion papers confer a major discretion on the court; this applies in particular to the trust variation jurisdiction[18] and the proposed jurisdiction to alter trust purposes to deal with a change in circumstances.[19] In these cases it is essential that the court's discretion should be exercised in a consistent and principled manner in all cases. That can best be achieved by allocating all such cases to a single court, which for practical reasons can only be the Court of Session. This is recognised in our Report on Variation and Termination of Trusts,[20] where we recommended that petitions for approval of an arrangement varying or terminating private trusts should be presented in the Outer House, subject to a power to remit the application to the Inner House in any case of particular difficulty.[21] It is further recognised in our DP on Accumulation,[22] where we suggested that the proposed jurisdiction to deal with a change of circumstances should only be available in the Court of Session.

7.15 Fourthly, court procedures have developed substantially in recent years. We have already mentioned the fact that trust applications in the Outer House are the subject of case management procedures, albeit on an informal basis. The "electronic revolution", involving the use of email communication in particular, makes it easy for solicitors outside Edinburgh to make applications to the Court of Session without the difficulty and expense of going through Edinburgh correspondents. Electronic procedures have been significantly developed, especially in the commercial court, and we think that similar developments could easily take place in relation to trust applications. This would be particularly useful if the majority of trust applications were transferred to the Outer House; that would enable a designated clerk to be appointed who could develop procedures modelled on those used by the commercial clerks.[23]

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[17] Available at http://www.scottish.parliament.uk/business/bills/32-charitiesTrustee/b32s2-introd-pm.pdf.
[18] See our DP on Variation and Termination of Trusts (DP No 129) and Report on Variation and Termination of Trusts (Scot Law Com No 206).
[19] See our DP on Accumulation, esp Pt 5.
[20] At paras 5.43-5.44.
[21] Recommendation 14.
[22] At para 5.34 and recommendation 6.
[23] In practice, Outer House trust applications tend to be dealt with by one of the designated commercial clerks.

7.16 Apart from the foregoing developments, we are conscious that trust law is a technical and specialised area. It requires considerable expertise not merely at a judicial level but among those who present the cases in court, and also among persons who may be appointed as reporters in cases where the facts require investigation. We are doubtful whether in practice these requirements would be satisfied in every sheriff court. We considered the possibility of having a small number of designated trusts sheriffs, who could move around the country as necessary to deal with trust applications. It seemed to us, however, that this was impracticable. First, arranging the movements of such sheriffs would involve a considerable amount of work, and the clarity and simplicity that were thought desirable in relation to charitable and public trusts[24] would be largely absent. Secondly, the hearings in trust applications are frequently extremely short, and it would make little sense to have a sheriff make a substantial journey to hear an application that might take only 15 or 20 minutes.

7.17 In the foregoing circumstances, we are now of opinion that the best scheme for trust litigation is as follows. First, jurisdiction in all trust applications should be exercised by the Court of Session. Secondly, all such applications should normally be dealt with in the Outer House, where they would be heard by a designated trust judge (as exists at present). Thirdly, case management procedures modelled on commercial court procedures should be used, as proposed in Proposal 16 at paragraph 7.5 above. As part of a modern, efficient procedural system, we think that in the majority of trust cases it should not be necessary to obtain a report. These are generally perceived as expensive and productive of delay. In fact we understand that the current procedure in the Outer House when dealing with trust applications is not to require a report unless it is plainly necessary to ascertain doubtful facts, and we would envisage that this practice would continue. Fourthly, a system should be developed whereby trust applications to the Court of Session may be made electronically by solicitors anywhere in Scotland. Fifthly, we think that the petition for directions is a useful procedure, a view that was confirmed in our earlier consultation.[25] We accordingly think that a simple, non-technical procedure should be devised which allows trustees or other interested parties to raise such proceedings. They would of course be heard in the Outer House, subject to the normal right to reclaim in the Inner House.

7.18 We would envisage that the foregoing proposals would apply to all the categories of application referred to in Proposal 24 in our DP on Trust Administration.[26] Finally, we think that no change should be made to the law relating to special cases; in cases where that is the appropriate procedure, one of its advantages is that an issue of law can be taken directly to the Inner House. We would envisage, however, that the great majority of trust applications on doubtful questions of law would take the form of a petition for directions.

7.19 Against the following background, we make the following proposal:

17. (a) The Outer House of the Court of Session should have exclusive jurisdiction in relation to applications:

(i) under the legislation replacing the Trusts (Scotland) Act 1921;

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[24] See para 7.14 above.
[25] See para 7.2 above.
[26] Set out in para 7.11 above.

(ii) relating to endowments under Part VI of the Education (Scotland) Act 1980;

(iii) dealing with the administration of trusts or the office of trustee, including *cy-près* applications; and

(iv) for directions in relation to the administration of a trust.

(b) Petitions under section 1 of the Trusts (Scotland) Act 1961 (variation of trusts) or any replacement for that legislation should be presented to the Outer House rather than, as at present, to the Inner House.

(c) The rules of the Court of Session should provide that in all such categories of case the Lord Ordinary has power to remit the application to the Inner House in any case of particular difficulty; and that where appropriate a reclaiming motion against the Lord Ordinary's decision should be competent.

(d) The part of section 26 of the Trusts (Scotland) Act 1921 (or any replacement for that legislation) which requires the Inner House to settle a draft scheme by the Lord Ordinary for administration of a charitable or permanent endowment should be repealed.

(e) A simple non-technical procedure should be devised whereby applications relating to trusts and their administration may be made by trustees or by any other interested party. Such applications would be heard in the Outer House, with the possibility of reclaiming to the Inner House.

We do not think it necessary to make a formal proposal in relation to the use of electronic communications and other devices in relation to Outer House trust applications; we think that these can be developed as appropriate by the Court of Session. Their utility is very obvious.

Chapter 8 *Ex officio* trustees

Scope of our previous consultation

8.1 We dealt with the appointment, resignation and removal of trustees in Part 4 of our Discussion Paper on Trustees and Trust Administration.[1] In that Part, we considered the position of an *ex officio* trustee. At that time, we thought that uncertainty existed as to whether an *ex officio* trustee could assume, or take part in the assumption of, new trustees.[2]

8.2 We have considered the position of *ex officio* trustees in more depth following reflection upon the responses received to our original consultation, and we have concluded that the legal position does require clarification. Indeed we think that such uncertainty might be wider than the issues originally addressed, namely the *ex officio* trustee's role in the assumption of new trustees.

8.3 All responses to our consultation bar one were supportive of clarification of the law in this area, to provide that *ex officio* trustees can assume new trustees in the same way as any other trustees.

8.4 We note, however, that the responses received on this issue have indicated further problems surrounding the use of *ex officio* trustees in practice. We think that these problems might be usefully addressed in our forthcoming report, and we are therefore keen to gather consultees' views on whether further recommendations for reform are merited.

What are *ex officio* trustees?

8.5 *Ex officio* trustees feature in a large number of trusts, where the truster has provided the holder of a certain office to be an appropriate trustee. The holder of that particular office from time to time then acts as trustee in accordance with the terms of the trust deed. Examples of *ex officio* trustees may include the Principals of or other officials in Scottish Universities, sheriffs and local holders of religious office. In such cases, the trust deed will provide that the trust is to be administered by the holder of the office for the time being, rather than the individual incumbent at the time of settlement.

8.6 Thus, unlike ordinary trustees, death of the individual trustee him or herself does not relieve the officeholder of the duties incumbent on the trustee. The duties of the trustee pass instead to the successor in the office and that new office holder will be a trustee of the trust, although it is open to that individual to decline to accept the trusteeship if he or she does not wish to act as trustee.[3] While resignation and removal of the individual is

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[1] Discussion Paper No 126, para 4.4. We refer to this as the "DP on Trust Administration".

[2] *Vestry of St Silas Church v Trs of St Silas Church* 1945 SC 110; *Winning and others (Balnagowan Trs) Petrs* 1999 SC 51.

[3] See Menzies, *The Law of Scotland affecting Trustees* (2nd ed, 1913), para 98: "Even a trustee nominated *ex officio* is not bound as such to accept the trust. The only approach to authority on the point is a *dictum* of Lord Justice-Clerk Hope [in *Shepherd v Hutton's Trs* (1855) 17 D 516 at 520] to the effect that 'no minister is bound to act as a trustee' *ex officio*, but the obvious absurdities to which the opposite proposition would lead are sufficient to account for the want of authority."

unproblematic, it is not clear at present how the office itself can be removed from the trust deed.

8.7 It has become clear to us that the use of *ex officio* trustees can create problems. Often the offices prescribed as *ex officio* trustees will involve substantial workloads in themselves, and the duties attendant on the *ex officio* trusteeship may be an unwarranted burden. In an extreme case the duties may simply not be performed. In such a case, while the trustee can be said to exist, the trust may be bereft of effective administration until a new and perhaps more willing successor takes office. It is clearly undesirable that trust estates should be neglected in this way. Moreover, from time to time, offices may disappear, for example through dissolution or merger. In such cases, the trust can be left without a trustee where it is administered only by *ex officio trustees*, with no other trustees involved. The result may be a desire on the part of those interested in the trust estate to remove current and future *ex officio* office-holders from trustee duties. It is at present unclear how this can be achieved.

Removal of *ex officio* trustees: the current law

8.8 We note that there are currently three routes, none perhaps entirely satisfactory, which may provide a solution in cases such as those described above. Each applies to different categories of trust.

8.9 In cases involving public trusts, a *cy-près* petition may be submitted to the Court of Session. In cases involving private trusts, a trust variation may be sought to remove the trustee concerned. In relation to the third category, however, that of charitable trusts, an anomaly now exists.

8.10 As a result of the Charities and Trustee Investment (Scotland) Act 2005 application for removal of an *ex officio* is made to the Office of the Scottish Charities Regulator (OSCR). Removal of an *ex officio* trustee can be achieved through notification to OSCR under the terms of section 17, a provision relating to changes in the trustees of a charity. It appears therefore there is available a relatively speedy and streamlined route to achieve removal of the *ex officio* trustee, by comparison with the more onerous methods required by other public and private trusts, as noted above.

Problems in the current law

8.11 While *prima facie* it appears Scots law has developed solutions to deal with the problems caused by the inability or unwillingness of *ex officio* trustees to act or the disappearance of their office, uncertainty continues to exist in this important area of trust management and administration. While the remedies noted above will be successful in removing the person occupying the office from the position of trustee, it is not clear how the office itself may be removed from its position in the trust.

8.12 For charitable trusts, we understand that OSCR will require the trustee him or herself to resign personally. This is unproblematic, and adheres to the general principle that no one should be forced to be a trustee against his or her will. It is not clear, however, how the office itself can be taken out of the trust. It appears that it will fall to the body which supplies the office to have itself removed from the trust deed (presumably on application to OSCR). This procedure is in itself perhaps unnecessarily cumbersome and duplicative. Of more

concern is the fact that the statutory basis for this is not clear under the 2005 Act, and the (limited) practice thus far seems to have grown up on a discretionary basis. Despite its inelegance however, it is capable of providing a solution for charitable trusts. In the case of a public trust, a similar result could be reached using the *cy-près* jurisdiction, provided that it can be demonstrated that it is plainly expedient that holders of the selected office should not continue to act as trustees. In this respect the court would have to be persuaded that it is not just the present incumbent who is in difficulty; it is all holders of the office in the foreseeable future. In the case of private trusts a similar result could probably be reached using trust variation jurisdiction, but the matter is not entirely clear. In any event, all of these are relatively cumbersome procedures.

Proposals for reform

8.13 In light of the difficulties noted above, a statutory scheme providing a power for the removal of *ex officio* trustees may be merited. Such a power might apply both to the office itself and to any particular holder of that office. We envisage the power would provide two options: first, the removal of the specified office from the trust deed itself and, secondly, the replacement of the individual *ex officio* trustee and the nomination of a replacement for his or her duties as a trustee (essentially, a power of delegation).

8.14 Such a provision would be advantageous to clarify the current law, and to provide greater certainty in relation to *ex officio* trustees. Trusts with *ex officio* trustees, especially those who struggle to devote sufficient time to the trust's management, may find it helpful to have a quick, simple and affordable method of either removing the designated office or replacing the relevant office-holder by passing the duties of the trustee to a nominated replacement. This latter option would be particularly advantageous where the *ex officio* trustee concerned is unable to fulfil his or her duties, but nonetheless the office concerned would like to maintain its links with the administration of the trust. For example, the Principal of Edinburgh University may be unable to devote sufficient time to acting as *ex officio* trustee in a trust for the awarding of legal scholarship study awards. The University would like to maintain links with the trust, and consequently would exercise the power to delegate the trustee duties to a nominated representative instead, eg the Head of the Law School at Edinburgh University.

8.15 It is possible, of course, that the scope and severity of the problems identified above have been exaggerated, and that to provide for such a power in statute is unnecessary. In seeking to ascertain the need for reform, we would be grateful for views on how wide an impact such a power might have.

8.16 In formulating a new statutory power addressing the management of *ex officio* trustees, consideration might also be given as to whether it is appropriate to provide a general power in relation to *ex officio* trustees for all three categories of trust in Scotland, or whether the three categories should be differentiated. As a preliminary matter, we think that charitable trusts may benefit from the continued oversight of OSCR, and therefore any power to remove *ex officio* trustees in charitable trusts might therefore be best effected through an amendment to section 17 of the 2005 Act. A new general statutory power could then be made applicable to public and private trusts. This would result in a more streamlined and coherent structure to the law as a whole, with the procedure for all three categories of trust being broadly similar, and based on the same underlying principles of expediency and utility. The only differentiation between the three categories of trust would

be OSCR retaining jurisdiction over charitable trusts, while the power in relation to public and private trusts would be exercised by the courts. A strong argument can be made that removal of an office as trustee should be closely monitored by the courts or OSCR, if the truster has specifically nominated that office in the original trust in order to achieve his or her chosen trust purposes. We would be grateful for views on this aspect of the proposed reform.

8.17 We therefore ask:

18. How common are *ex officio* trustees in Scottish trusts? To what extent are problems involving *ex officio* trustees common in the administration of trusts? Have consultees experienced issues surrounding the resignation or removal of the office of the *ex officio* trustee?

19. Are consultees in favour of a new statutory power in relation to non-charitable trusts to allow for (i) the removal of an office as trustee (where the office-holder is an *ex officio* trustee); (ii) the replacement of such an office with another office, the holder of which is to act as an *ex officio* trustee; and (iii) a power for an *ex officio* trustee to resign in favour of a nominated replacement individual or office-holder?

20. If so, are there any reasons for such a statutory power to differentiate between public/private and charitable trusts, except to the extent that the power would be exercised by the courts, and OSCR respectively?

21. Are there are any other issues surrounding *ex officio* trustees which the Commission might usefully address?

Chapter 9 Powers of advancement

Background and current law

9.1 The Discussion Paper on Trustees and Trust Administration[1] made proposals in relation to the advancement of capital by trustees to beneficiaries.[2] In brief, we proposed the replacement of the current rules on advances with a new, wider, statutory power.

9.2 In many cases an express power of advancement is contained in the trust deed. In the absence of such a power, there are currently two methods by which advances of capital from a trust estate can be made to beneficiaries under Scots law. The common method is an application under section 16 of the Trusts (Scotland) Act 1921. In addition, application to the Court of Session for exercise of its *nobile officium* is also competent.[3]

9.3 Section 16 of the 1921 Act provides the Court of Session with a power to authorise trustees to advance capital to beneficiaries. It reads:

> "The court may, from time to time under such conditions as they see fit, authorise trustees to advance any part of the capital of a fund destined either absolutely or contingently to beneficiaries who at the date of the application to the court are not of full age, if it shall appear that the income of the fund is insufficient or not applicable to, and that such advance is necessary for, the maintenance or education of such beneficiaries or any of them, and that it is not expressly prohibited by the trust deed, and that the rights of such beneficiaries, if contingent, are contingent only on their survivance."

9.4 The Court of Session may also grant authority to trustees to advance capital through exercise of its *nobile officium*. Generally, this method of advancing capital to beneficiaries is used only where an application under the 1921 Act is incompetent, for example, where the beneficiary concerned is of full age. It was noted in the DP on Trust Administration that exercise of the *nobile officium* is also limited to situations where there has been some unforeseen change in circumstances, and where an advance of capital is necessary for the maintenance or education of the beneficiary concerned.[4]

Criticisms of the current law

9.5 In the DP on Trust Administration, we considered that the current rules on advances of capital were unduly restrictive for a number of reasons:

- Section 16 of the 1921 Act limits advances of capital to beneficiaries who are not of "full age". We noted that this was restrictive: adult and in particular elderly

[1] Discussion Paper No 126, 2004. We refer to this as the "DP on Trust Administration".
[2] A power of advancement is a power in trustees to pay capital to a beneficiary before his or her share vests or becomes payable.
[3] See our DP on Trust Administration, paras 6.2-6.9.
[4] Ibid, para 6.6.

beneficiaries may need advances of capital if they are unable to work or have insufficient income of their own.[5]

- Section 16 of the 1921 Act is also limited by purpose: advances of capital are available *only* for "the maintenance or education" of beneficiaries. We expressed concern that this was also too restrictive, noting that there are other reasons for which a beneficiary may require an early capital payment, such as the setting up or expansion of a business or, in the case of an elderly beneficiary, money to make alterations to a home.[6]

- The 1921 Act requires an advance of capital to be "necessary". We considered that this standard was too high, and was out of step with the law in other jurisdictions such as England and Wales.[7]

- The 1921 Act allows advances to contingent beneficiaries but only if their rights to capital are contingent only upon their survivance. We noted that the current provision is limited to a greater extent than its counterpart in England and Wales, where advances to any beneficiary entitled to capital may be made where his or her interest is contingent upon an event other than survivance, such as marriage or graduation.[8]

9.6 In addition to the particular limitations of the 1921 Act, both facets of the current law require court authorisation before advances of capital may be made. We considered this to be limiting: requiring applications to the court could be off-putting where the amount to be advanced is modest. It is also arguable that trustees are in a better position than the courts to assess the needs of particular beneficiaries.[9] Having said that, it was noted that Scots law, unlike the law in England and Wales,[10] does not require the consent of any person who has a prior life or other interest in the trust estate, and who might be prejudiced by an advance before such an advance can be made.

Proposals for reform

9.7 In light of the restrictions of the current law, we considered that reform was necessary. Proposals for a new, wider, statutory power, which would replace section 16 of the 1921 Act, and render resort to the *nobile officium* redundant, are therefore made at paragraph 6.19 of the DP on Trust Administration. These include a power for trustees to place the sum advanced in a new trust for the beneficiary.[11] We also proposed that if power to advance capital was to be handed from the court to trustees, all those with prior interests in the trust capital should be required to consent in writing.[12] Where a person with a prior life

[5] Ibid, para 6.11.
[6] Ibid, para 6.12.
[7] Ibid, para 6.14.
[8] Trustee Act 1925, s 32.
[9] Ibid, para 6.16.
[10] Trustee Act 1925, s 32.
[11] DP on Trust Administration, proposal 26(2). While such a power has been held to exist in England and Wales, it has never been recognised in Scots law.
[12] Ibid, proposal 26(1)(d).

or other interest is incapable of giving consent, or is withholding consent unreasonably, the court may still be called upon to authorise an advance.[13]

9.8 Alongside the proposals for a new statutory power, we asked consultees whether such a power should be limited to a specific proportion of the value of the beneficiary's prospective share.[14] At present, Scots law does not impose a limit on the amount of capital that may be advanced to a beneficiary, a practice which differs from other jurisdictions. In England and Wales, for example, a beneficiary may only receive up to one half of his or her share of the trust estate. Greater advances cannot be made, even if the trust estate increases in value.

Consultation responses

9.9 Our proposals met with general approval on consultation. The majority of consultees favoured the replacement of section 16 of the 1921 Act with a new power to advance capital, along the lines suggested at paragraph 6.19 of the DP on Trust Administration. Although some minor reservations were expressed on specific aspects of the proposals, there was general consensus that reform of this area of trust law was desirable.

9.10 Despite there being general agreement with the proposals, there were mixed responses to the question of whether there should be a cap on the proportion of a beneficiary's share which might be advanced. Suggestions for a cap ranged from one third of the value of the beneficiary's share to no cap at all. The Law Society considered that a cap could assist trustees in resisting excessive requests for advances from beneficiaries, while other consultees thought that maximum flexibility, i.e. no cap at all, should be the default position.

Further proposals

9.11 We remain of opinion that the law on advances of capital is unduly restrictive, and should be reformed. Nevertheless, we are concerned that, if enacted, the proposals in the DP on Trust Administration could be too wide in that they would confer an unlimited power upon trustees to favour some beneficiaries at the expense of others without court approval. That would be acceptable if it were the considered wish of the truster. As a default position, however, we think that an unrestricted power may go too far. We accordingly think that there is scope for limited further consultation on a slightly altered version of our proposals.

9.12 Comparative research has proved very useful in this area. In particular, the provisions relating to advances of capital found in England and Wales and in Australian jurisdictions have provided useful comparators. In England and Wales, unless the trust deed stipulates otherwise, trustees have the power to advance up to one half of the presumptive or vested share or interest of a beneficiary to that beneficiary for his or her "advancement or benefit".[15] If the beneficiary is or becomes absolutely and indefeasibly entitled to a share in the trust property, the money advanced will be taken into account as part of the overall share

[13] Ibid, proposal 26(3).
[14] Ibid, question 26(4).
[15] Trustee Act 1925, s 32.

received.[16] The English statutory power of advancement has now been in existence for 85 years and is, we understand, well regarded.[17]

9.13 In Australia, default statutory provisions authorising the advance of capital have been enacted for each of the states and territories. Most of these closely follow the scheme laid down in section 32 of the Trustee Act 1925 in England and Wales. All of those provisions limit the amount that can be advanced to a beneficiary. In some states the amount that may be advanced is limited to one half of the beneficiary's prospective share,[18] while in others it is stipulated that one half of the beneficiary's share or $2000, whichever is greater, may be advanced.[19] In Queensland and Western Australia, in addition to capping the amount which may be advanced, trustees may impose conditions as to repayment, payment of interest, or the giving of security. Trustees also have the power to waive such conditions or to release the obligations undertaken therein at any time.

9.14 We are particularly attracted by the provisions in Queensland and Western Australia,[20] which not only cap the amount of trust capital which can be advanced but also

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[16] Trustee Act 1925 s 32(1)(b).

[17] *Underhill and Hayton: Law of Trusts and Trustees*, David Hayton, Paul Matthews, Charles Mitchell (eds) (18th ed, 2010) states, at para 63.2, that the statutory power represents the power that was previously inserted in well drafted settlements.

[18] Australian Capital Territory: Trustee Act 1925, s 44; New South Wales: Trustee Act 1925, s 44; South Australia: Trustee Act 1936, s 33A; Tasmania: Trustee Act 1898, s 29.

[19] Queensland: Trusts Act 1973, ss 62-63; Northern Territory: Trustee Act, s 24A; Victoria: Trustee Act 1958, s 38; Western Australia: Trustees Act 1962, s 59.

[20] Sections 62 and 63 of the Trusts Act 1973 (QLD) provide:

"62 *Power to apply capital for advancement etc*.

(1) Where under a trust a person is entitled to the capital of the trust property or any share thereof, the trustee, in such manner as the trustee in the trustee's absolute discretion thinks fit, may from time to time out of that capital pay or apply for the maintenance, education (including past maintenance or education), advancement or benefit of that person, an amount not exceeding in all $2000 or one-half that capital (whichever is the greater) or with the consent of the court an amount greater than that amount.

(2) The power conferred by this section may be exercised whether the person is entitled absolutely or contingently on the person attaining any specified age or on the occurrence of any other event, and notwithstanding that the interest of the person so entitled is liable to be defeated by the exercise of a power of appointment or revocation, or to be diminished by the increase of the class to which the person belongs.

(3) The power conferred by this section may be exercised whether the person is so entitled in possession or in remainder or in reversion.

(4) Any money so paid or applied shall be brought into account as part of the share in the trust property to which the person is or becomes absolutely or indefeasibly entitled.

(5) No payment or application pursuant to this section shall be made so as to prejudice any person entitled to any prior life or other interest whether vested or contingent, in the money paid or applied unless that person is in existence and of full age and consents in writing to the payment or application, or unless the court, on the application of the trustee, so orders.

(6) For the purposes of this section the trustee may raise money by sale, mortgage or exchange of the trust property.

63 *Conditional advances for maintenance etc*.

(1) Where a power to pay or apply any property for the maintenance, education, advancement, or benefit of any person, or for any 1 or more of those purposes, is vested in a trustee, the trustee when exercising the power shall have authority to impose on the person any condition, whether as to repayment, payment of interest, giving security, or otherwise; and at any time after imposing any such condition, the trustee may, either wholly or in part, waive the condition or release any obligation undertaken or any security given by reason of the condition.

(2) In determining the amount or value of the property that a trustee who has imposed a condition pursuant to subsection (1), may pay or apply in exercise of the power, any money repaid to the trustee or recovered by the trustee shall be deemed not to have been so paid or applied by the trustee.

(3) Nothing in this section shall impose upon a trustee any obligation to impose any condition pursuant to subsection (1); and a trustee, when imposing any condition as to giving security, shall not be affected by any restrictions upon the investment of trust funds, whether imposed by this Act or by any rule of law or by the trust instrument (if any).

(4) A trustee shall not be liable for any loss which may be incurred in respect of any money that is paid or applied under this section, whether the loss arises through failure to take security, or through the security being

include a power to impose conditions upon advances. We think that a power to impose conditions would be a useful addition to Scots law. These provisions strike an appropriate balance between the interests of the beneficiaries who are in immediate need of capital, or would benefit from an immediate advance of capital, and other, frequently future or contingent, beneficiaries who have no such requirement. They would also help to protect the trustees from pressure to advance what they consider an excessive part of the trust funds; this was a point made by the Law Society in its consultation response. As far as we can ascertain, there have been no reported cases on conditional advances in either Queensland or Western Australia, which suggests that the powers are working well in practice.

9.15 We therefore put forward the following, modified, proposals:

22. Section 16 of the Trusts (Scotland) Act 1921 and the Court of Session's common law powers to authorise advances of capital should be replaced by a new statutory provision along the following lines:

Trustees should have power to advance up to half of a beneficiary's share in the capital of the trust fund where:

(a) the trust deed does not expressly prohibit advancement of capital;

(b) at the date of the advance the beneficiary has a right to all or part of the capital of the trust estate which is vested, is vested subject to defeasance or diminution by the occurrence of some uncertain future event, or will vest provided some uncertain future event occurs;

(c) the advance would be, in their view, for the maintenance, education or benefit of the beneficiary;

(d) every person with a prior life or other interest who would be prejudiced by the advance consents.

The power would be a default power, and would be superseded by any contrary provision in the trust deed.

23. The court should continue to have power, on application, to authorise an advance where a person with a prior life or other interest who would be prejudiced by the advance:

(a) is incapable of consenting and a reasonable person in his or her position would have consented; or

(b) is withholding consent unreasonably.

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insufficient, or through failure to take action for its protection, or through the release or abandonment of the security without payment, or from any other cause."

24. **The trustees should have authority to impose any condition upon the advance, whether as to repayment of the sum advanced, payment of interest, giving security, or otherwise; and at any time after imposing any such condition, the trustees should be entitled, either wholly or in part, to waive the condition or release any obligation undertaken or any security given by reason of the condition.**

25. **The trustees should be entitled to place the sum advanced in a new trust for the beneficiary, even if others may thereby gain incidental benefit.**

PART 3: NEW MATTERS

Chapter 10 Information to be provided to beneficiaries and others

10.1 We deal in this Chapter with trustees' duties to disclose certain information to beneficiaries (and others)[1] about the trust in which they have an interest. As we explain, this area of the law is largely undeveloped in Scotland, while the law in England and other common law jurisdictions, though developed to a greater extent, is neither well-established nor settled.

10.2 There is very scant authority in this area from the Scottish courts. The early Victorian decision in *Tod v Tod's Trustees*[2] held that beneficiaries are entitled to see the vouchers as well as the accounts themselves in the administration of a trust. In a much more recent case beneficiaries successfully sought a commission and diligence in respect of vouching for the trust accounts.[3] In the course of his short judgment Lord Clyde said:

> "In general I should have thought that trustees were bound to give a beneficiary full information about their administration and let him see the vouchers as well as the accounts. The refusal to do so might well invite a sinister inference."[4]

Statutory rights to information

10.3 Some jurisdictions have statutory statements of trustees' duties of disclosure to beneficiaries (or, looked at from the other end of the telescope, beneficiaries' rights to obtain information) under trust law.[5] Neither England and Wales nor Scotland is among them. Whilst that is perhaps not surprising, given the common law basis of much of trust law in both jurisdictions, the relative paucity of reported decisions in English law is more surprising.[6] It will be seen that much of the running in this area has been made by offshore jurisdictions, notably the Isle of Man, and by other common law jurisdictions, particularly Australia.

Right to be informed of status as beneficiary

10.4 Before turning to less settled aspects of the law, we note that it is accepted as a matter of English law that trustees are obliged to inform a person that he or she is a trust beneficiary.[7] This applies absolutely in the case of an adult beneficiary with an interest in possession, though matters are more nuanced where the beneficiary has a future interest

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[1] We deal later in paras 10.20-10.24 with information to be given to protectors and enforcers.
[2] (1842) 4 D 1275.
[3] *Nouillan v Nouillan's Exrs* 1991 SLT 270. *Tod v Tod's Trs* does not appear to have been cited to the court.
[4] Ibid at 271.
[5] Lewin, para 23-06, fn 2, citing amongst others the Trusts Law (2009 revision), s 100 (Cayman Islands) and the Trusts (Jersey) Law 1984 (as amended), art 29. We note that the DCFR Book X.-6:104(1) and (4) make provision for trustees' obligations to inform and report to beneficiaries on the state and investment of the trust fund, trust debts, and disposal of trust assets and their proceeds.
[6] What English authority exists is, on the whole, consistent with the Scottish position. We point out below (at paras 10.8 and 10.10) two particular instances where this is not so.
[7] See Lewin, paras 23-07 to 23-14; Thomas and Hudson, para 12.02.

(for instance a contingent interest) or is within the class of beneficiaries of a discretionary trust. As regards the relevant information which must be proffered, the editors of Lewin have this to say:

> "[T]he information that needs to be given is the existence of the settlement and the beneficiary's interest under it. We consider that information about the general nature of the beneficiary's interest should be given, including (in contrast to the position concerning executors)[8] conditions attached to the beneficiary's interest. But the trustees need offer no advice or explanations about the legal implications or effect of the beneficiary's interest […]. Unless it is self-apparent from the trustees' communication, sufficient information about the identity of the trustees should also be provided to enable the beneficiary to seek further information from the trustees on demand. We do not consider that the trustees have to provide the beneficiary with copies of any accounts or trust documents without demand – if the beneficiary wants further information or access to accounts or trust documents it is up to him to seek it from the trustees."[9]

10.5 The effect of this is that, in general, a person who is a beneficiary under a trust should be informed of that fact. We consider that this is a sensible starting point and also represents Scots law, at least so far as "ordinary" trusts are concerned:[10] one of the rights of a beneficiary is the ability to hold the trustees to account, which cannot possibly be done if the trustees have the option of not informing a person that he or she is a beneficiary.[11] Since executors are in the same position as trustees – as provided by section 2 of the Executors (Scotland) Act 1900 for executors nominate, and section 20 of the Succession (Scotland) Act 1964 for executors dative – any rule which applies to trustees will apply equally to executors.[12] It follows, further, from this that there is a duty on an executor to inform a person of his or her status not only if he or she is a testamentary beneficiary but also if the person has legal rights or intestate succession rights. In order to gauge views on these matters, we ask:

26. (a) As a general rule, should trustees be obliged to inform a person that he or she is a beneficiary of the trust? If so, what exceptions should be made? Should they be based on the age and capacity of the beneficiary, and/or on whether the beneficiary has a vested interest or not? Are there any other relevant considerations?

(b) Should any such general rule apply also to executors, i.e. should an executor be obliged to inform a person that he or she is a testamentary beneficiary, is entitled to legal rights, or has intestate succession rights (as appropriate)?

(c) Should the rule, and any exceptions, be set out in statute?

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[8] The position of executors is different: see Lewin, para 23-11.
[9] Lewin, para 23-12.
[10] See chs 11-13 for special trusts.
[11] This is a generalisation, and it will not be necessary for all beneficiaries to be told of their status, either immediately the status arises or, in some cases, at all. But we see these as exceptions to the general rule.
[12] This is subject to contrary provision in the trust deed. As mentioned in fn 8 above, English law does not apply to executors in exactly the same way as it applies to trustees.

Further information rights

10.6 What information a beneficiary can obtain thereafter is the subject of the rest of this Chapter, along with an examination of the legal basis for such a right. These issues are uncertain in several important respects.[13]

10.7 As we have already noted, the law in England and Wales is to be found in reported decisions. This is not a satisfactory situation, as not only is there a lack of cases but the ones which exist are, necessarily, concerned with particular applications in particular situations and they have not given rise to satisfactory general statements of principle. What is clear, though, is that the law on the entitlement of a beneficiary to information, on demand, from a trustee has undergone a measure of re-examination in the last 8 years or so. We consider first of all its basis, and then examine its scope.

Basis for right to information

10.8 Professors Thomas and Hudson, the authors of *The Law of Trusts*, begin their chapter on Disclosure of Information by Trustees with a section entitled "The Orthodox View".[14] The "orthodox view":

> "has until recently been that a beneficiary was entitled to see trust documents and to be given information concerning trust affairs; and, moreover, that such rights had a proprietary basis, ie they were founded on the basis that trust documents were trust property in which the beneficiary had a proprietary interest".[15]

There is long-standing authority for this.[16] It will be seen that this view has been criticised,[17] but as a basis for a rule in Scots law it will not do. That is because it depends for its existence on the English doctrine of equity, by which property rights in the trust assets are held, simultaneously, by both the trustees and the beneficiaries. As Scots law does not recognise this analysis of property rights, the justification for a beneficiary to be entitled to information based on proprietary rights will not work.[18]

10.9 A recent development of the law came in the Privy Council decision from the Isle of Man: *Schmidt v Rosewood Trust Ltd*.[19] It concerns the rights of a person who could not directly or indirectly demonstrate that he had a proprietary right in the trust assets (a failure which resulted in the Isle of Man Court of Appeal ruling that there was no entitlement to the information). The Privy Council, in a judgment delivered by Lord Walker, upheld the claims of such a person, saying that:

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[13] In certain situations the law is clear, for instance where a trustee who was also a beneficiary wished to buy a fellow beneficiary's share of the trust fund he was obliged to let the latter see a trust valuation which he had obtained: *Dougan v Macpherson* (1902) 4 F (HL) 7, (1902) 9 SLT 439.

[14] Thomas and Hudson, ch 12 (for which Professor Thomas is responsible).

[15] Thomas and Hudson, para 12.03.

[16] Eg *O'Rourke v Darbishire* [1920] AC 581 at 626 per Lord Wrenbury: a beneficiary "is entitled to see all the trust documents because they are trust documents and because he is a beneficiary. They are in a sense his own. Action or no action, he is entitled to access to them. This has nothing to do with discovery. The right to discovery is a right to see someone else's documents. A proprietary right is a right to access to documents which are your own." *In re Londonderry's Settlement* [1965] Ch 918 is another case commonly cited in this regard.

[17] See Thomas and Hudson, paras 12.07-12.09.

[18] See Panico, para 12.87; George Gretton, "Trusts" in Kenneth Reid and Reinhard Zimmermann (eds), *A History of Private Law in Scotland*.

[19] [2003] 2 WLR 1442. For a discussion of the case, and of the issues discussed in this chapter more generally, see Michael Gibbon, "Beneficiaries' information rights" 2010 *Trusts & Trustees* vol 17 no 1, 27-33.

> "the more principled and correct approach is to regard the right to seek disclosure of trust documents as one aspect of the court's inherent jurisdiction to supervise, and if necessary to intervene in, the administration of trusts. The right to seek the court's intervention does not depend on entitlement to a fixed and transmissible beneficial interest".[20]

The court added that a proprietary right was neither sufficient nor necessary, as issues such as confidentiality might preclude disclosure even to a beneficiary with a vested interest in possession.[21]

10.10 This is a departure from (or, at the very least, a radical development of) the orthodox view in English law. The effect of the decision, which has been followed in numerous jurisdictions,[22] is to put the onus on the court rather than the trustees. There has been a later attempt by the English courts to provide some guidance for trustees to avoid the need for court applications in certain cases (by Briggs J in *Breakspear v Ackland*[23]) but the requirement to seek court guidance on disclosure (as on other matters of trust administration) is one which accords with the traditional Chancery view in England that trusts must always be subject to the scrutiny and control of the courts.[24] This does not reflect the traditional Scots view of the role of the court in respect of trust administration,[25] and we would not wish to require or encourage trustees or beneficiaries to go to court except where necessary.[26]

10.11 We have, so far, considered (and rejected as possible options for a basis for information rights in Scots law) two rationales, authority for both of which can be found in English law. The first is that a beneficiary has the right to access trust documents because of his or her proprietary claim to trust property, of which the documents form part; the second is that questions of whether a particular beneficiary has the right to see a particular document is a matter for judicial discretion. There is a third option. It is alluded to in the dissenting opinion of Kirby P in the New South Wales Court of Appeal in a case about the disclosure of a "letter of wishes", *Hartigan Nominees Pty Ltd v Rydge*.[27] Kirby P stated:

> "I do not consider that it is imperative to determine whether that document is a 'trust document' (as I think it is) or whether the respondent, as a beneficiary, has a

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[20] [2003] 2 WLR 1442 at para 51.
[21] Ibid at para 54. This was in response to *dicta* of Kirby J in the Court of Appeal of New South Wales in *Hartigan Nominees Pty Ltd v Rydge* (1992) 29 NSWLR 405; we refer to these *dicta* at para 10.11 below.
[22] Eg Jersey (*Alhamrani v Russa Management Ltd* [2006] WTLR 1551, (2004-05) 7 ITELR 308), Guernsey (*Countess Bathurst v Kleinwort Benson (Channel Islands) Trustees Ltd* [2007] WTLR 959), Victoria (*Crowe v Stevedoring Employees Retirement Fund Pty Ltd* [2003] Pens LR 343 Sup Ct (Vic)), New Zealand (*Foreman v Kingstone* [2005] WTLR 823 (HC)) and Bermuda (*Wingate v Butterfield Trust (Bermuda) Ltd* [2008] WTLR 357).
[23] [2008] EWHC 220 (Ch), [2009] Ch 32. This case turned on a request to see a "letter of wishes".
[24] Eg "It is fundamental to the law of trusts that the court has jurisdiction to supervise and if appropriate intervene in the administration of a trust, including a discretionary trust": *Schmidt v Rosewood Trust Ltd* [2003] 2 WLR 1442, para 36. See also Michael Gibbon, "Beneficiaries' information rights" 2010 *Trusts & Trustees* vol 17 no 1, 27-33 at 27.
[25] See, eg, *Board of Management for Dundee General Hospital v Bell's Trs* 1952 SC (HL) 78, esp at 92 per Lord Reid; and generally our DP on Trust Administration, paras 5.3-5.8.
[26] It is perhaps unfortunate that the court in *Schmidt* was faced with a trust which was, apparently, designed to be non-transparent: see para 1 of the Privy Council's opinion. "It is a widely held view that any decision other than the one reached [in *Schmidt*] would have meant that (particularly in the offshore context) it would have been possible to create trusts that were effectively unpoliceable": Michael Gibbon, "Beneficiaries' information rights" 2010 *Trusts & Trustees* vol 17 no 1, 27-33 at 30. Against that background the decision is unsurprising, but it is perhaps not helpful that the outcome is imposed on all types of trust.
[27] (1992) 29 NSWLR 405.

> proprietary interest in it (as I am also inclined to think he does). Much of the law on the subject of access to documents has conventionally been expressed in terms of the 'proprietary interest' in the document of the party seeking access to it. Thus, it has been held that a *cestui que trust* has a 'proprietary right' to seek all documents relating to the trust: see *O'Rourke v Darbishire* [1920] AC 581, 601, 603. This approach is unsatisfactory. Access should not be limited to documents in which a proprietary right may be established. Such rights may be *sufficient*; but they are not *necessary* to a right of access which the courts will enforce to uphold the *cestui que trust's* entitlement to a reasonable assurance of the manifest integrity of the administration of the trust by the trustees."[28]

Thomas and Hudson add:

> "Kirby P agreed with the comments on this issue made in Ford and Lee's *Principles of the Law of Trusts*, namely:
>
> > 'The beneficiary's rights to inspect trust documents are founded therefore not upon any equitable proprietary right which he or she may have in respect of those documents *but upon the trustee's fiduciary duty to keep the beneficiary informed and to render accounts*. It is the extent of that duty that is in issue.'"[29]

10.12 It can be argued – and Thomas and Hudson do so[30] – that this analysis is entirely consistent with the orthodox view based on a beneficiary's proprietary rights. For common law jurisdictions any such argument is more potent than it is in Scots law, where the beneficiary's interest in the trust assets is a personal right as against the trustees and not a proprietary right in the assets. We find the analysis of the beneficiary's right to information as being based on the trustees' fiduciary duties to be an attractive one. If a beneficiary is to exercise effective control over the trustees' actings – as he or she undoubtedly has the right to do in an ordinary trust – the ability to do so would be severely impeded if there were no effective right to relevant pieces of information. (We discuss below what might be "relevant" in this context.) Failure by the trustees to respond constructively to a beneficiary's request for information would be seen as a breach of duty.[31] To ascertain views, we therefore ask:

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[28] Ibid at 421 (with emphasis in the original).
[29] Thomas and Hudson, para 12.11 (with emphasis added).
[30] At para 12.13. At all events, the *Schmidt v Rosewood* decision has not been universally received in Australia. The law is reviewed by Bryson AJ in *McDonald v Ellis* [2007] NSWSC 1068, who said (at paras 49-50): "The history of Equity and the nature of its remedies mean that the treatment of equitable interests as proprietary, and the development of rules based on that treatment, can never be entirely logical or satisfactory; but if this is perceived as a problem, it is an inherent problem and should not be regarded as a basis for discarding a well-established rule. An obiter dictum in the Privy Council about trust law in the Isle of Man has in my opinion very little claim to be followed at first instance in New South Wales where a different view has been accepted. The Privy Council does not exercise appellate authority over the courts of New South Wales, and its decisions made since its appellate power was abolished in 1986 have not had binding force in New South Wales. Still less have the Judicial Committee's obiter dicta. As with other decisions which are not binding, its claim to be followed depends upon the extent to which the views expressed are persuasive." See also the recent review of the authorities in the Western Australian Supreme Court in *Murray v Schreuder* [2009] WASCA 75 at paras 44-58.
[31] A "constructive response" may, in appropriate cases, involve an application to the court for directions: see para 7.2.

27. Should the rule of Scots law be that trustees owe a duty to make available to a beneficiary, on request, relevant information in trust documents? (We specify what we consider to be such information in paragraph 10.13 below.) If not, on what other basis should the beneficiary's right to information be dependent?

Content of information

10.13 What information should a trustee make available to a beneficiary? The reported cases tend not to give lists of such information,[32] but rather to discuss documents which are on the borderline between what should be disclosed and what should not. However, the information which would normally be expected to be made available includes that contained in documents:[33]

(a) creating the trust;

(b) relating to who is a trustee;

(c) exercising or releasing powers of appointment.

In addition, the following are included:

(d) trust accounts;

(e) vouchers for payments made by the trustees or their agents;

(f) written notices in relation to the beneficiary's interest;

(g) opinions from counsel or other advisers on the administration of the trust (plus relevant instructions);

(h) other legal advice obtained by the trustees (eg from solicitors) on the administration of the trust;

(i) actuarial reports and investment reports which relate to the value of the trust assets.

Categories (g) and (h) do not, though, include any documents relating to legal proceedings relating to the trust and which are taken against the trustees.

10.14 What is *not* included is material which relates to, or records the deliberations of trustees or their reasons for their decisions.[34] Thus, agendas and minutes of trustees'

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[32] See, for instance, *Re Londonderry's Settlement* [1965] Ch 918 per Danckwerts J at 935: "[I]t is quite a simple matter to make general observations on the right of beneficiaries to inspection of trust documents, but it does not carry one any further until one knows what is meant by 'trust documents.' For instance, one of the definitions of trust documents which was suggested seems to me quite hopeless. It was suggested that trust documents included everything in the trustees' hands as such. That will cover practically everything that reaches the trustees in their official capacity, from advertisements for pink pills to blackmailing letters from people who think they have a grudge against the trustees. That does not solve our problem in the least."

[33] For more detail see Thomas and Hudson, para 12.32. Also compare (and contrast) the trust documents which may be inspected by a beneficiary under the DCFR (at Book X.-6:106(6)).

[34] At least two reasons for this are advanced: first, the exercise of discretion is not open to challenge in the court (provided that *bona fides* is not challenged), and so there is no obvious benefit in disclosure and, secondly, there

meetings would not normally be disclosable.[35] "Letters of wishes", in which the truster (usually) explains to the trustees what circumstances are relevant for the exercise of any discretion, and so on, are also not normally disclosable.[36] One of the reasons for this is that the truster is taken to have deliberately not included the information in the trust deed itself, typically because the contents are intended to be confidential.[37] Also excluded from disclosure are papers which relate to the interests of another beneficiary, though of course they would be disclosable if that person made a request.

10.15 Where trustees are uncertain as to whether a document should be disclosed, they will need to consider a court application, which will usually be by way of a petition for directions. The lists of information set out above (of information which is (or is not) normally disclosable) is not prescriptive, nor is it exhaustive. There are a number of reasons why a court application may be necessary:[38] the trustees may consider that a document is confidential; or that disclosure might harm the interests of another beneficiary or a third party; or that the requesting beneficiary has an ulterior motive which affects the decision of whether to disclose the information in the circumstances.

Practicalities

10.16 We envisage that, before information is disclosed, the beneficiary or his or her solicitor[39] must make a demand of the trustees (or any individual trustee) specifying the information which is requested. Trustees are not required to make the information available other than on request. It is sufficient to allow the requesting beneficiary (or his or her solicitor) access to the relevant documents. They may be copied, at the beneficiary's expense.[40] The right is to information, though, and not to the physical documents (which may, nowadays, not be physical at all but electronic).[41]

10.17 In order to test whether those with an interest in this area of the law agree with our preliminary views,[42] we ask:

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may be positive disadvantages in disclosing this material. As Salmon LJ said in *Re Londonderry's Settlement* [1965] Ch 918 at 937: "Nothing would be more likely to embitter family feelings and the relationship between the trustees and members of the family, were trustees obliged to state their reasons for the exercise of the powers entrusted to them."

[35] But see Harold Ford and Tony Lee, *Principles of the Law of Trusts* (Sydney; 3rd ed, 1996, update 72 (2009)), para 9.7310 which suggests that some of the minutes will be disclosable.

[36] Many of the reported cases concern letters of wishes. Disclosure is occasionally ordered: eg *Breakspear v Ackland* [2008] EWHC 220 (Ch), [2009] Ch 32; *Re Avalon Trust* [2006] JRC 105A, 9 ITELR 450 (Jersey). There is also an argument that the exercise of the *Hastings-Bass* principle (which we discuss in ch 14) assumes that beneficiaries have access to all information which is relevant to trustees' decisions. Letters of wishes will typically fall into this category. For details of this argument see Thomas and Hudson, para 12.36 (though of course this was written before the Court of Appeal's decision in *Pitt v Holt; Futter v Futter* [2011] EWCA Civ 197, 9 March 2011, as discussed in ch 14, was issued).

[37] We discuss at paras 10.18-10.19 below the possibility of trusters being able to provide that certain documents should remain confidential to the trustees and not disclosable.

[38] See further Lewin, para 23-17.

[39] This reflects the current English law: see, eg, *Re Cowin* (1886) 33 Ch D 179 at 186-7.

[40] This has long been the law in England: see, eg, *Ex p Holdsworth* (1838) 4 Bing NC 386; *Ottley v Gilbey* (1845) 8 Beav 602.

[41] This is the same approach as taken in the freedom of information legislation.

[42] The same issue can also be addressed from the opposite direction, namely by asking to what extent a truster should be able to provide that information that would normally be confidential should be discloseable to beneficiaries. We see no policy reasons for preventing a truster from making information available in this way; whether trustees choose to act in such circumstances is entirely a matter for their own judgment. For an example, see art 29 of the Trusts (Jersey) Law 1984, as amended, which specifies classes of information which are not to be disclosed, "[s]ubject to the terms of the trust and subject to any order of the court".

28. Do you agree with, or have any comments on, our analysis set out in paragraphs 10.13-10.15 above as to what information is disclosable? Should there be a statutory list of documents whose information is disclosable (other than in exceptional circumstances, for which judicial discretion would normally be expected), and if so should it be the list in paragraph 10.13?

Possibility of exclusion by truster

10.18 To what extent should the truster be able to provide that certain information which would otherwise be disclosable is to be kept confidential? Behind this question lies a tension between the rights of the truster,[43] on the one hand, and, on the other, the duty of the trustees to act at all times in the beneficiaries' best interests. To take an extreme example, if a truster were to provide in the trust deed that trust accounts were to be confidential, or were only to be shown to specified beneficiaries, it is hard to see how those beneficiaries who are to be deprived of such information will be able to satisfy themselves that the trustees are acting as they ought to do. Will the trust not become effectively unpoliceable? We consider that public policy reasons should weigh in so as to prohibit this. And to take a less extreme example, a truster may for good reason decide that he or she wishes to express certain preferences to the trustees which are to be kept confidential. This is typically done by means of a letter of wishes, but we have seen that these are in some instances disclosable.[44] Should it be possible for a truster to specify (for instance in the trust deed) that any letter of wishes is to remain confidential at all times? This seems reasonable, certainly at the outset.[45] But if the trust continues to exist for many years and circumstances change (for instance with a previously wealthy discretionary beneficiary becoming incapacitated and dependant on costly care) is it right that the beneficiaries remain unable to see the letter of wishes which may, in the trustees' view, require them to pay less to the incapacitated beneficiary than they would otherwise choose to do? If so, the beneficiaries' ability to challenge the trustees is restricted in an important way.

10.19 In our DP on Accumulation we discussed issues relating to the degree of control which a truster could exert in respect of a long-term trust;[46] our proposal was to create a new judicial power allowing the alteration of trust purposes where there has been a material change of circumstances.[47] We consider that this would be a suitable model for any provisions relating to the trusters' powers to restrict beneficiaries' right to information. An appropriate balance would be struck, in our view: for a certain period of time, the trustees would be bound by the truster's wishes (or, where there was doubt as to the effect of those wishes, they would have to seek court directions) but once that time had elapsed the trustees or the beneficiaries could, on a material change of circumstances, seek judicial alteration of the truster's wishes. But in order to gauge views on this, we ask:

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[43] Usually considered at the time of setting up the trust, but the issue may arise at a later time: for instance, we understand that it is not uncommon for letters of wishes to be sent to trustees (or existing letters amended) after the creation of the trust.
[44] See para 10.14 above and its fn 36.
[45] But see the argument sketched in fn 36 above.
[46] In Pt 5.
[47] Ibid, para 5.57, proposal 6. The power is only to be exercisable after the trust has been in existence for a certain period of time (which we proposed be 25 years).

29. (a) Should a stipulation of the following kind be effective, namely a stipulation by a truster that information which would otherwise be disclosable at the request of a beneficiary is not to be disclosed?

(b) If so, are there any types of information in relation to which such a stipulation may not be made? (If possible, it would be helpful for responses to refer to the list at paragraph 10.13.) Should any other conditions be placed on such a stipulation for it to be effective?

(c) Should the court be able to review any such stipulation, on the basis that it counts as a trust purpose, under the proposed jurisdiction outlined in our Discussion Paper on Accumulation of Income and Lifetime of Private Trusts (DP No 142) at proposal 6?

Special trusts

10.20 In Chapters 11 to 13 we consider vehicles other than the conventional beneficiary trusts. We raise for consultation different types of private trust, whose linking characteristic is that they admit the possibility of being established in order to fulfil a *purpose*. This stands in stark contrast to the traditional idea of a trust as something which needs to have *beneficiaries*.[48] We consider here, just briefly, how the information rights discussed in this Chapter will be accommodated in such trusts.

10.21 The first point to note is that, for a trust set up purely for a purpose, there will be no beneficiaries identifiable from the trust deed. Thus, there is no question of beneficiaries' information rights arising. Instead, private purpose trusts of this nature tend to require an "enforcer".[49] The enforcer stands, in many ways, in place of the beneficiary in an "ordinary" trust. We cite the example of the Cayman Islands legislation, which provides that, subject to the terms of his appointment:

> "an enforcer has the same rights as a beneficiary of an ordinary trust – […]
>
> > (ii) to be informed of the terms of the trust, to receive information concerning the trust and its administration from the trustee, and to inspect and take copies of trust documents".[50]

10.22 It is possible, though, to set up a special trust for both a purpose and for one or more beneficiaries. This is a feature of the Cayman Islands legislation referred to in the preceding paragraph, which permits so-called STAR trusts to be established, for a combination of purposes and/or beneficiaries. However, the statute provides that "[a] beneficiary of a special trust does not, as such, have standing to enforce the trust, or an enforceable right against a trustee or an enforcer, or an enforceable right to the trust property".[51] This would, therefore, preclude the beneficiary from exercising the rights to obtain information which we have been discussing in this Chapter. If consultation responses are broadly in favour of adopting private purpose trusts into Scots law, along the lines of the trusts we discuss in

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[48] Of course, charitable and public trusts are an exception, but we are here dealing only with private trusts.
[49] See ch 12 in general, and particularly paras 12.10-12.18.
[50] Trusts Law (2009 Revision), s 102(a)(ii).
[51] Ibid, s 101(1).

later chapters of this paper, we see no reason why any beneficiaries of such trusts should be treated other than as in the STAR trusts.

10.23 Nevertheless, we seek views on the following questions:

30. If a special regime for private purpose trusts, with an enforcer, were introduced into Scots law, should the rule for such trusts be that, as with STAR trusts in the Cayman Islands, the trustees are obliged to provide information about the trust to the enforcer but not to any beneficiaries of the trust? Alternatively, for such trusts should there be a default rule that information is to be provided to an enforcer but not to beneficiaries, such a rule to apply if the truster makes no provision to the contrary?

31. In either event, should the information that is to be provided be as contemplated in paragraph 10.13 above?

10.24 In Chapter 11 we discuss the possible introduction of protectors into Scots law. We think it clear that any person appointed as a protector should have the fullest possible information rights about the operation of the trust. This would include information about the manner in which the trustees reached their decisions; the crucial reason for appointing a protector is to serve as a close check on the trustees' actings, and understanding how they reach their decisions may be critical in fulfilling that function. We think, however, that this should be a default provision; if a truster wishes to provide otherwise in the trust deed, he or she should be permitted to do so. We accordingly propose:

32. If a protector is appointed to a trust, he or she should have a right to examine all documents, of any sort, kept by or on behalf of the trustees. This right will be subject to modification only if the trust deed provides otherwise.

Chapter 11 Protectors

11.1 As we have mentioned in Chapter 1, trusts are of fundamental importance to the financial and investment sector in Scotland. We accordingly wish to ensure that the Scottish law of trusts keeps up to date with developments in other parts of the world that have proved useful to that sector; otherwise there is a serious risk that Scotland will be left behind other jurisdictions in this highly competitive area of business. In this and the following chapters we consider three legal institutions and one legal principle that have proved successful in attracting and retaining investment and financial business in other parts of the world.

11.2 We think that these institutions may be of particular utility in Scotland. Scotland is a relatively small country which has, for its size, a large and well-respected financial sector; fund management, pensions and life assurance are all important areas of economic activity, and much of the business carried out in Scotland in these areas is drawn from elsewhere. To that extent Scotland is similar to some of the offshore jurisdictions that have been the pioneers in developing new forms of legal institution in the trust field.

11.3 The first of the institutions is the protector. We would like views on whether it is appropriate for Scotland to make statutory provision for protectors, or possibly advisory trustees, another institution that serves a somewhat similar function.[1] Protectors have been found regularly in offshore trusts since the 1980s. Their function is "to ensure that the trustee of [an offshore] trust, so many miles away from the settlor and vested with the settlor's property, was actually and efficiently discharging the various trustee duties".[2] In this way the settlor is given a degree of control, or at least influence, over the trustees, and may have some assurance that the trust is being properly administered. The protector is frequently given power to dismiss and appoint trustees; in the latter role a protector may be described as an "appointer".[3] More recently protectors have started to appear in trust deeds in more mainstream jurisdictions. The matter is considered in an Issues Paper published by the New Zealand Law Commission,[4] to which we are indebted for information about the institution. The paper points out that protectors started to appear more frequently in trust deeds in New Zealand in the late 20th century, with varying powers. In a Report published in 2002,[5] the Commission recommended a new section in the New Zealand Trustee Act which would define a protector as a person who, by virtue of the trust deed, may give trustees directions that the trustees are obliged to follow or whose consent to the exercise of a trustee power is necessary; it would further enable trustees to apply to the court for directions in any case where the trustee knew or ought to have known that following the protector's directions would conflict with the trust or any rule of law. The Commission point out that this matter will be reconsidered in the course of their current review of the law of

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[1] The institution of the protector is the subject of very detailed discussion in Panico, ch 10; it is also mentioned in Thomas and Hudson, paras 23.34-23.36.

[2] Donovan Waters, "The Protector: New wine in old bottles?" in Anthony Oakley (ed) *Trusts in Contemporary Trust Law* at p 63.

[3] John Glover "Discretionary trusts, fiduciary duties and the Family Law Act: has the family court acted beyond power?" (2000) 14 Aust Family Law Jnl 184 at 190-192.

[4] Review of Trust Law in New Zealand: Introductory Issues Paper (Issues Paper 19, Nov 2010: http://www.lawcom.govt.nz/project/review-law-trusts?quicktabs_23=issues_paper), paras 2.57-2.60.

[5] New Zealand Law Commission, Some Problems in the Law of Trusts, NZLC R 79 (2002) at para 24.

trusts in New Zealand. Particular issues that they highlight are the control by the court of a protector and his interference in the trust, the standard expected of a protector, and whether the protector's role should be fiduciary.

11.4 The powers exercised by protectors can vary significantly. Ultimately the definition of the role is a matter for the individual trusters, but the legislation found in jurisdictions that expressly recognise protectors provides useful checklists of the functions that may be exercised. One example is found in the legislation of the British Virgin Islands:

> "There may be conferred on the settlor or some other person, whether named as protector, nominator, committee or by any other name, by the instrument creating the trust, any powers, and without limitation to the foregoing power may be conferred on that person to do any one or more of the following:
>
> (a) determine the law of which jurisdiction shall be the proper law of the trust;
>
> (b) change the forum of administration of the trust;
>
> (c) remove trustees;
>
> (d) appoint new or additional trustees;
>
> (e) exclude any beneficiary as a beneficiary of trust;
>
> (f) include any person as a beneficiary of the trust in substitution for or in addition to any existing beneficiary of the trust;
>
> (g) withhold consent from specified actions of the trustees either conditionally or unconditionally."[6]

The foregoing provision has been followed in legislation in other jurisdictions. A further provision that is sometimes encountered is a power in a protector to verify the trust accounts.[7] Yet a further power that may be conferred on a protector is a power to represent any beneficiaries who are minor or otherwise lacking in legal capacity, or who have yet to be ascertained, or who cannot be contacted despite trustees' reasonable endeavours to find them.[8] In such cases the trust instrument might require the protector to consent to or ratify any acts carried out by the trustees, and the protector's consent or ratification would be construed as if it had been granted by the beneficiaries.

11.5 In legislation dealing expressly with protectors it is normal to find a provision specifying that the protector must not be regarded as a trustee.[9] Such a provision is generally regarded as essential to prevent the protector from being regarded as a co-trustee or the sole real trustee; if that were to happen, it could have very serious tax or estate planning consequences. Although protectors are declared not to be trustees, it does not follow that their powers are not fiduciary, and in fact different jurisdictions take different approaches to the question of whether the duties of a trustee are fiduciary in nature. Thus in

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[6] Section 86(2) of the Trustee Ordinance 1961, as amended by the Trustee (Amendment) Act 1993.
[7] Eg San Marino, Law of 17 March 2005, art 54(5).
[8] Eg the Cook Islands, International Trust Act 1984, s 21.
[9] Examples are to be found at Panico, para 10.99.

the Cook Islands it is made clear that the powers of a protector are personal, and that he or she shall not be liable or accountable as a trustee or other person having fiduciary duty to any person.[10] A similar provision is found in Guernsey.[11] In other jurisdictions a protector is obliged to exercise his or her powers in good faith; an example is the British Virgin Islands, where the legislation, after providing that a protector is not to be deemed a trustee, states that unless otherwise provided in the trust instrument, a protector "is not liable to beneficiaries for the bona fide exercise of the power".[12] Similar provisions are found in the Bahamas[13] and Mauritius.[14] In yet other jurisdictions the powers and duties of protectors are expressly made fiduciary; examples include Belize and Nevis.[15] In St Kitts, the duties of a protector are taken further; they are required to act honestly and in good faith with a fiduciary duty to the beneficiaries of the trust or to the purpose for which the trust is created, and are bound to exercise the care, diligence and skill that a reasonably prudent person would exercise in comparable circumstances.[16] The latter duties are mandatory, and prevail over any contrary provision in the trust deed.

11.6 In their Issues Paper the New Zealand Law Commission refer to a view in New Zealand that the popularity of the protector there was strange because New Zealand trust legislation permitted the appointment of advisory trustees.[17] Section 49 of the New Zealand Trustee Act 1956 provides that "where any advice is … given by the advisory trustee, the responsible trustee may follow the same … and shall not be liable for anything done".[18] This is in practice a powerful incentive for the responsible trustee to act on any advice given by the advisory trustee. Moreover, the advisory trustee may be consulted on any matter relating to the trust. The difference between a protector and an advisory trustee is identified by the New Zealand Law Commission in their Report of 2002;[19] a trustee may elect to consult an advisory trustee but is obliged to act on the direction of a protector.

11.7 In view of the clear popularity of the institution of protector in a substantial number of other jurisdictions, we would like to ask whether there is any demand for legislative recognition of a similar institution in Scotland. While we do not want to add unnecessarily to the length of the trusts legislation, it does seem to us that Scots law should aspire to the highest international standards in facilitating the reasonable wishes of trusters, and recognising protectors, and possibly advisory trustees, may be a feature that would be regarded as attractive by those considering setting up a trust in Scotland. We accordingly ask the following question:

33. (a) Should the trust legislation make provision for either protectors or advisory trustees?

(b) If so, in general terms what provision should be made? In particular:

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[10] International Trusts Act 1984, s 20(4), as amended.
[11] Trusts (Guernsey) Law 2007, s 15(2)(b) (reproduced in Appendix B).
[12] Trustee Ordinance 1961, s 86(3), as amended by the Trustee (Amendment) Act 1993.
[13] Bahamian Trustee Act 1988, s 81(3).
[14] Mauritian Trusts Act 2001, s 24(4).
[15] Belize Trusts Act 1992, s 16(5); Nevis International Exempt Trust Ordinance 1994, s 9(5).
[16] Trusts Act 1996, s 25(8).
[17] Issues Paper 19 (see fn 4 above), para 2.61.
[18] The full text of s 49 is reproduced in Appendix B.
[19] New Zealand Law Commission, Some Problems in the Law of Trusts, NZLC R 79 (2002) at para 24.

(i) Should legislation list the powers that may be conferred on protectors? If so, is the list found in the legislation of the British Virgin Islands appropriate? Should a power to verify accounts be included? Are any other powers desirable?

(ii) Should protectors' duties be made expressly fiduciary in nature? Should they be subject to an express duty to exercise the care, diligence and skill that a reasonably prudent person would exercise in comparable circumstances?

(iii) Is it desirable that specific provision should be made for the control of protectors by the court? For example, should a protector be entitled to apply to the court for directions? Should the truster, or any other person, have power to apply to the court to remove a protector, or to compel him or her to take action in furtherance of his or her responsibilities?

11.8 If statutory provision were made for protectors in Scots law, three other ancillary matters are relevant. The first relates to the removal or replacement of protectors other than by application to the court. We think that this can normally be left to the provisions of the individual trust deed, but the default rule should be that the truster has power to appoint or replace a protector. The second issue is whether a protector should be entitled to remuneration. If the office were made fiduciary in nature, the default rule would be that he or she was not entitled to remuneration, in accordance with the usual rule applicable to fiduciaries. Obviously the default rule can be superseded by contrary provision in the trust deed. If the office were not fiduciary in nature, it might be desirable to make express provision about remuneration, and we would welcome suggestions as to what the default rule should be: whether in the absence of any contrary provision a protector should be entitled to reasonable remuneration or whether, again subject to contrary provision, the office should be gratuitous in nature.

11.9 The third issue is whether the trustees' liability should be limited in the event of intervention by a protector. When statutory provision is made for protectors, the almost invariable practice is to provide that trustees should not be liable for breach of trust for any acts carried out following protectors' advice, consent or directions. An example is found in section 15 of the Trusts (Guernsey) Law 2007 (as amended),[20] which permits the appointment of a protector and provides that a trustee who acts in compliance with the valid exercise of any power conferred on a protector "does not, by reason only of such compliance, act in breach of trust". As a general principle, however, we think that, as a default rule, it is essential that either the trustee or the protector should be liable to beneficiaries for any decision that does not meet the appropriate standard of care.[21] We are inclined to favour a fairly robust rule to the effect that, if the trustees act in accordance with a direction by the protector, they are immune from any claim for breach of trust, but (at least if the office of protector is fiduciary in nature) the protector is liable to beneficiaries for the

[20] Section 15 is reproduced in Appendix B.
[21] See discussion in Panico, paras 10.124-10.128.

consequences of his or her act. On the other hand we would envisage this as a default rule, and if a truster wishes to appoint a protector who is not subject to personal liability in this way we cannot see any fundamental objection; the central point is that the protector acts on behalf of the truster with a view to furthering the truster's intentions. Against this background, we ask the following question:

34. If Scots law makes provision for the appointment of protectors, should trustees be expressly protected from personal liability in the event that they act in accordance with the directions or instructions of the protector? In such a case, should the default rule be that the protector is liable to the beneficiaries for the consequences of his or her instructions, but with power in the truster to exclude this rule, so that the protector incurs no personal liability?

Chapter 12 Private purpose trusts

12.1 An institution that has appeared in recent years in a number of jurisdictions is the non-charitable purpose trust. By "purpose trust", what is meant is a trust that does not have defined persons as beneficiaries but rather exists to achieve a defined purpose, frequently of a philanthropic or business nature. Legislation to permit such trusts first appeared in Bermuda.[1] That model has been followed in a number of other jurisdictions.[2] A major development occurred in 1997 when the Cayman Islands enacted the Special Trusts (Alternative Regime) Law of that year; this permitted a type of purpose trust that has come to be known as a STAR trust. The legislation is now found in the 2009 revision of the Cayman Islands Trust Law.[3] The STAR model has been followed in other jurisdictions, notably Guernsey,[4] Bermuda,[5] and the Bahamas.[6] The Guernsey legislation is somewhat shorter and simpler than the Cayman Islands legislation, and could serve as an alternative model for reform. Nevertheless, the Cayman Islands STAR legislation has generally been regarded as the paradigm for these developments, and the discussion that follows centres on that model.[7] The STAR Trust has been described by Professor David Hayton as "the most sophisticated trust vehicle in the world",[8] and Paolo Panico, in his recent work on *International Trust Laws*, describes the STAR Trust as an "ambitious legislative endeavour".[9] In *The Law of Trusts* by Professors Geraint Thomas and Alastair Hudson,[10] the STAR Trust is considered in detail and is described as "the most ambitious and sophisticated offshore legislation".[11] We should add that we are greatly indebted to these works by Mr Panico and Professors Thomas and Hudson, and also to Anthony Duckworth's work on STAR Trusts,[12] in our consideration of the subject of private purpose trusts.

General issues

12.2 The non-charitable purpose trust is already recognised in Scotland; nearly all, if not all, non-charitable public trusts fall into that category. In such a case the trust may be enforced in the public interest by the Lord Advocate. So far as Scots law is concerned, we do not think that there is any conceptual reason that private purpose trusts should not be recognised. Indeed, already, many commercial trusts might fall into that category, including some investment vehicles and trusts set up in connection with financing transactions.

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[1] In Pt II of the Bermudian Trusts (Special Provisions) Act 1989.
[2] The Channel Islands, the Isle of Man, Mauritius, San Marino and Dubai.
[3] The relevant provisions are reproduced in Appendix B.
[4] Trusts (Guernsey) Law 2007, s 12 (reproduced in Appendix B).
[5] Bermudian Trusts (Special Provisions) Amendment Act 1998, s 12A.
[6] Purpose Trusts Act 2004.
[7] Other models exist for private purpose trusts, usually of a simpler and less well developed nature than the STAR trust. One example is found in the Trusts (Jersey) Law 1984 (as amended), arts 11-14 (reproduced in Appendix B). Others are found in various Canadian provinces: Ontario Perpetuities Act 1990, s 16; British Columbia Perpetuities Act 1996, s 24(1); Alberta Perpetuities Act 2000, s 20; all of the latter are subject to a perpetuity period of 21 years.
[8] David Hayton, "STAR Trusts" (1998) 8 The Offshore Tax Review 43.
[9] OUP, 2010, at para 12.120.
[10] OUP, 2nd ed, 2010.
[11] At para 42.01. See generally the first part of ch 42, written by Professor Thomas.
[12] Anthony Duckworth, *Star Trusts: the Special Trusts (Alternative Regime) Law 1997: Cayman Islands – 2nd Generation of Purpose Trusts and More* (Gostick Hall Publications, 1998).

12.3 In English law, non-charitable purpose trusts are not recognised.[13] The reasons given in the leading case were as follows:

> "There can be no trust over the exercise of which this court will not assume control; or an uncontrollable power of disposition would be ownership and not trust. If there be a clear trust but for uncertain objects, the property, that is the subject of the trust, is undisposed of and the benefit of such trust must result to those to whom the law gives the ownership in default of disposition by the former owner. But this doctrine does not hold good with regard to trusts for charity. Every other trust must have a definite object. There must be somebody on whose favour the court can decree performance."[14]

12.4 The principle that a trust, to be valid, must be for the benefit of identifiable persons or must be for charitable purposes, in the technical sense of that expression, has been recognised in subsequent English and Commonwealth cases.[15] In Scotland however, public trusts other than charitable trusts have always been recognised as valid.

12.5 The reasons for the non-recognition of non-charitable purpose trusts have been the subject of a great deal of discussion.[16] Four principal reasons have been identified.[17] These are:

(i) uncertainty;

(ii) lack of an adequate enforcement mechanism;

(iii) the rule against perpetuities; and

(iv) public policy.

So far as Scots law is concerned, the third of these is easily dealt with; the rule against perpetuities has never been part of Scots law,[18] and we do not propose that any such rule should be enacted. The other three objections, however, merit some consideration.

Uncertainty

12.6 In relation to uncertainty, we do not think that there is any fundamental problem in Scots law. No doubt there is an onus on trusters and those who draft trust deeds for them to ensure that the trust purposes are sufficiently clear and definite, as a matter of both substance and form. In some cases particular trust purposes may fail for uncertainty. In this respect, however, there does not appear to us to be any fundamental difference from public trusts, where there is a requirement that there should be sufficiently definite trust purposes.[19] The fact that some trusts may not be drafted in sufficiently definite form does not appear to

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[13] The law is discussed in Panico, paras 12.02 onwards; the leading case is *Morice v Bishop of Durham* (1804) 9 Ves 399, 32 ER 656 (1st Instance); (1805) 10 Ves 522, 32 ER 947 (on appeal).
[14] *Morice v Bishop of Durham* (1804) 9 Ves 399 at 404-405 per Sir William Grant MR.
[15] *Bowman v Secular Society Ltd* [1917] AC 406; *Leahy v Attorney General for New South Wales* [1959] 2 All ER 300; Re *Endacott* [1968] Ch 232.
[16] See Panico, ch 12 and the authorities cited there.
[17] See Panico, para 12.21.
[18] See our DP on Accumulation, esp Pt 2.
[19] This is subject to the *cy-près* doctrine, which can deal with both initial uncertainty and a subsequent failure of the trust purposes. In relation to private trusts, we discuss this matter below at paras 12.20-12.24.

us to be a reason for barring all such trusts. Historically, the benevolent treatment of public trusts (and trusts that are charitable in the narrower sense) has been justified on the basis of the public benefit that such trusts are designed to produce. Nevertheless, we cannot see any fundamental legal reason for not recognising private purpose trusts, provided that they are framed in sufficiently definite terms. Individuals, corporations and other persons may have perfectly good reasons for setting up purpose trusts; indeed, many existing commercial trusts come close to being purpose trusts.

12.7 An example is a trust whereby assets are held to facilitate a particular financing transaction, for example in relation to a commercial or residential development where numerous parties are involved and further parties will become involved following the sale or letting of the development. In such a case assets are held as collateral for the completion and disposal of the development, but the identity of those who will benefit from the collateral cannot be known. For example the initial developer is likely to sell his interest to another party or other parties, frequently by means of a complex series of arrangements involving sales and leases and on occasion less formal intra-group transfers. Those who contract with the original developer may well transfer their interest on to other parties. The finance for the development is likely to come from outside sources, banks or other investors, and they will take security over the interests held by the parties to whom they provide funding. The trust of collateral is designed to ensure that security is available for any party who suffers loss as a result of the non-completion or defective completion of the development. While such a trust can be forced into the model of a trust for identifiable beneficiaries, it is perhaps more realistic to consider it as a trust set up for the purpose of providing security against the risk that the development will not be completed or will be defectively completed. Another example is the trust used in a securitisation transaction. In such a transaction a finance company entitled to receivables from a large number of debtors typically declares a trust over these receivables in favour of other intermediaries which, using the consumer debts as collateral, sell loan notes to the public. Once again, the trust can be forced into the model of a trust for identifiable beneficiaries, but again it seems more realistic to regard it as a trust designed for the purpose of providing collateral for certain financing arrangements. The fundamental point is perhaps that the dividing line between trusts for identifiable beneficiaries and purpose trusts is not easily drawn.

12.8 The uncertainty objection in English law relates to the so-called "beneficiary principle" whereby it is necessary that a trust should be for the benefit of identifiable persons if it is to be valid, unless it is charitable.[20] This principle does not, however, appear to be part of Scots law, and indeed it is arguable that private purpose trusts can already be created in Scotland.[21] Nevertheless, there is clearly doubt about the matter, and the fact that public trusts are recognised as a category might tend to suggest that private purpose trusts are not

[20] This is discussed at length, in a manner that is essentially hostile to purpose trusts, in an entertaining article by Paul Matthews, "The New Trust: Obligations without Rights?" in Anthony Oakley (ed), *Trends in Contemporary Trust Law*. Other discussion of the same theme is found in an article by Professor David Hayton, "Developing the Obligation Characteristic of the Trust" (2001) 117 LQR 96, and in Thomas and Hudson, paras 42.13-42.15, where the position of STAR trusts is specifically discussed.

[21] Even Professor Matthews, in the article cited immediately above, accepts that Scotland is different. He states (at pp 1-2) the importance in English law of the fact that the beneficiary's personal right against the trustee developed into an interest in the property. He continues: "Had the right remained purely personal [as is, eg, Scots law], it might have developed into a law of obligations rather like the civil law of contract, i.e. voluntarily assumed obligations, without the need for a doctrine of consideration. This in turn might have assisted the development of purpose trusts."

recognised. Whatever the present position may be, we can see no reason why Scots law should follow the English rule.

Public policy

12.9 The fourth objection to purpose trusts is public policy. This is clearly recognised in Scots law in that, to be valid, any trust must give rise to an identifiable benefit.[22] We have considered this principle at some length in our DP on Accumulation.[23] Clearly the principle would apply to private as well as public purpose trusts. Nevertheless, we do not understand why this principle should be a fundamental barrier to the recognition of private purpose trusts; it merely emphasises that such a trust must produce practical benefits. In addition to this principle, it is obvious that any trust purposes must be legal and not otherwise contrary to public policy. These are existing principles, and we can see no difficulties arising from their application.

Enforcement

12.10 The most significant of the four objections to the recognition of private purpose trusts is the second, the lack of an adequate enforcement mechanism. In the case of a trust for named or identified beneficiaries, it is those beneficiaries who have power and title to enforce the trust against the trustees. With a purpose trust, however, there are no named or identified beneficiaries in the normal sense, and consequently some other person must be given power to enforce the trust. In the case of public trusts, enforcement is by the Lord Advocate acting in the public interest. Clearly that mechanism would not be appropriate for private trusts. This problem has been addressed in the jurisdictions that recognise non-charitable purpose trusts, and we are of opinion that if it adopts the private purpose trust Scots law should adopt the same solution. The standard solution, which is found in the Cayman Islands STAR legislation, is to require a person creating a non-charitable purpose trust to appoint an enforcer under the trust deed. The enforcer has power to compel the trustees to observe the provisions of the trust and to take action against them should that be necessary. In this respect an enforcer acts in the same way as the Lord Advocate does in the case of a public trust.

12.11 While the appointment of an enforcer is normally mandatory, in some cases, notably the Cook Islands, Cyprus, Mauritius and Labuan, this is not so. We do not discuss these cases further, however, because we think that enforcement is an important issue and that it should be compulsory to appoint a person who can take action against the trustees should that be necessary.

12.12 A clear example of the use of an enforcer is found in the Cayman Islands legislation relating to STAR trusts; this is now contained in Part VIII of the Cayman Islands Trusts Law (2009 Revision). In the legislation a STAR trust is referred to as a "special trust", the word "special" signifying that the trust is subject to Part VIII of the Trusts Law. An enforcer is defined as "a person who has standing to enforce a special trust".[24] "Standing to enforce" is

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[22] Eg *McCaig v Glasgow University* 1907 SC 231; *McCaig's Trs v Kirk Session of the United Free Church of Lismore* 1915 SC 426; *Aitken's Trs v Aitken* 1927 SC 374; *Lindsay's Ex v Forsyth* 1940 SC 458. See generally Stair Memorial Encyclopaedia, vol 24, para 86.

[23] DP No 142. See esp its paras 2.59-2.76, where the cases cited in the previous footnote are discussed.

[24] Section 95(1). Part VIII is reproduced in full in Appendix B.

defined as meaning the right or duty to bring an action for the enforcement of a special trust.[25] Section 100(1) and (2) of the Trusts Law provides as follows:

> "(1) A beneficiary of a special trust does not, as such, have standing to enforce the trust, or an enforceable right against a trustee or an enforcer, or an enforceable right to the trust property.
>
> (2) The only persons who have standing to enforce a special trust are such persons, whether or not beneficiaries, as are appointed to be enforcers –
>
> (a) by or pursuant to the terms of the trust; or
>
> (b) by order of the court."

12.13 Section 100(1) achieves two objectives. First, it prevents any named beneficiary from taking steps to enforce the trust either against a trustee or against an enforcer. Secondly, it excludes the rule whereby the beneficiaries of a trust, if of full age and capacity, can agree to bring the trust to an end and compel the trustees to distribute the property to them.[26] That is obviously important because a purpose trust is designed to achieve objectives that go beyond the mere benefit of named beneficiaries. So far as the right to enforce the trust is concerned, section 100(2) confers that right on the enforcer or enforcers. Normally an enforcer will be appointed by the settlor, but as an alternative the court is given power to appoint an enforcer. Section 100(4) provides as follows:

> "The court may, on the application of a trustee or an enforcer, appoint an enforcer –
>
> (a) if the terms of the trust require the appointment of an enforcer but –
>
> (i) it is impossible to make the appointment without the court's assistance; or
>
> (ii) it is difficult or inexpedient to make the appointment without the court's assistance;
>
> (b) if an enforcer with a duty to enforce is unable, unwilling or unfit to do so; or
>
> (c) if there is no enforcer who is of full capacity and who –
>
> (i) is a beneficiary; or
>
> (ii) has a duty to enforce and is fit and willing to do so."

12.14 In the event that there is no enforcer who is of full capacity, the trustee is obliged, by section 100(5), to apply to the court within 30 days for the appointment of an enforcer, or for the administration of the special trust under the direction of the court, or for such other order as the court may think fit; failure to do so is an offence carrying a fine. Thus the legislation

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[25] Ibid. "Trust" is defined to include a trust of a power, which is a power where the trustee is obliged to consider whether or not to exercise the power.

[26] Recognised in Scots law in *Miller's Trs v Miller* (1890) R 301 and *Yuill's Trs v Thomson* (1902) 4 F 815. The equivalent English principle is laid down in *Sanders v Vautier* (1841) 4 ER 282.

clearly contemplates that there should at all times be an enforcer who can enforce the provisions of the trust against the trustee.

12.15 Further provisions relating to enforcers are found in sections 101 and 102 of the Trusts Law. Section 101(2) provides that, subject to evidence of a contrary intention, an enforcer is deemed to have a fiduciary duty to act responsibly with a view to the proper execution of the trust. It is generally considered that it is not imperative that an enforcer should be subject to fiduciary duties, and indeed section 101(2) contemplates that possibility if the settlor so directs. Nevertheless, the default position in the Cayman Islands is that an enforcer is subject to fiduciary duties, and we can see obvious practical advantages in that as a default position, in view of the vital role that an enforcer plays in the administration of the trust. Section 101(3) deals with the enforcement of the enforcer's duties; it provides that a trustee or another enforcer or any person expressly authorised by terms of the special trust has standing to bring an action for the enforcement of any duty of an enforcer. In this way the powers under the trust are mutually reinforcing: the enforcer can compel observance of the trustee's duties and the trustee, or another enforcer, can compel performance of the enforcer's duties. The beneficiaries, however, are excluded by section 100(1).

12.16 Section 102 provides that, subject to the terms of his appointment, an enforcer has the same rights as a beneficiary of an ordinary trust to bring administrative and other actions and to make applications to the court concerning the trust. The enforcer also has the same rights as a beneficiary of an ordinary trust to be informed of the terms of the trust, to receive information concerning the trust and its administration from the trustee, and to inspect and take copies of trust documents. The enforcer is given the rights of a trustee of an ordinary trust to protection and indemnity in the performance of his duties, and is further entitled to make applications to the court for an opinion, advice or direction or for relief from personal liability in respect of the performance of his duties. All of these seem to us to be eminently sensible provisions. Finally, in the event of a breach of trust an enforcer has, on behalf of the trust, the same personal and proprietary remedies against the trustee and against third parties as a beneficiary of an ordinary trust. This provision simply follows through the logic of an enforcer's position, that he or she is in the same position as a beneficiary in an ordinary trust in relation to the enforcement of the terms of the trust.

12.17 Under the Cayman Islands STAR trust regime it is only the duly appointed enforcer who can enforce the trust. Section 101(3) provides that proceedings to enforce the enforcer's duties can be brought by a trustee or another enforcer or any person expressly authorised by the terms of the special trust. A question arises as to the person to whom the enforcer's fiduciary duties (if these are not excluded) are owed. Thomas and Hudson comment that, in the case of a pure purpose trust, it cannot sensibly be said that the fiduciary duty is owed to the trust's purposes. Nor does it make sense to say that an enforcer owes such a duty to him or herself, and there is no indication that the duty is owed to the settlor (truster). The conclusion reached is that:

> "Presumably what is meant is that an enforcer is subject to a statutory duty to act and to conduct himself with the same degree of responsibility *as if* he had been appointed an enforcer of a trust for persons."[27]

[27] Thomas and Hudson, para 42.11 (with emphasis in the original).

Nevertheless, there does not appear to be any indication that enforcers in the Cayman Islands, and indeed in other jurisdictions, fail to perform their duties properly, and it may be that the foregoing difficulty is more conceptual than real. Indeed, a similar problem can be said to arise in relation to trustees of a pure purpose trust: the trustees cannot owe such a duty to the trust's purposes, and there is no identified or identifiable person to whom the duties can be said to be owed. Yet purpose trusts can still operate in a perfectly satisfactory manner; the Scottish public trust is the obvious example. Exactly the same is true of charitable trusts that do not have identified or identifiable beneficiaries. Consequently we do not think that the existence of an identifiable person to whom a fiduciary duty is owed is essential; such a duty can, it seems, take an abstract form. As such the concept appears to be workable in practice.

12.18 In the Cayman Islands, as explained above, the offices of trustee and enforcer are mutually reinforcing; each can enforce the duties of the other. While this is essentially circular, it does not appear to have given rise to particular problems in practice. A slightly different approach is found in Bermuda:

> "The Supreme Court may make such order as it considers expedient for the enforcement of a purpose trust on the application of any of the following persons –
>
> (a) any person appointed by or under the trust for the purposes of this subsection;
>
> (b) the settlor, unless the trust instrument provides otherwise;
>
> (c) a trustee of the trust;
>
> (d) any other person whom the court considers has sufficient interest in the enforcement of the trust;
>
> and where the Attorney-General satisfies the court that there is no such person who is able and willing to make an application under this subsection, the Attorney-General may make an application for enforcement of the trust."[28]

In this way the legislation provides for wider enforcement mechanisms, conferring a greater degree of flexibility. This may permit trusts to evolve and adapt. Nevertheless, we think it unlikely that in Scotland the Lord Advocate would be willing to undertake the responsibilities that the Attorney-General of Bermuda undertakes under this section; Bermuda is a much smaller jurisdiction, and the trust industry is likely to have much greater significance there than it has in Scotland. Flexible provisions such as those found in Bermuda depend on a fallback right to enforce the provisions of the trust, which is why the Attorney-General is involved as a "long-stop" enforcer. In Scotland we think that it would almost certainly be preferable to insist on the appointment of a designated enforcer, as is done under the STAR legislation.

[28] Section 12B(1) of the Trusts (Special Provisions) Amendment Act 1998.

Further issues in relation to purpose trusts

12.19 *(i) Formalities for setting up trust*. Under the Cayman Islands legislation, if a trust is to be a STAR trust it must be created by or on the terms of a written instrument, whether testamentary or *inter vivos*, and the instrument must contain a declaration to the effect that Part VIII of the Trusts Law is to apply.[29] We think that, if private purpose trusts were to be introduced in Scotland, a broadly similar provision would be appropriate; we see no practical difficulties from it, and it makes the status of any particular trust quite clear.

12.20 *(ii) The cy-près doctrine*. Scottish public trusts, and charitable trusts in other jurisdictions, are subject to the *cy-près* jurisdiction whereby, if the purposes of the trust become impossible or impracticable of fulfilment, or it is manifestly expedient that the trust purposes should be altered in the light of changed circumstances, the court may pronounce an order permitting the alteration of trust purposes. Specific legislative provision for alteration of the trust purposes is contained in the purpose trust legislation of most of the jurisdictions that permit such trusts. Under the STAR trust regime in the Cayman Islands, section 104(1) of the Trusts Law provides as follows:

> "If the execution of a special trust in accordance with its terms is or becomes in whole or in part –
>
> (a) impossible or impracticable;
>
> (b) unlawful or contrary to public policy; or
>
> (c) obsolete in that, by reason of changed circumstances, it fails to achieve the general intent of the special trust,
>
> the trustee shall, unless the trust is reformed pursuant to its own terms, apply to the court to reform the trust *cy-près* or, if or insofar as the court is of the opinion that it cannot be reformed consistently with the general intent of the trust, the trustee shall dispose of the trust property as though the trust or the relevant part of it has failed."

If private purpose trusts are permitted in Scots law, we are of opinion that a broadly similar provision would be desirable to deal with failure of objects or the possibility that changed circumstances render the alteration of the trust purposes manifestly expedient. The policy considerations are broadly the same as those that apply to public trusts under the common law.

12.21 We have given consideration to whether the jurisdiction to alter trust purposes suggested in our DP on Accumulation[30] might suffice for this purpose, but we have come to the conclusion that, in the case of purpose trusts, something further is required. Two reasons support this conclusion. First, under a conventional trust in favour of named or identified beneficiaries a beneficiary has an interest under the trust deed which can be given effect in a manner that is usually straightforward and which will subsist until his or her death or until the termination of his or her interest by another event. A mere purpose, by contrast, can be terminated or rendered inappropriate by changes of circumstances that can occur in

[29] See s 96 of the Trusts Law (2009 Revision). Failure to meet these requirements means that the trust is an ordinary one: s 96(3).
[30] At paras 5.25-5.42.

a multitude of forms. Something is required to deal with that possibility. Secondly, the beneficiaries under a conventional trust have a continuing interest in the enforcement of the trust according to its terms, subject obviously to the possibility of variation or alteration, whereas there is no such equivalent interest in the case of a mere purpose. For those reasons we think that greater flexibility is required in the case of a purpose trust, and this is best achieved through a version of the *cy-près* jurisdiction. Moreover, the jurisdiction to alter trust purposes suggested in our DP on Accumulation only applies, as a default position, if a trust has been in existence for 25 years or longer. A failure of objects or a change of circumstances making it manifestly expedient to alter the trust purposes can clearly occur earlier than that, and in the case of a purpose trust the result of the change of circumstances or other event could be to render the trust wholly or substantially incapable of fulfilment; there may not be any default beneficiaries who will take the trust income until the twenty-fifth anniversary of its creation. For this reason we think that an equivalent of the *cy-près* jurisdiction must be available as soon as the trust is set up.

12.22 If an equivalent of the *cy-près* jurisdiction were not made available and the purposes of a pure purpose trust failed, the result would be a resulting trust in favour of the truster; this is in accordance with ordinary principles of trust law. That may well have adverse tax consequences, however, and it is most unlikely that any truster would want a resulting trust, even as a default position. In trusts for named or identified beneficiaries, it is usual to provide a long-stop beneficiary to make sure that a resulting trust does not occur. For the reasons discussed in the last two paragraphs, we are of opinion that an equivalent of the *cy-près* jurisdiction would be the most satisfactory way of achieving a broadly similar result.

12.23 We should also mention section 103 ("Uncertainty") of the Cayman Islands Trusts Law.[31] It is designed to permit the trustee or any other designated person (which would presumably include an arbiter or expert appointed for the purpose) to resolve any uncertainty as to the objects or mode of execution of a trust. If that is not possible, the court is entitled to "reform" the trust, under the *cy-près* jurisdiction found in section 104, or to settle a plan for its administration or to make such other order as may be thought expedient with a view to ensuring that the purposes of the trust are fulfilled. Declaring the trust void is clearly seen as a last resort, although it is obviously a possibility if objects are wholly lacking in certainty. We incline to the view that, if private purpose trusts were permitted in Scotland, it would be desirable to include a broadly comparable provision in the legislation, but we would welcome views on this matter.

12.24 *Cy-près* provisions are found in other jurisdictions that permit purpose trusts. For example, Guernsey provides a *cy-près* jurisdiction that is applicable to any trust property that is held for a charitable or non-charitable purpose.[32] The cases where the jurisdiction applies are set out in detail, and include cases where the purpose is fulfilled as far as possible, where it cannot be carried out, or cannot be carried out according to the directions given and the spirit of the gift, or the purpose has ceased in any way to provide a suitable and effective method of using the property, regard being had to the spirit of the gift. There is further provision that, where trust property is held for a charitable or non-charitable purpose, the Royal Court of Guernsey may approve any arrangement which varies or revokes the purposes or terms of the trust or enlarges or modifies the powers of management or

[31] This is reproduced in Appendix B.
[32] See s 59 of the Trusts (Guernsey) Law 2007 (which is reproduced in Appendix B).

administration of the trustees, if the court is satisfied that that is suitable or expedient and is consistent with the original intention of the settlor and the spirit of the gift.[33] An application to that effect may be made by the trustees or by Her Majesty's Procureur (for this purpose the equivalent of the Lord Advocate). The foregoing Guernsey provisions might provide an alternative model in Scotland for a form of *cy-près* jurisdiction, although it would probably be sufficient to confine such a jurisdiction to private purpose trusts, in that public trusts are already catered for by the existing *cy-près* jurisdiction.

12.25 *(iii) Identity of trustee*. Under the STAR trust legislation in the Cayman Islands, a trustee must be a trust corporation licensed to conduct business under relevant Cayman Islands legislation. Section 105(1) of the Trusts Law provides as follows:

> "Except as authorised by an order of the court, or permitted by or pursuant to this section –
>
> (a) the trustee of a special trust shall be, or include, a trust corporation; and
>
> (b) the trustee shall keep in the Islands at the office of the trust corporation a documentary record of –
>
> (i) the terms of the special trusts;
>
> (ii) the identify of trustee and the enforcers;
>
> (iii) all settlements of the property upon the special trust and the identity of the settlor;
>
> (iv) the property subject to the special trust at the end of each of its accounting years; and
>
> (v) all distributions or applications of the trust property."

12.26 The expression "trust corporation" is defined in subsection (2) as "a body corporate licensed to conduct trust business, with or without restriction, under the Banks and Trust Companies Law (2009 Revision) or registered as a private trust company under that Law". Under a power found at subsection (3) the court may authorise non-compliance with subsection (1) on such terms as it thinks fit if it is satisfied that the execution of the trust will not be prejudiced. The foregoing provisions are backed up by criminal sanctions imposed on those who administer special trusts in breach of subsection (1)(a) and any trustee who acts in breach of subsection (1)(b).

12.27 We invite views as to whether comparable provisions should be enacted in Scotland. We can envisage two principal reasons for such a requirement. First, the trustee is required to keep full records of the trust, as specified in section 105(1)(b), and is obliged to do so at its office within the jurisdiction. That could be of great importance if any question arose as to the status or terms of the trust, or if there were any serious question about the propriety of the trustees' actings. Secondly, at least in the case of a pure purpose trust the trustees' duties are not owed to any identifiable beneficiary, as occurs with a standard beneficiary

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[33] Ibid, s 60 (which is reproduced in Appendix B).

trust. The duties are enforceable at the instance of the enforcer, but, since the enforcer's duties are only themselves enforceable by the trustees, any other enforcer or any person appointed by the truster to do so, there is a degree of circularity in the enforcement arrangements. For this reason it may be important to ensure that trustees acting in private purpose trusts are persons of unquestioned integrity. It may also be an advantage that they are subject to a degree of regulatory or disciplinary control.

12.28 So far as Scotland is concerned, the notion of a "trust corporation" in the Cayman Islands sense does not exist and thus some alternative would have to be found if it were thought desirable to restrict those who could be trustees of such trusts. A possible scheme would be to insist that one trustee of such a trust should be a trust company which is a subsidiary of, for example, a bank authorised to conduct business under the relevant banking legislation, or which is controlled by a firm of solicitors or a firm of chartered accountants. Solicitors and chartered accountants are subject to disciplinary rules, and we can see no reason for excluding trust companies controlled by them from the right to be a trustee of a private purpose trust. Indeed, it would be quite practicable to allow trusts in which a solicitor or chartered accountant, rather than a trust company, is one of the trustees. Trust companies that are subsidiaries of authorised banks are likewise subject to a system of regulatory control.

12.29 In any event, we think that the provisions of section 105(1)(b) would be useful. Any trustee of such a trust should be obliged to keep at an office (which could be the office of the designated solicitor to the trust) a documentary record of the various matters enumerated in that provision. This would avoid the risk that a purpose trust might, because of uncertainty in its administration, disappear into some kind of black hole. It would in addition ensure that the enforcer can be provided with information about precisely what is happening in the trust. That seems to us to be important if the enforcer is to perform his or her duties properly.

12.30 *(iv) Requirements for valid trust purposes*. It is clearly essential that the trust purposes in any private purpose trust should be set out with sufficient clarity to be enforced. With that in mind, several jurisdictions that have permitted private or other non-charitable purpose trusts have included in their legislation a declaration of the requirements for valid trust purposes. Under the Cayman Islands STAR trust legislation, the objects of a special trust may be persons or purposes or both, and the purposes may be of any number or kind, charitable or non-charitable, provided that they are lawful and not contrary to public policy.[34]

12.31 A slightly more detailed provision is found in other jurisdictions. The Trusts (Special Provisions) Act 1989 of Bermuda, which authorised purpose trusts, provided that the trust purposes should be specific, reasonable and possible, and that the purposes should not under the law be immoral, contrary to public policy or unlawful.[35] That definition has been followed in a number of other jurisdictions, including the British Virgin Islands[36] and the Isle of Man.[37] The law in Bermuda was changed by the Trusts (Special Provisions) Amendment Act 1998. In this case, it was specified that purpose trusts should be valid on condition that

[34] See s 99 of the Trusts Law (2009 Revision) (which is reproduced in Appendix B).
[35] At s 13(1). As explained shortly below this legislation has since been amended.
[36] Trustee Ordinance 1961, s 84(2), as amended by the Trustee (Amendment) Act 1993.
[37] Purpose Trusts Act 1996, s 1(1).

their purposes were sufficiently certain to allow the trust to be carried out, lawful, and not contrary to public policy.[38] That definition has been followed in the Bahamas[39] and Dubai.[40]

12.32 A different approach has been followed in Guernsey under the Trusts (Guernsey) Law 2007. In Guernsey the validity of non-charitable purpose trust depends only on the existence of an adequate enforcement mechanism:

> "A trust for or including non-charitable purposes created by an instrument in writing and the terms of which provide for –
>
> (a) the appointment of an enforcer in relation to the trust's non-charitable purposes, and
>
> (b) the appointment of a new enforcer at any time when there is none,
>
> is valid and enforceable in relation to its non-charitable purposes."[41]

The issue of illegality of trust purposes is, however, addressed by a provision which applies to trusts of every sort and requires that such trusts should do nothing that is illegal, immoral or contrary to public policy.[42]

12.33 We incline to the view that any legislation should say something about the issue of the certainty of trust purposes, but we would welcome comments as to whether the more prescriptive approach found in Bermuda or the more general approach found in the Cayman Islands and Guernsey would be appropriate. The point of adverting to this issue is simply that it is critical that anyone setting up such a trust should ensure that the purposes are sufficiently definite to be properly enforced and that the trust should confer an identifiable benefit. An express provision in the legislation would draw trusters' attention to these matters.

Use of purpose trusts

12.34 We think that purpose trusts might be very useful in practice; the evidence from jurisdictions that contain purpose trust legislation strongly supports this view.[43] Many of the uses of such trusts are commercial. For example, they may be used for the holding of collateral in project financing agreements; in those cases, the person who is likely to take the benefit of the collateral, should it be enforced, cannot be determined, and what is involved is essentially a commercial purpose rather than the benefit of any particular legal person. Another example is found in securitisation transactions, where the form of trust that is characteristically used at present can better be characterised as a purpose trust (the provision of security for the payment of debts) than a trust for identified beneficiaries. Certain types of off-balance sheet transaction may also be facilitated by using a purpose trust; to take a transaction off-balance sheet, it is necessary that it should be performed by a

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[38] Section 12A.
[39] Purpose Trusts Act 2004, s 3.
[40] Trust Law 2005, art 29(2).
[41] Section 12(1) of the Trusts (Guernsey) Law (which is reproduced in Appendix B).
[42] Ibid, s 11.
[43] Panico, paras 12.01 and 12.89; Thomas and Hudson, paras 42.01-42.06 and 42.62-42.70; Anthony Duckworth, *Star Trusts: the Special Trusts (Alternative Regime) Law 1997: Cayman Islands – 2nd Generation of Purpose Trusts and More* (Gostick Hall Publications, 1998), Pt III.

company that is not a subsidiary of the company that wishes to take the transaction off-balance sheet, and that can readily be achieved if the other company's voting shares are controlled by a purpose trust.[44] Yet another example is found in stakeholder and similar security arrangements,[45] where a purpose trust can be used to hold funds or other property for the purposes of the arrangement. Such trusts can also be useful for holding shares in private companies where the truster wishes the maintenance of the company and its business, and possibly arrangements for the benefit of its employees or the neighbourhood in which it operates, to be taken into account in the arrangements under which the shares are held.[46] Finally, so far as the commercial field is concerned, a purpose trust can be used in support of agency arrangements, to provide some level of security in respect of property that is affected by the agency. If the agency is conducted through a company whose shares, or at least voting shares, are held by a purpose trust, the principal can, through the trust, control the agent company without that company being a subsidiary.

12.35 In the estate planning field, there is evidence that the availability of flexible estate-planning arrangements is regarded as important, and a purpose trust can greatly aid the flexibility of such arrangements. Indeed, it is the simple flexibility of the STAR trust, which may function as both a purpose trust and a beneficiary trust, that is one of its greatest strengths. Mr Duckworth points out that a STAR trust may be particularly appropriate when the settlor intends to benefit persons, perhaps his family, but also wishes to achieve another objective, perhaps to ensure the continuance of his business.[47] If a conventional trust is used in favour of named or identified beneficiaries, the problem is that when the beneficiaries are adult they will be able to terminate the trust and do as they wish with the trust property. A further problem is that the trustee may be concerned that retention of the business would involve a breach of a trustee's duty to act with ordinary prudence in managing investments.[48] If a purpose trust along the lines of a STAR trust is used, the rule in *Saunders v Vautier*[49] (or *Miller's Trustees v Miller*[50]) will be excluded. Likewise, the trustee will be able to follow the purpose of retaining the settlor's business in such a way as to secure its long-term continuation and any resulting benefits to employees for the locality where it operates, without fear that that course is contrary to the duty of prudent investment. In the field of estate planning in relation to private companies, a private purpose trust can readily be used for holding voting stock or for other complex estate-planning purposes. The flexibility is much greater than under a conventional trust.

Further issues

12.36 We should mention certain further issues that arise in relation to private purpose trusts. First, the duties of the trustee of a private purpose trust are not owed to any identifiable persons; although the enforcer can compel performance of the duties, those duties are not owed to him. Thus the trustee's duties are in a sense abstract, without any obligee. The idea of an obligation that is not owed to anyone or that cannot be enforced by

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[44] The non-voting shares carry the economic benefit, and those may be held by the company that promotes the transaction; thus it retains the economic benefit but yields control to the purpose trust.
[45] Referred to in common law jurisdictions as escrow agreements.
[46] This is the type of arrangement that is discussed in much greater detail in ch 13.
[47] Anthony Duckworth, *Star Trusts: the Special Trusts (Alternative Regime) Law 1997: Cayman Islands – 2nd Generation of Purpose Trusts and More* (Gostick Hall Publications, 1998), p 69 onwards.
[48] A problem that is discussed at greater length in ch 13.
[49] (1841) 49 ER 282.
[50] (1890) R 301.

the obligee may seem odd, but such duties are not unknown. In Scots law the obvious example of such duties is the public trust, and in systems based on English law a charitable trust may present similar features. The duties of the trustees of such a trust may be of a very general nature, for example the provision of aid to the third world, or the advancement of Christian missions in a particular locality (which may be large), or the provision of recreational facilities (possibly of no specified type) in a named area. In such cases it is common to find that no beneficiaries can be named or identified. Yet such trusts are valid, and may be enforced in Scotland by the Lord Advocate (or by OSCR if the trust is charitable). From a practical point of view, we cannot see that a private purpose trust is any different. The notion of an obligation that is not owed to an identifiable person may present conceptual difficulties, but it seems to us that they can be overcome and should not be decisive.

12.37 Secondly, a STAR-type trust may have named or identified beneficiaries as well as purposes; indeed it is theoretically possible for it to exist only for the benefit of such beneficiaries. The beneficiaries' interests may be discretionary in nature, as in a conventional discretionary trust, or may be fixed, as with conventional interests in liferents or fee. The question may arise in some contexts as to whether the beneficiaries of such a trust have rights in law as against the trustees. That might occur if the beneficiary were sequestrated or on his or her death or divorce; in such cases it is necessary to determine what the beneficiary's estate is, and that in turn depends on his or her rights under any trust of which he or she is a beneficiary. Under a STAR-type trust, however, a beneficiary has no right to enforce his or her entitlement under the trust; that is left entirely to the enforcer, even if the beneficiary has a fixed interest.[51] In such circumstances it might be argued that, without a personal right of enforcement, the beneficiary cannot be said to have any rights under the trust. We are nevertheless of opinion that the beneficiary does have rights, under the trust: either a right to trust assets or income, if the trust is not discretionary, or a right to be considered for exercise of the trustees' discretion, if it is discretionary. It is generally thought that the ability to enforce is not essential for the existence of a legal obligation and its correlative right.[52] This point is already recognised in Scots law, in that a *jus quaesitum tertio* may be created in favour of a person who is not in existence.[53] In the case of a STAR-type trust, in any event, it should be assumed that both trustees and enforcers will perform their duties properly. That is especially so if it is required that one of the trustees should come from a category of persons that are likely to be of clear integrity, such as solicitors or accountants or the subsidiaries of authorised banks.[54]

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[51] Section 100(1) of the Cayman Islands Trust Law (2009 Revision) provides that a beneficiary of a STAR trust does not, as such, have standing to enforce the trust, or an enforceable right against a trustee or enforcer, or an enforceable right to trust property: see paras 12.12-12.13 above.

[52] A contrary point of view is sometimes advanced by proponents of positive theories of law, as presented, for example, by Austin or Hart. Other theories of law do not seem to share the same difficulty. For example, Neil MacCormick's writing in the Stair Memorial Encyclopaedia, vol 11, paras 1073-1077, argues that it is impossible to hold that the existence of a right is dependent on the ability to enforce it. The law recognises passive rights such as arise when an obligation is owed to a person who lacks legal capacity. MacCormick's view is that the power to enforce a right is merely ancillary to the right itself. We therefore note that, if a personal right to enforce were regarded as the criterion of an obligation, it would not be satisfied by the rights of nations in traditional international law, which lacks any mechanism (short of war or *ad hoc* sanctions) to enforce those rights. A similar point applies to legal systems in their very early stages of development, where a sense of binding legal obligation can exist before any courts or any other enforcement mechanisms have come into existence.

[53] *Morton's Trs v Aged Christian Friends Soc* (1899) 2 F 82, 7 SLT 220. See also Stair Memorial Encyclopaedia, vol 15, para 834.

[54] See paras 12.27-12.28 above.

12.38 One further difference exists between a STAR-type trust and a traditional beneficiary trust: the beneficiaries of the former, even if they are all of full age and full capacity, cannot collectively bring the trust to an end, in accordance with the principle in *Miller's Trustee v Miller.*[55] That has the effect of limiting beneficiaries' rights against the trustees, but that is as far as it goes. It does not, it seems to us, in any way remove the trustees' obligation to perform their duties properly, or the beneficiaries' rights to whatever entitlement they may have under the trust.[56]

12.39 We should briefly note one further possible objection to private purpose trusts, namely that they might be used to defeat the interests of creditors. We do not think that there is any substance in this objection. So far as the truster's own creditors are concerned, protection is afforded by the law relating to gratuitous alienations. In this respect the position of a purpose trust would not be any different from a trust in favour of named or identifiable beneficiaries. So far as creditors of the beneficiaries are concerned, a creditor of a discretionary beneficiary of a STAR-type trust would not be able to attach the beneficiary's interest, because the beneficiary has no right to anything. Exactly the same is true, however, of the beneficiary of a discretionary trust. If a beneficiary of a STAR-type trust has fixed rights, the position is probably the same, unless a trustee in sequestration were held to have greater rights than the beneficiary. When sums are actually paid to the beneficiary, however, they would fall into the sequestrated estate. At the very least, the position of the beneficiary's creditors would be no worse than under a traditional discretionary trust.

Conclusion and questions

12.40 We are of opinion that private purpose trusts could be introduced into Scots law relatively easily. Scots law already recognises the category of public purpose trusts, and we can see no fundamental objection in principle or policy to extending such trusts to those set up for purely private purposes. English law in this area has been troubled by the complexities arising from the "beneficiary principle", stemming from *Morice v Bishop of Durham*[57] whereby, apart from charitable trusts and a small number of anomalous cases, a trust must exist for the benefit of defined persons.[58] Those complexities are not part of Scots law.

12.41 At a practical level, in our opinion three issues arise in relation to private purpose trusts: the need for certainty in the trust purposes, enforcement and public policy issues. We are of opinion that all of these can be catered for. Certainty is ultimately a matter for the draftsman, but we think that the necessary criteria can be set out in the manner already discussed.[59] Enforcement can be dealt with through the institution of an enforcer, as

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[55] (1890) R 301; see para 12.13 above.

[56] The rule in *Miller's Trs* and its English equivalent, *Saunders v Vautier* (1841) 49 ER 282, is not followed in the US where, following the decision of the Supreme Judicial Court of Massachusetts in *Claflin v Claflin*, 149 Mass 19, 20 NE 454 (1889), the courts have generally taken the view that the intentions of a settlor or testator should be carried out in full, without any right in the beneficiaries to terminate trust purposes earlier than contemplated. The rule is found in the Uniform Trust Code at Section 411(b): "A noncharitable irrevocable trust may be terminated upon consent of all the beneficiaries if the court concludes that continuance of the trust is not necessary to achieve any material purpose of the trust. A noncharitable irrevocable trust may be modified upon consent of all of the beneficiaries if the court concludes that modification is not inconsistent with a material purpose of the trust". In *Miller's Trs* a broadly similar approach is found in the dissenting opinion of Lord Young.

[57] (1804) 9 Ves 399, 32 ER 656; (1805) 10 Ves 522, 32 ER 947 (on appeal). See para 12.3 above.

[58] See the discussion in Panico, paras 12.02 onwards.

[59] At paras 12.30-12.33.

discussed above.[60] Public policy is already catered for in Scots law through the principle that any trust must produce an identifiable benefit.[61] We can see no particular difficulty in applying that principle to private purpose trusts. Finally, we should point out that no-one will be compelled to use such trusts; whether they are adopted is entirely a matter for individual trusters.

12.42 Private purpose trusts are already permitted in the legal systems of a significant number of jurisdictions. Apart from the Cayman Islands and Guernsey, they are found in Jersey, the Isle of Man, Belize, Bermuda, the British Virgin Islands, Cyprus, the Cook Islands, Western Samoa and Mauritius; the New Zealand Law Commission are currently giving consideration to whether they might be appropriate in New Zealand law.[62] There is evidence that in the jurisdictions that recognise private purpose trusts the institution is widely used for a significant range of purposes, as described above.[63] We think that such trusts might prove equally useful in Scotland, both for Scots and, possibly, for persons from other jurisdictions. In particular, a purpose trust could be used as the legal structure for certain types of business, possibly in place of a partnership or company, or as the structure for clubs and other unincorporated associations. At present it is possible to achieve many of the functions of a private purpose trust through the use of an incorporated company, but that is widely perceived as cumbersome and inconvenient, and it can have adverse tax consequences. A private purpose trust would allow the same practical result to be reached but in a simpler and more direct fashion; that might prove very attractive. At present, however, we are uncertain as to how much demand there might be for an innovation along these lines. In addition, we would welcome views on whether legislation along the lines of the Cayman Islands STAR legislation would be appropriate; the critical feature of the STAR trust, as against the more typical private purpose trust, is that it can benefit named or identifiable beneficiaries as well as purposes. The advantage of such an arrangement is obviously its extreme flexibility, and there does appear to be evidence that STAR trusts are well regarded and popular. We accordingly ask the following questions:

35. (a) Is it desirable to have legislation expressly permitting the setting up of private purpose trusts (purpose trusts other than the existing category of public trusts) in Scotland?

(b) If so, would legislation broadly along the lines of the Cayman Islands STAR legislation, or alternatively the Guernsey trust law, be appropriate? In particular, is it desirable that such legislation should permit trusts that allow for both purposes and identifiable beneficiaries, along the lines of the STAR legislation? Alternatively, is it sufficient merely to provide for private purpose trusts, leaving conventional trusts to deal with all cases where a trust is set up for identifiable beneficiaries?

(c) In particular, is it desirable that such legislation should include the institution of enforcer? If so, should enforcers be subject to

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[60] At paras 12.10-12.18.
[61] See para 12.9 above.
[62] New Zealand Law Commission, Issues Paper 19 (see fn 4 above), paras 2.63-2.66.
[63] At paras 12.34-12.35.

fiduciary duties along the lines of the Cayman Islands STAR trust legislation?

(d) If private purpose trusts were introduced, should the legislation contain each of the following requirements:

(i) A requirement that the trust purposes should be set out in writing, and should contain a declaration that the special regime for private purpose trusts is to be applicable?

(ii) A statement of the limitations on such trusts, for example that the trust purposes should be specific, reasonable and possible, and should not be unlawful or contrary to public policy? In relation to illegality and public policy, is it sufficient to rely on the existing Scottish principles, including the principle that a trust to be valid must produce an identifiable benefit? Alternatively, should specific provision be made in the legislation incorporating that principle?

(iii) Specific provision for the *cy-près* jurisdiction, as discussed above at paragraphs 12.20-12.24?

(iv) Restrictions on who may be a trustee? In this connection, if restrictions are appropriate, what categories of persons should be authorised to be trustees? We have in mind in particular solicitors and chartered accountants and trust companies controlled by them and trust companies controlled by authorised banks, but we would welcome comments on other categories that might be appropriate.

(v) The exclusion of the rule in *Miller's Trustees v Miller*, as discussed above at paragraph 12.13?

In addition, we would welcome comments on any matters that it is thought might usefully be covered in such legislation.

Chapter 13 Trusts to hold the controlling interest in companies

Background

13.1 A trust may be used to hold the controlling interest in a private company. From the point of view of estate planning, this may be the most sensible way of holding such a shareholding. Nevertheless, the use of a trust for this purpose presents a number of fundamental problems. The difficulties arise principally out of the obligation imposed on trustees to act with ordinary prudence in their management of trust property, and of the trust investments in particular.[1] We considered the law in this area in Part 3 of our Discussion Paper on Breach of Trust[2] and we consider certain aspects of trustees' duties further in this Discussion Paper.[3] Our proposals and questions in this area do not envisage that the basic duty on trustees to use ordinary prudence in the management of trust property should be reduced or abrogated in any way. We do consider the question of immunity clauses,[4] and propose that limitation or exclusion of liability should be permitted but that this should not apply to cases where a trustee is guilty of gross negligence in carrying out his or her duties under the terms of the trust. For present purposes it is sufficient to note that immunity clauses or other clauses which define trustees' duties restrictively are permitted, subject to the exclusion for gross negligence.

13.2 The basic duty that a trustee must use ordinary prudence in the management of trust investments has two important practical consequences in relation to private companies. First, it obliges the trustees to monitor the conduct of directors of the company, and to take action if that is necessary to protect the company's business. An example of that might be a proposal that the company should enter into a venture that was highly speculative, or otherwise exposed it to a serious risk of loss. Secondly, the duty obliges the trustees to deal with the shareholding in such a way as to maximise the beneficiaries' financial advantage. The beneficiaries' interests are paramount; if they conflict with the interests of the company, it is the beneficiaries' interests that must invariably prevail.[5] In some cases this might require trustees to sell their shareholding in a private company and to invest the proceeds in more diversified investments. Alternatively, it might oblige the trustees to accept a takeover bid for the company if that seemed the safest course, even if the directors were anxious to reject the bid because they thought that it undervalued the company's prospects. In all these cases there is a possible conflict between the interests of the beneficiaries and the interests of the company, and the result may be that the company's interests are seriously prejudiced by a decision that the trustees feel compelled to make in the beneficiaries' interests.

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[1] *Raes v Meek* 1889 16 R HL31; *Knox v Mackinnon* 1888 15 R (HL) 83; *Tibbert v McColl* 1994 SLT 1227. These cases are discussed in our DP on Breach of Trust, para 3.2.
[2] Discussion Paper No 123. We refer to this as the "DP on Breach of Trust".
[3] See ch 6.
[4] DP on Breach of Trust, paras 3.18-3.50.
[5] This applies unless there is a contrary provision in the trust deed.

13.3 Apart from these general considerations, a number of particular issues may arise if a trust is used to hold shares in a private company. Examples include the following:

(i) The owner of an established business may not consider the business purely as an investment, but may rather view it in terms of its long-term development. His concerns may include securing the employment of his descendants, and he may also be concerned to protect the interests of employees, or the community in which the business is conducted. In such a case the truster may not want the trust shareholding to be sold merely because the trustees feel that they need to diversify their investments or because they see the possibility of a short-term gain.

(ii) Even in cases where the owner of a business views it as an investment, he may want to take a longer-term view of the business than the duties of trustees would ordinarily permit.

(iii) The owner of a business might also prefer to leave important decisions regarding the running of the business to the directors rather than the trustees. In such a case the duty of the trustees to monitor the directors and to intervene where necessary may be considered undesirable.

(iv) Where a trust controls an entrepreneurial business, carrying a higher rate of risk than the classic balanced investment portfolio, it may be difficult to give precise content to the trustees' duties. Almost no case law exists in this area,[6] and it is not clear what ordinary prudence involves in such a case.

(v) The trustees' obligation to monitor the directors and intervene when necessary can create a potential source of conflict if the truster wishes to remain in charge of the company and to nominate his successors in that position.

(vi) Trustees will usually lack the knowledge, experience and skill that is required to assess business decisions made by directors. Thus interference by trustees in the company's affairs may not be well judged. This problem may be especially acute if the trustee is a professional trust company; the expertise professed by such companies is acting as trustee, not managing a business.

(vii) Apart from the uncertainty regarding the duties of trustees in relation to an entrepreneurial business, it can be said that the requirement of prudence imposed on trustees is incompatible with many aspects of entrepreneurial decision-making.

13.4 It is, of course, possible for a truster to take these problems into account when setting up a trust and to limit or modify the trustees' duty of care in relation to the trust's shareholding in a private company. If private purpose trusts were introduced to Scots law, as discussed in Chapter 12, the possibilities open to such a truster would be significantly increased, in that the trust deed could make specific provision for purposes related to the

[6] One example is *Bartlett v Barclays Bank Trust Co Ltd* [1980] Ch 515.

company's business and its long-term maintenance.[7] It is also possible to structure the company itself to limit the possibility of intervention by the trustees, for example by splitting shares in the company into voting and non-voting shares. It may be that appropriate provisions in the trust deed and the constitution of the company can deal in a satisfactory manner with the majority of cases where a trust is the preferred means of holding shares in a private company.

13.5 Nevertheless, such solutions are, we understand, perceived as having disadvantages.[8] In any event, they require complex drafting, and any mistake in the drafting can have very serious consequences. For this reason it may be desirable to have a specific statutory form of trust that is designed to deal with the problems of a shareholding in a private company. A regime specifically aimed at trusts of this nature could exist either on its own or in parallel with legislation permitting private purpose trusts. In the latter event there would be some overlap, but we do not think that that should cause any practical difficulties. The advantage of a specific regime is that it deals in a very precise way with the difficulties that are set out in paragraphs 13.2 and 13.3 above. A general regime permitting private purpose trusts does not achieve that with nearly the same precision. Consequently we would invite comments on three possibilities: first, that legislation should permit private purpose trusts (whether or not along the lines of the STAR trust);[9] secondly, that legislation should permit trusts to deal with shareholdings in private companies; and thirdly, that legislation should permit both of these, using distinct regimes.

VISTA trusts

13.6 The paradigm example of a trust designed to hold the controlling interest in a company is found in the Virgin Islands Special Trusts Act 2003 ("VISTA").[10] This enables trusts in the British Virgin Islands, known as VISTA trusts, to be created in terms designed to avoid the problems that arise when a conventional trust owns a controlling shareholding in a company.

13.7 The primary purpose of the Special Trusts Act is stated in section 3:

> "The primary purpose of this Act is to enable a trust of company shares to be established under which
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> (a) the shares may be retained indefinitely; and
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> (b) the management of the company may be carried out by its directors without any power of intervention being exercised by the trustee."

13.8 It can thus be seen that the Act addresses directly the two main problems presented by the existing rules on prudent investment: the shareholding in the private company need not be disposed of even if that appears desirable according to the criterion of prudent investment, and the management of the company is entrusted to the directors without any interference from the trustee. These purposes are developed in the following sections of the Act, notably sections 5 to 9. Section 5 sets out the trustee's duties in relation to designated

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[7] See paras 12.34-12.35.
[8] See Panico, para 12.141 onwards, and Thomas and Hudson, para 42.25.
[9] See para 12.1 above (and ch 12 generally) for an explanation of the STAR trust.
[10] The Act is reproduced in Appendix B.

shares.[11] Such shares are held by the trustee on trust to retain them, and that duty to retain is to have precedence over any duty to preserve or enhance the value of the trust fund. Section 5(3) provides that the trustee is not to be accountable for losses arising directly or indirectly from holding rather than disposing of designated shares. Under subsection (4), the excluded losses include the absence or inadequacy of financial return, any decrease in value of designated shares, the results of speculative or imprudent activities of the company and any act or omission of the directors, regardless of whether it is made or carried out in good faith. These are far-reaching provisions which effectively negate the trustee's duty to display ordinary prudence in relation to the holding of the designated shares.

13.9 Section 6 of the Act contains restrictions on the trustee's powers in relation to designated shares. Section 6(2) provides that voting or other powers in respect of designated shares are not to be exercised by the trustee so as to interfere in the management or conduct of any business of the company. Moreover, the trustee is directed to leave the conduct of business and all decisions as to the payment or non-payment of dividends to the directors, and is not to compel the payment of any dividend. Section 6(3) provides that a trustee of designated shares is not to take steps to instigate or support any action by the company against any of its directors for breach of duty to the company; is not to take steps to procure the appointment or removal of any of the directors; is to take no steps to wind up the company (subject to a limited power in section 9); and is not to apply to the court for any form of relief or remedy in relation to the company. The effect of this provision is to prevent the trustee from interfering in the running of the company. The directors are protected from action by the trustee, and the trustee is unable to compel the company to pay any dividend.

13.10 Section 7 of the Act provides that the trust instrument may contain rules for determining the manner in which voting and other powers in relation to the directors of the company should be exercised by the trustee. Those rules may stipulate a number of matters; examples include a requirement that the trustee ensure that a particular person should hold or retain office as director, or that a particular person should be appointed to the office of director at some future date or upon some future event.

13.11 Section 8 provides a procedure whereby, if an "interested person" has a complaint concerning the conduct of the company's affairs, and the ground for that complaint is "permitted", the interested person may call upon the trustee to intervene in the affairs of the company to deal with the complaint. "Interested person" is defined in section 2(2), and covers a beneficiary, the object of any discretionary power, the parent or legal guardian of any minor falling within the foregoing categories, and a protector. A "permitted" complaint is one that falls within grounds for complaint specified in the trust instrument; nevertheless, in terms of section 8(2), the trust instrument need not specify any permitted grounds for complaint. This section is designed to provide a kind of safety valve to deal with cases where there is a genuine complaint by the beneficiaries of the trust or those representing their interests as to the manner in which the company's business is carried out. It only applies, however, if the trust instrument so permits, and then only to the extent that is expressly permitted by the trust instrument.

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[11] Section 4 provides that the terms of a trust may direct that the provisions of the Act should apply to specified shares which are referred to as "designated shares" (the definition being contained in s 2(1)).

13.12 Section 9 permits the trustee to dispose of the designated shares, but normally only with the consent of the directors (or a majority of the directors) and such consents, if any, as are required by the trust instrument. This provision permits sale of the designated shares but in a manner that will, generally speaking, be under the control of the directors of the company, and possibly of another person appointed by the settlor.

13.13 Section 10 enacts provisions whereby the court may grant relief in respect of any breach of duty by the trustee. Section 11 provides that, where it is shown to the court that the retention of the designated shares is no longer compatible with the wishes of the settlor, the court has power to order or authorise a sale or other disposal of those shares. Section 12 provides that the beneficiaries are not to be entitled to call for or direct a transfer of the designated shares or to terminate or modify the trust relating to such shares, if that is excluded by the trust instrument. Thus the rule commonly referred to as the rule in *Saunders v Vautier*[12] in the British Virgin Islands and other common law jurisdictions and the rule in *Miller's Trustees v Miller*[13] in Scotland may be excluded from VISTA trusts. Finally, three short provisions at the end of the Act should be noticed. Section 13 provides that a trustee of designated shares shall not be a director of the company. Section 14 provides for ascertainment of the wishes of the settlor. Section 15 provides that a trustee of designated shares is to have no fiduciary responsibility or duty of care in respect of the assets of, or the conduct of the affairs of, the company, except when acting or required to act on an intervention call in terms of section 8.

13.14 The provisions of the Special Trusts Act are relatively detailed. They provide an alternative regime designed to deal with the specific problems that arise when a trust holds a majority shareholding in a company and the truster wishes that shareholding to be used in such a way as to further the interests of the company rather than the narrower interest of the beneficiaries. It may be that such provisions are more elaborate than is required to deal with any perceived problem in Scotland. If that were so, a further possibility is exemplified by the Bahamian Purpose Trusts Act 2004, which permits the setting up of purpose trusts and states that a trust may be declared "for a non-charitable purpose, including, exclusively or otherwise, the purpose of holding, or investing in shares in a company or any other assets constituting the trust property".[14] This makes it clear that a trust may be set up for the purpose of holding shares in a company, without any further purposes beyond that. In this way the company is in effect treated as an end in itself. That result can probably be achieved under the existing law, in that the named beneficiary of a trust may be any legal person, including a company. Thus there is no objection to setting up a trust for behoof of a company. The feature that is different in the Bahamian legislation (and more strongly so in the VISTA legislation) is that the company's own shares are held for its benefit. At first sight this appears conceptually odd, but in fact all that it means is that the shares should be used to advance the interest of an identified person, in this case the company. In practice the

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[12] (1841) 49 ER 282.
[13] (1890) R 301.
[14] Section 3(1). In full, it provides:
"3(1) A trust may be declared by trust instrument for a non-charitable purpose, including, exclusively or otherwise, the purpose of holding, or investing in shares in a company or any other assets constituting the trust property if–
(a) the purpose is possible and sufficiently certain to allow the trust to be carried out;
(b) the purpose is not contrary to public policy or unlawful under the laws of The Bahamas;
(c) the trust instrument specifies the event upon the happening of which the trust terminates and provides for the disposition of surplus assets of the trust upon its termination."
Similar provision is found in art 29(2) of the Trusts Law 2005 of the Dubai International Financial Centre.

provisions appear to work in a perfectly satisfactory manner, and seem to be reasonably popular.[15] The conclusion expressed in Thomas and Hudson is that:

> "VISTA provides opportunities for many individuals who would otherwise set up trusts to hold share in their companies but who previously felt disinclined to do so as a result of the existing prudent trustee rules. […] Essentially the Act sets up a special trust system which is ideally suited to the ownership of shares in private companies, just as the English Settled Land Act 1925 and the English Trusts of Land and Appointment of Trustees Act 1996 set up special trust systems the provisions of which were specifically crafted to deal with the unique features of particular types of assets."[16]

13.15 We should note one further feature of the VISTA trust. Under section 4(1) of the Act, the designated shares must be shares in a Virgin Islands company, although there is no bar on bringing other companies within the purview of the legislation by making use of a Virgin Islands holding company. This restriction obviously simplifies the possible interaction of the special trust regime contained in the VISTA legislation and the rules, including the mandatory rules, of any given trust of company law. Nevertheless, we do not think that there is any particular need for a system specially designed to hold a majority shareholding in a company to specify that the company must be incorporated in the same jurisdiction as the trust. Conflicts might occur between the trust legislation and the relevant companies legislation, but such cases would simply have to be dealt with on an individual basis. In any event, at least in the jurisdictions that recognise trusts, holdings by trustees are a well known feature of commercial life and the general policy of company law is to ignore the existence of any trust obligations that apply to the shares.[17] So far as United Kingdom company law is concerned, we do not think that there is any insuperable difficulty to the use of trusts along the lines of the VISTA legislation. The most significant provision is section 168 of the Companies Act 2006, which provides that a company may by ordinary resolution remove a director before the expiration of his period of office. This provision is mandatory so far as the company is concerned. It does not, however, restrict the way in which shareholders may cast their votes in any resolution to remove a director. Indeed, in the very common case where the directors own a controlling shareholding, it cannot be expected that section 168 will provide any sort of effective sanction against them. Consequently, the fact that a trustee is prohibited from taking steps to procure the appointment or removal of any directors (as provided in section 6(3) of the Special Trusts Act) is immaterial. In any event, section 8 of the Special Trusts Act permits intervention in circumstances defined in the trust deed, although there is no obligation for the trust deed to permit such intervention. Nevertheless, we would invite views as to whether there are any provisions of United Kingdom company law that would make the use of a VISTA-style trust impossible or undesirable.

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[15] See Thomas and Hudson, paras 42.62-40.70.
[16] Ibid, paras 42.62-42.63.
[17] An exception is found in the Scottish practice of registering trust holdings as such, but the relationship of trustee and beneficiary is a matter with which UK company law is not in any way concerned.

13.16 In the light of the foregoing discussion, we ask the following questions:

36. (a) Does the trustee's duty of prudence in relation to investments give rise to practical difficulties in respect of controlling shareholdings in private companies? If so, what is the general nature of such difficulties?

(b) If such difficulties are significant, would it be desirable for Scots law to adopt a form of trust based, with appropriate modifications, on the VISTA legislation? If so, should the provision for such trusts be in addition to legislation for purpose trusts, as discussed in Chapter 12?

(c) If such provision would be desirable, what modifications if any would be appropriate?

(d) Would the use of a VISTA-style trust in Scotland raise any issues as to the compatibility of such legislation with United Kingdom company law?

37. (a) Alternatively, if the rules on prudent investment are a practical problem, would it be possible to deal with the difficulty through the medium of a purpose trust by providing that a trust might be declared for the purpose of holding or investing in shares in a designated company?

(b) If this approach is preferred, should any further specific modifications be made to basic legislation permitting private purpose trusts in order to deal with the holding of a controlling interest in a private company?

The foregoing question is based broadly on section 3(1) of the Bahamian Purpose Trusts Act 2004.[18] It assumes that legislation permitting private purpose trusts would be enacted along the lines discussed in Chapter 12 of this Discussion Paper.

[18] Discussed at para 13.14 above; the legislation is set out in fn 14.

Chapter 14 Error and other defects in trustees' exercise of discretionary powers

14.1 A further issue on which we would like to consult, at a very general level, is the way in which errors (or other defects) in trustees' exercise of their discretionary powers can be corrected. This involves consideration of the English rule that is usually known as the rule in *Hastings-Bass*.[1] Very shortly before this paper was ready to be published, the Court of Appeal issued a decision reviewing and restating this rule in greatly restricted form in two conjoined cases, *Pitt v Holt* and *Futter v Futter*.[2] The leading judgment is given by Lloyd LJ who, in a case heard shortly before he was promoted to the Court of Appeal, had set out the generally accepted formulation of the rule:

> "Where trustees act under a discretion given to them by the terms of the trust, in circumstances in which they are free to decide whether or not to exercise that discretion, but the effect of the exercise is different from that which they intended, the court will interfere with their action if it is clear that they would not have acted as they did had they not failed to take into account considerations which they ought to have taken into account, or taken into account considerations which they ought not to have taken into account."[3]

It has been suggested that *Hastings-Bass* itself did not establish any principle upon those lines.[4] Nevertheless, what (until the recent decision of the Court of Appeal) was understood to be the rule has been applied in a large number of cases in England and in other jurisdictions.[5] It seems that the principle proved useful in cases where trustees had made a discretionary decision that ultimately turned out to have been based on false premises or a false understanding of the likely consequences. Frequently the misunderstanding related to the tax consequences of the trustees' decision. Consequently, the rule attracted criticism from Revenue and Customs, who have began to oppose its application in a number of cases before the courts and tax tribunals.[6] They were the appellants in *Pitt*.

14.2 Lloyd LJ's judgment in *Pitt* is lengthy and reviews the many relevant authorities. The full implications will no doubt emerge over the coming weeks and months, as practitioners' and academics' comments begin to appear. (We also do not know whether there will be an

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[1] *Re Hastings-Bass*, [1975] Ch 25. As will be clear from what follows the rule has been developed a great deal from its initial formulation, and we explain at para 1.20 that the most recent development came shortly before this Discussion Paper was ready to be published.

[2] [2011] EWCA Civ 197, 9 March 2011. The appeals are from *Pitt v Holt* [2010] EWHC 45 (Ch) and *Futter v Futter* [2010] EWHC 449 (Ch).

[3] *Sieff v Fox* [2005] EWHC 1312; [2005] 1 WLR 3811 at para 119.

[4] Lord Neuberger, "Aspects of the law of mistake: re Hastings-Bass" (2009) Trusts and Trustees 189.

[5] Eg Jersey (*Re K Holdings Trust* [2009] JRC 245; *Re Sanne Trust Co Ltd* [2009] JRC 25A), Guernsey (*Gresh v RBC Trust Co (Guernsey) Ltd* (judgement 25/2009)), the Isle of Man (*McBurney v McBurney* [2009] WTLR 1489), and the Cayman Islands (*A v Rothschild Trust Cayman Ltd* [2004-05 CILR 485]; *Re Wang Trust* (April 2010, unreported)). We set out the new formulation of the rule in para 14.2.

[6] See HM Revenue & Customs, Tax Bulletin 83, available at http://www.hmrc.gov.uk/bulletins/tb83.htm.

appeal to the Supreme Court.) There is a useful summary towards the end of Lloyd LJ's judgment of the extent of "the *Hastings-Bass* rule":

> "222. *The Hastings-Bass rule*. The principle promulgated first by Warner J in *Mettoy*, developed thereafter, and set out by myself in paragraph 119(i) of my judgment in *Sieff v Fox* is not correct. Two kinds of case need to be distinguished.
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> i) On the one hand there may be a case in which, for example because of an inadvertent misunderstanding of the position, an act done by trustees in the exercise of a dispositive discretion is not within the scope of the relevant power. If so it is void. That was the case in *Re Abrahams' Will Trusts*, as it was interpreted in *Re Hastings-Bass*. It would have been the case in *Re Hastings-Bass* but for the Court of Appeal having allowed the appeal by the trustees.
>
> ii) On the other hand, the case may be one in which the trustees' act in exercise of their discretion is within the terms of their power, but is said to have been vitiated by their failure to take into account a relevant matter, or their taking something irrelevant into account, when deciding to exercise, and exercising, the discretion. The correct approach to such cases is dealt with at paragraph [127] above.[7] The trustees' act is not void; it may be voidable. To be voidable it must be shown to have been done in breach of a fiduciary duty of the trustees. The duty to take relevant, and no irrelevant, matters into account is a fiduciary duty. Relevant matters may include fiscal consequences of the act in question. However, if the trustees fulfil their duty of skill and care by seeking professional advice (whether in general or in specific terms) from a proper source, and act on the advice so obtained, then (in the absence of any other basis for a challenge) they do not commit a breach of trust even if, because of inadequacies of the advice given, they act under a mistake as to a relevant matter, such as tax consequences. In the absence of a breach of trust, the trustees' act is not voidable. Even if it is voidable, it cannot be avoided unless a beneficiary seeks to have it avoided, and a claim to that effect will be subject to the discretion of the court and to the usual range of equitable defences.
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> iii) The same principles may apply to acts on the part of other persons in a fiduciary position, of whom a receiver appointed under the Mental Health Act 1983 is an example."

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[7] Para 127 reads: "The cases which I am now considering concern acts which are within the powers of the trustees but are said to be vitiated by the failure of the trustees to take into account a relevant factor to which they should have had regard – usually tax consequences – or by their taking into account some irrelevant matter. It seems to me that the principled and correct approach to these cases is, first, that the trustees' act is not void, but that it may be voidable. It will be voidable if, and only if, it can be shown to have been done in breach of fiduciary duty on the part of the trustees. If it is voidable, then it may be capable of being set aside at the suit of a beneficiary, but this would be subject to equitable defences and to the court's discretion. The trustees' duty to take relevant matters into account is a fiduciary duty, so an act done as a result of a breach of that duty is voidable. Fiscal considerations will often be among the relevant matters which ought to be taken into account. However, if the trustees seek advice (in general or in specific terms) from apparently competent advisers as to the implications of the course they are considering taking, and follow the advice so obtained, then, in the absence of any other basis for a challenge, I would hold that the trustees are not in breach of their fiduciary duty for failure to have regard to relevant matters if the failure occurs because it turns out that the advice given to them was materially wrong. Accordingly, in such a case I would not regard the trustees' act, done in reliance on that advice, as being vitiated by the error and therefore voidable."

14.3 The rule has not been applied in Scotland; indeed, so far as we are aware, no attempt has been made to argue that it should apply. There has, however, been an interesting article by Mr Derek Francis[8] suggesting how an analogous principle might be evolved in Scotland on the basis of the decision in *Dundee General Hospitals v Bell's Trustees.*[9] In that case, Lord Reid considered the circumstances in which the discretion of trustees might be reviewed. He expressed the view that this might be possible:

> "If it can be shown that the trustees considered the wrong question, or that, although they purported to consider the right question, they did not really apply their minds to it or perversely shut their eyes to the facts or that they did not act honestly or in good faith then there was no true decision."[10]

14.4 That principle approaches what is now the rule in *Hastings-Bass*, as set out in paragraph 14.2 above. It proceeds on grounds, analogous to those that apply to judicial review of administrative action, that require the court to hold that in effect there was no proper decision at all. (The rule in *Hastings-Bass* is also based on the law of mistake,[11] although there has been a good deal of confusion in the cases about the precise manner in which it proceeds.[12]) We will take time to consider the Court of Appeal's full decision in *Pitt*, and we may decide to issue a short paper on matters raised by that case in the near future.[13] In the meantime it seems to us that two questions arise that are relevant to our present project: first, should a rule dealing with errors and other deficiencies by trustees in exercising their discretionary powers be incorporated into Scots law, and if so should such incorporation be in statutory form? We think that, if such a rule is to be incorporated, statutory provision would be desirable; the English cases which preceded the Court of Appeal's decision in *Pitt* – which were influential in other jurisdictions,[14] whose reaction to the recent decision is yet to be seen – are far from clear as to the basis for the rule, and there has been some critical academic commentary.[15] We would, therefore, like to know whether there is any support for, or opposition to, an appropriate statutory enactment. We accordingly ask the following question:

38. Is there support for, or opposition to, the statutory enactment of a rule which would enable the exercise of trustees' discretionary powers to be reduced or otherwise altered if the trustees were in error as to the considerations that ought to have been taken into account by them in the exercise of their power?

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[8] Derek Francis, "*Hastings-Bass* and his Scottish friends" 2008 SLT (News) 161.
[9] 1952 SLT 270; 1952 SC (HL) 78.
[10] 1952 SLT 270 at 275; 1952 SC (HL) 78 at 92.
[11] See *Pitt v Holt; Futter v Futter*, cited in fn 2 above, at paras 164-210 and 223.
[12] See Michael Ashdown, "In Defence of the Rule in *Re Hastings-Bass*" (2010) 16 Trusts and Trustees 826.
[13] One point which strikes us about the effect of the Court of Appeal's decision – and which Lloyd LJ recognises in para 128 of his judgment – is that where trustees rely on negligent or incorrect professional advice (eg on tax) it may be hard for the beneficiaries to recover the resulting loss to the trust. Hitherto, the *Hastings-Bass* rule allowed trustees to seek to have their actions based on such advice declared void, and many successfully did so. It is difficult to imagine that the beneficiaries would have similar prospects of success in an action of professional negligence in respect of defective advice.
[14] See fn 5 above.
[15] Most notably in the article by Lord Neuberger cited at fn 4 above; in a further article by Lord Walker of Gestingthorpe, "The limits of the principle in *Re Hastings-Bass*" (2002) 4 Private Client Business 226; and in a recent article by Richard Nolan and Adam Cloherty, "Taxing times for *Re Hastings-Bass*" (2010) 126 LQR 513. In favour of a version of the rule, see Michael Ashdown, "In Defence of the Rule in *Re Hastings-Bass*" (2010) 16 Trusts and Trustees 826.

Chapter 15 List of questions and proposals

1. Are there any further matters, beyond those considered in this and earlier discussion papers in the trust project, that we ought to consider in our report and draft Bill? In this connection, we are particularly concerned to know whether there are any recent developments in the commercial and investment world that should be reflected in Scottish Trusts legislation. This applies both to commercial and financial developments within the United Kingdom and to the position internationally, where new forms of trust or new procedures may be appearing that could usefully be replicated in Scotland.

   (Paragraph 1.21)

2. Would there be an advantage in Scotland's having a comprehensive statutory statement of trust law along the lines of, for example, the Trusts (Jersey) Law?

   (Paragraph 2.4)

3. Where a person suffers loss as a result of some act or omission of the trustees (or anyone for whom they are responsible) in the course of administering the trust, the trustees as a body will be liable to make reparation for such loss. In addition, any individual trustee who is personally at fault will be liable jointly and severally with the trustees as a body, and in that event any damages awarded against the individual trustee will be payable out of his or her private patrimony. In all such cases, however, it should be essential that the claim, so far as directed against an individual trustee, is on the basis that he or she was personally at fault.

   (Paragraph 3.11)

4. It is not necessary to provide a statutory definition of "personal" liability, or of the circumstances in which personal liability is incurred. That matter should be left to the judgment of the court, but our report should contain a more detailed discussion of the circumstances in which such liability will be incurred.

   (Paragraph 3.12)

5. We further ask if, contrary to the foregoing proposal, it is thought that a statutory definition of the circumstances in which a trustee incurs personal liability should be provided, what criteria might be used in such a definition?

   (Paragraph 3.12)

6. The body of trustees and any individual trustee who is personally at fault should each have a right of relief against the other, that right being subject to the power of apportionment in section 3(1) of the Law Reform (Miscellaneous Provisions) (Scotland) Act 1940.

(Paragraph 3.13)

7. Is it appropriate to make provision in legislation for the obtaining of insurance by trustees? If so, how might such an obligation be formulated?

(Paragraph 3.16)

8. (a) Where trustees are pursuers in an action or other legal proceedings, they should be personally liable for any award of expenses made in favour of the defender, but they should be entitled to apply to the court for an order excluding such personal liability. In order to do so, they would require to satisfy the court that the assets of the trust were sufficient to pay the defender's expenses if successful in his or her defence, or alternatively that other security exists for payment of such expenses.

(b) Where trustees are defenders in an action or other legal proceedings, any award of expenses in favour of the pursuers should be enforceable against the trust estate, with no recourse against the trustees' private patrimonies.

(c) The foregoing provisions should be without prejudice to the court's power to impose personal liability in cases where the trustees have engaged in unnecessary litigation or have behaved improperly, in the situations set out in footnote 5 above.

(Paragraph 4.13)

9. The court should have power to dispense with personal liability as set out in proposal 8(a) in any case where such liability would be inequitable or unfair.

(Paragraph 4.14)

10. Do you agree with the view expressed in paragraph 5.8 above?

(Paragraph 5.9)

11. Should it be set out in statute that client money held by a solicitors' firm (or other professional firm) is held on trust?

(Paragraph 5.10)

12. If you answer yes to question 10, should the rule apply regardless of whether the relevant assets were held by trustees immediately before being transferred to the nominee (as opposed to being held by a person in his or her own right)?

(Paragraph 5.11)

13. What is the likely impact on the market of a rule requiring a nominee to hold on trust assets transferred to it by another person? Any supporting evidence would be welcomed. Would the impact be lessened if the rule were restricted to cases in which the transferor of the assets is a body of trustees?

(Paragraph 5.12)

14. Do you consider the existing law relating to the custody of trust documents and assets to be satisfactory? If not, what changes should be made?

(Paragraph 5.13)

15. Unless otherwise provided by statute, in carrying out their trust duties –

(a) Every trustee should have to use the same care and diligence that a person of ordinary prudence would use in managing the affairs of others.

(b) An unremunerated trustee who has professional qualifications or business experience should be subject only to the foregoing duty unless he or she is instructed to provide professional or other specialised advice to the trust. In the latter event, the trust will be required to use any special knowledge or expertise that it is reasonable to expect of a member of his or her profession or business.

(c) A trustee who provides professional trust services and is remunerated for doing so should be required to exercise the level of skill and care that it is reasonable to expect of a member of his or her profession or business.

(Paragraph 6.11)

16. Provision should be made in the Rules of Court for case management procedures in trust cases in the Outer House. These should be modelled on the existing procedures used in the Commercial Court.

(Paragraph 7.5)

17. (a) The Outer House of the Court of Session should have exclusive jurisdiction in relation to applications:

(i) under the legislation replacing the Trusts (Scotland) Act 1921;

(ii) relating to endowments under Part VI of the Education (Scotland) Act 1980;

(iii) dealing with the administration of trusts or the office of trustee, including *cy-près* applications; and

(iv) for directions in relation to the administration of a trust.

(b) Petitions under section 1 of the Trusts (Scotland) Act 1961 (variation of trusts) or any replacement for that legislation should be presented to the Outer House rather than, as at present, to the Inner House.

(c) The rules of the Court of Session should provide that in all such categories of case the Lord Ordinary has power to remit the application to the Inner House in any case of particular difficulty; and that where appropriate a reclaiming motion against the Lord Ordinary's decision should be competent.

(d) The part of section 26 of the Trusts (Scotland) Act 1921 (or any replacement for that legislation) which requires the Inner House to settle a draft scheme by the Lord Ordinary for administration of a charitable or permanent endowment should be repealed.

(e) A simple non-technical procedure should be devised whereby applications relating to trusts and their administration may be made by trustees or by any other interested party. Such applications would be heard in the Outer House, with the possibility of reclaiming to the Inner House.

(Paragraph 7.19)

18. How common are *ex officio* trustees in Scottish trusts? To what extent are problems involving *ex officio* trustees common in the administration of trusts? Have consultees experienced issues surrounding the resignation or removal of the office of the *ex officio* trustee?

(Paragraph 8.17)

19. Are consultees in favour of a new statutory power in relation to non-charitable trusts to allow for (i) the removal of an office as trustee (where the office-holder is an *ex officio* trustee); (ii) the replacement of such an office with another office, the holder of which is to act as an *ex officio* trustee; and (iii) a power for an *ex officio* trustee to resign in favour of a nominated replacement individual or office-holder?

(Paragraph 8.17)

20. If so, are there any reasons for such a statutory power to differentiate between public/private and charitable trusts, except to the extent that the power would be exercised by the courts, and OSCR respectively?

(Paragraph 8.17)

21. Are there are any other issues surrounding *ex officio* trustees which the Commission might usefully address?

(Paragraph 8.17)

22. Section 16 of the Trusts (Scotland) Act 1921 and the Court of Session's common law powers to authorise advances of capital should be replaced by a new statutory provision along the following lines:

Trustees should have power to advance up to half of a beneficiary's share in the capital of the trust fund where:

(a) the trust deed does not expressly prohibit advancement of capital;

(b) at the date of the advance the beneficiary has a right to all or part of the capital of the trust estate which is vested, is vested subject to defeasance or diminution by the occurrence of some uncertain future event, or will vest provided some uncertain future event occurs;

(c) the advance would be, in their view, for the maintenance, education or benefit of the beneficiary;

(d) every person with a prior life or other interest who would be prejudiced by the advance consents.

The power would be a default power, and would be superseded by any contrary provision in the trust deed.

(Paragraph 9.15)

23. The court should continue to have power, on application, to authorise an advance where a person with a prior life or other interest who would be prejudiced by the advance:

(a) is incapable of consenting and a reasonable person in his or her position would have consented; or

(b) is withholding consent unreasonably.

(Paragraph 9.15)

24. The trustees should have authority to impose any condition upon the advance, whether as to repayment of the sum advanced, payment of interest, giving security, or otherwise; and at any time after imposing any such condition, the trustees should be entitled, either wholly or in part, to waive the condition or release any obligation undertaken or any security given by reason of the condition.

(Paragraph 9.15)

25. The trustees should be entitled to place the sum advanced in a new trust for the beneficiary, even if others may thereby gain incidental benefit.

(Paragraph 9.15)

26. (a) As a general rule, should trustees be obliged to inform a person that he or she is a beneficiary of the trust? If so, what exceptions should be made? Should they be based on the age and capacity of the beneficiary, and/or on whether the beneficiary has a vested interest or not? Are there any other relevant considerations?

(b) Should any such general rule apply also to executors, i.e. should an executor be obliged to inform a person that he or she is a testamentary beneficiary, is entitled to legal rights, or has intestate succession rights (as appropriate)?

(c) Should the rule, and any exceptions, be set out in statute?

(Paragraph 10.5)

27. Should the rule of Scots law be that trustees owe a duty to make available to a beneficiary, on request, relevant information in trust documents? (We specify what we consider to be such information in paragraph 10.13 below.) If not, on what other basis should the beneficiary's right to information be dependent?

(Paragraph 10.12)

28. Do you agree with, or have any comments on, our analysis set out in paragraphs 10.13-10.15 above as to what information is disclosable? Should there be a statutory list of documents whose information is disclosable (other than in exceptional circumstances, for which judicial discretion would normally be expected), and if so should it be the list in paragraph 10.13?

(Paragraph 10.17)

29. (a) Should a stipulation of the following kind be effective, namely a stipulation by a truster that information which would otherwise be disclosable at the request of a beneficiary is not to be disclosed?

(b) If so, are there any types of information in relation to which such a stipulation may not be made? (If possible, it would be helpful for responses to refer to the list at paragraph 10.13.) Should any other conditions be placed on such a stipulation for it to be effective?

(c) Should the court be able to review any such stipulation, on the basis that it counts as a trust purpose, under the proposed jurisdiction outlined in our Discussion Paper on Accumulation of Income and Lifetime of Private Trusts (DP No 142) at proposal 6?

(Paragraph 10.19)

30. If a special regime for private purpose trusts, with an enforcer, were introduced into Scots law, should the rule for such trusts be that, as with STAR trusts in the Cayman Islands, the trustees are obliged to provide information about the trust to the enforcer but not to any beneficiaries of the trust? Alternatively, for such trusts should there be a default rule that information is to be provided to an enforcer but not to beneficiaries, such a rule to apply if the truster makes no provision to the contrary?

(Paragraph 10.23)

31. In either event, should the information that is to be provided be as contemplated in paragraph 10.13 above?

(Paragraph 10.23)

32. If a protector is appointed to a trust, he or she should have a right to examine all documents, of any sort, kept by or on behalf of the trustees. This right will be subject to modification only if the trust deed provides otherwise.

(Paragraph 10.24)

33. (a) Should the trust legislation make provision for either protectors or advisory trustees?

(b) If so, in general terms what provision should be made? In particular:

(i) Should legislation list the powers that may be conferred on protectors? If so, is the list found in the legislation of the British Virgin Islands appropriate? Should a power to verify accounts be included? Are any other powers desirable?

(ii) Should protectors' duties be made expressly fiduciary in nature? Should they be subject to an express duty to exercise the care, diligence and skill that a reasonably prudent person would exercise in comparable circumstances?

(iii) Is it desirable that specific provision should be made for the control of protectors by the court? For example, should a protector be entitled to apply to the court for directions? Should the truster, or any other person, have power to apply to the court to remove a protector, or to compel him or her to take action in furtherance of his or her responsibilities?

(Paragraph 11.7)

34. If Scots law makes provision for the appointment of protectors, should trustees be expressly protected from personal liability in the event that they act in accordance with the directions or instructions of the protector? In such a case, should the default rule be that the protector is liable to the beneficiaries for the consequences of his or her instructions, but with power in the truster to exclude this rule, so that the protector incurs no personal liability?

(Paragraph 11.9)

35. (a) Is it desirable to have legislation expressly permitting the setting up of private purpose trusts (purpose trusts other than the existing category of public trusts) in Scotland?

(b) If so, would legislation broadly along the lines of the Cayman Islands STAR legislation, or alternatively the Guernsey trust law, be appropriate? In particular, is it desirable that such legislation should permit trusts that allow for both purposes and identifiable beneficiaries, along the lines of the STAR legislation? Alternatively, is it sufficient merely to provide for private purpose trusts, leaving conventional trusts to deal with all cases where a trust is set up for identifiable beneficiaries?

(c) In particular, is it desirable that such legislation should include the institution of enforcer? If so, should enforcers be subject to fiduciary duties along the lines of the Cayman Islands STAR trust legislation?

(d) If private purpose trusts were introduced, should the legislation contain each of the following requirements:

(i) A requirement that the trust purposes should be set out in writing, and should contain a declaration that the special regime for private purpose trusts is to be applicable?

(ii) A statement of the limitations on such trusts, for example that the trust purposes should be specific, reasonable and possible, and should not be unlawful or contrary to public policy? In relation to illegality and public policy, is it sufficient to rely on the existing Scottish principles, including the principle that a trust to be valid must produce an identifiable benefit? Alternatively, should specific provision be made in the legislation incorporating that principle?

(iii) Specific provision for the *cy-près* jurisdiction, as discussed above at paragraphs 12.20-12.24?

(iv) Restrictions on who may be a trustee? In this connection, if restrictions are appropriate, what categories of persons should be authorised to be trustees? We have in mind in particular solicitors and chartered accountants and trust companies controlled by them and trust companies controlled by authorised banks, but we would welcome comments on other categories that might be appropriate.

(v) The exclusion of the rule in *Miller's Trustees v Miller*, as discussed above at paragraph 12.13?

(Paragraph 12.42)

36. (a) Does the trustee's duty of prudence in relation to investments give rise to practical difficulties in respect of controlling shareholdings in private companies? If so, what is the general nature of such difficulties?

(b) If such difficulties are significant, would it be desirable for Scots law to adopt a form of trust based, with appropriate modifications, on the VISTA legislation? If so, should the provision for such trusts be in addition to legislation for purpose trusts, as discussed in Chapter 12?

(c) If such provision would be desirable, what modifications if any would be appropriate?

(d) Would the use of a VISTA-style trust in Scotland raise any issues as to the compatibility of such legislation with United Kingdom company law?

(Paragraph 13.16)

37. (a) Alternatively, if the rules on prudent investment are a practical problem, would it be possible to deal with the difficulty through the medium of a purpose trust by providing that a trust might be declared for the purpose of holding or investing in shares in a designated company?

(b) If this approach is preferred, should any further specific modifications be made to basic legislation permitting private purpose trusts in order to deal with the holding of a controlling interest in a private company?

(Paragraph 13.16)

38. Is there support for, or opposition to, the statutory enactment of a rule which would enable the exercise of trustees' discretionary powers to be reduced or otherwise altered if the trustees were in error as to the considerations that ought to have been taken into account by them in the exercise of their power?

(Paragraph 14.4)

APPENDIX A

Text of letter from SLC Chairman to the Advocate General

28 September 2010

The Rt Hon the Lord Wallace of Tankerness QC
Advocate General for Scotland
Dover House
Whitehall
LONDON
SW1A 2AU

Scottish Law Commission
promoting law reform

Your ref:
Our ref: L/1/5/19A

STATUTORY TRUSTS / AGENCY: SCOTLAND
FINANCIAL SERVICES AND MARKETS ACT 2000

In the course of two different projects earlier this year the Scottish Law Commission came across an issue about which I feel you would wish to be aware. It arose as part of an investigation into what might be regarded as a rather technical area of trust law but, on further examination, it turns out to have potentially striking practical consequences.

In the trust law project, for which I am the lead Commissioner, we have been examining the role of nominees in relation to trust assets. As part of this we considered the position under the Financial Services and Markets Act 2000 (the 2000 Act). I appreciate that this legislation may very well soon be amended or repealed as part of the review of the Financial Services Authority but I hope that the issue will nonetheless have some relevance, perhaps for the replacement legislation.

Section 139(1)(a) of the 2000 Act provides the FSA with a rule-making power:

> "(1) Rules relating to the handling of money held by an authorised person in specified circumstances ("clients' money") may—
>
> > (a) make provision which results in that clients' money being held on trust in accordance with the rules; …"

The effect of this is that rules may (and, as I mention below, in fact do) provide that, in specified circumstances, clients' money is to be made subject to a statutory trust. The main benefit of this is to offer better protection for the client in the event of the nominee's insolvency. However, this applies only as a matter of English and Northern Irish law; the position in Scotland is rather different. Section 139(3) reads (with emphasis added):

> "(3) In the application of subsection (1) to Scotland, the reference to money being held on trust is to be read as a reference to its being held *as agent* for the person who is entitled to call for it to be paid over to him or to be paid on his direction or to have it otherwise credited to him."

Rules have been made under section 139(1): an example is in Chapter 7.7 (Statutory trust) of the Client Assets Sourcebook (CASS), which is part of the FSA's handbook. The opening paragraph (7.7.1G) reads:

> "Section 139(1) of the [2000] Act (Miscellaneous ancillary matters) provides that rules may make provision which result in client money being held by a firm on trust (England and Wales and Northern Ireland) or as agent (Scotland only). This section creates a fiduciary relationship between the firm and its client under which client money is in the legal ownership of the firm but remains in the beneficial ownership of the client. In the event of failure of the firm, costs relating to the distribution of client money may have to be borne by the trust."

Almost identical provision is made in Chapter 5.3 of CASS in respect of insurance monies. This is the other context in which the issue has arisen for us, as we are currently engaged on a joint project on insurance law.

The CASS provisions clearly indicate that the aim is to create a fiduciary relationship, by means of a trust, between the firm and its client. Specific reference is made to insolvency ("failure of the firm"). In such an event, the clients' money will be better protected by virtue of having been held on trust rather than simply in accordance with an ordinary creditor-debtor relationship. Yet this only applies in England, Wales and Northern Ireland, but as a matter of Scots law the trust is rejected in favour of agency. We are not sure why this choice was made. It is not clear why the trust is not a suitable vehicle in Scots law. It is, of course, true that Scots property law does not recognise the division of ownership into 'legal' and 'beneficial', as is the case in English law. But, as you know, under Scots law a trustee holds and owns trust assets in a separate patrimony from that in which his or her (or its) personal assets are held. As a result, we do not see why a trust would not achieve the same benefits under Scots law as are achieved under English law. Allied to this, it is far from obvious that agency as it applies in Scots law is a direct functional equivalent to the trust. In particular, certain benefits which flow from the trustee-beneficiary relationship would not necessarily result from agency. There is, therefore, some doubt in our minds as to whether the desired policy, namely the enhanced protection of client money in the event of the nominee's insolvency, is achieved in Scots law in an effective way.

I should mention that, in order to try to understand the reasons behind the drafting of section 139 of the 2000 Act, the trust law team here made enquiries of lawyers in HM Treasury. We received a prompt and helpful reply to the effect that the instructions for the 2000 Act do not disclose a policy reason for the choice of agency. However, they refer to the predecessor legislation (section 55(5) of the Financial Services Act 1986), which had an identical provision, and they instruct that the same policy be carried through into the 2000 Act. It appears, therefore, that no independent policy consideration was given to this matter when the 2000 Act was being prepared; rather, the 1986 provision was simply adopted. We are also aware that very similar provision is made in section 13 of the Estate Agents Act 1979. It therefore appears to be a statutory measure of some vintage.

The effect of the 2000 Act and of the CASS rules are, of course, beyond our remit in either the trust law or insurance law project. But in the course of our work on those projects we have had discussions with experts in the investment and insurance industries, from which we understand that the CASS rules are of the highest practical importance in protecting customers. In addition, we are aware that the litigation arising out of the collapse of Lehman Brothers has cast a spotlight on, amongst other things, the operation of CASS Chapter 7 as it applies in English law. The stark question which strikes us is whether the rules would achieve the intended level of client protection in the event of an insolvency north of the border.

LORD DRUMMOND YOUNG

APPENDIX B

We set out some comparative legislation in this Appendix –

(I) Trusts (Jersey) Law 1984, articles 11-14 (pages 106-107);

(II) Trusts (Guernsey Law) 2007, sections 12, 15, 59 and 60 (pages 108-110);

(III) Cayman Islands Trusts Law (2009 Revision), sections 95-109 (pages 110-114);

(IV) Virgin Islands Special Trust Act 2003 (in its entirety) (pages 115-123);

(V) Trustee Act 1956 (New Zealand), section 49, as amended (pages 124-125).

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(I) TRUSTS (JERSEY) LAW 1984 (AS AMENDED), ARTICLES 11-14

11 Validity of a Jersey trust
(1) Subject to paragraphs (2) and (3), a trust shall be valid and enforceable in accordance with its terms.

(2) Subject to Article 12, a trust shall be invalid –
(a) to the extent that –
(i) it purports to do anything the doing of which is contrary to the law of Jersey,
(ii) it purports to confer any right or power or impose any obligation the exercise or carrying out of which is contrary to the law of Jersey,
(iii) it purports to apply directly to immovable property situated in Jersey, or
(iv) it is created for a purpose in relation to which there is no beneficiary, not being a charitable purpose;
(b) to the extent that the court declares that –
(i) the trust was established by duress, fraud, mistake, undue influence or misrepresentation or in breach of fiduciary duty,
(ii) the trust is immoral or contrary to public policy, or
(iii) the terms of the trust are so uncertain that its performance is rendered impossible.

(3) Where a trust is created for 2 or more purposes of which some are lawful and others are unlawful –
(a) if those purposes cannot be separated the trust shall be invalid;
(b) where those purposes can be separated the court may declare that the trust is valid as to the purposes which are lawful.

(4) Where a trust is partially invalid the court may declare what property is trust property, and what property is not trust property.

(5) Where paragraph (2)(a)(iii) applies, any person in whom the title to such immovable property is vested shall not be, and shall not be deemed to be, a trustee of such immovable property.

(6) Property as to which a trust is wholly or partially invalid shall, subject to paragraph (5) and subject to any order of the court, be held by the trustee in trust for the settlor absolutely or if the settlor is dead for his or her personal representative.

(7) In paragraph (6) "settlor" means the particular person who provided the property as to which the trust is wholly or partially invalid.

(8) An application to the court under this Article may be made by any person referred to in Article 51(3).

12 Trusts for non-charitable purposes

A trust shall not be invalid to any extent by reason of Article 11(2)(a)(iv) if the terms of the trust provide for the appointment of an enforcer in relation to its non-charitable purposes, and for the appointment of a new enforcer at any time when there is none.

13 Enforcers

(1) It shall be the duty of an enforcer to enforce the trust in relation to its non-charitable purposes.

(2) The appointment of a person as enforcer of a trust in relation to its non-charitable purposes shall not have effect if the person is also a trustee of the trust.

(3) Article 21(4) shall apply to an enforcer as if the reference in sub-paragraph (b) of that paragraph to "a trustee" were a reference to "an enforcer" and the references in that sub-paragraph to the "trustee's trusteeship" and "such trusteeship" were both references to the "enforcer's appointment".

14 Resignation or removal of enforcer

(1) Subject to paragraph (3), an enforcer may resign his or her office by notice in writing delivered to the trustee.

(2) A resignation takes effect on the delivery of notice in accordance with paragraph (1).

(3) A resignation given in order to facilitate a breach of trust shall be of no effect.

(4) An enforcer shall cease to be enforcer of the trust in relation to its non-charitable purposes immediately upon –

(a) the enforcer's removal from office by the court;

(b) the enforcer's resignation becoming effective;

(c) the coming into effect of a provision in the terms of a trust under which the enforcer is removed from office or otherwise ceases to hold office; or

(d) the enforcer's appointment as a trustee of the trust.

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(II) TRUSTS (GUERNSEY) LAW 2007, SECTIONS 12, 15, 59-60

12 Trusts for non-charitable purposes; and enforcers

(1) A trust for or including non-charitable purposes created by an instrument in writing and the terms of which provide for -

(a) the appointment of an enforcer in relation to the trust's non-charitable purposes, and

(b) the appointment of a new enforcer at any time when there is none,

is valid and enforceable in relation to its non-charitable purposes.

(2) It is the fiduciary duty of an enforcer to enforce the trust in relation to its non-charitable purposes.

(3) The appointment of a person as enforcer of a trust has no effect if the person is also a trustee of the trust.

(4) An enforcer may resign his office by delivering a written notice of resignation to the trustees.

(5) Subject to subsection (6), a resignation takes effect -

(a) on delivery of the notice, or

(b) on such later date or on the happening of such later event as may be specified therein.

(6) A resignation given to facilitate a breach of trust or a breach of the enforcer's fiduciary duty has no effect.

(7) An enforcer ceases to be the enforcer of a trust immediately on -

(a) his removal from office by the Royal Court,

(b) his resignation becoming effective,

(c) the coming into effect of a provision in the terms of the trust under or by which he is removed from office or otherwise ceases to hold office, or

(d) his appointment as a trustee of the trust.

(8) A trustee of a trust which includes non-charitable purposes which is valid and enforceable by virtue of subsection (1) shall, at any time when there is no enforcer in relation to those purposes, take such steps as may be necessary to secure the appointment of an enforcer.

(9) Where the trustee of a trust which includes non-charitable purposes which is valid and enforceable by virtue of subsection (1) has reason to believe that the enforcer in relation to those purposes -

(a) is unwilling or is refusing to act,

(b) is bankrupt or otherwise unfit to act, or

(c) is incapable of acting,

the trustee shall apply to the Royal Court for the removal of the enforcer and the appointment of a replacement.

(10) For the avoidance of doubt, the settlor or a corporation can be appointed as an enforcer.

(11) The terms of a trust for non-charitable purposes may provide for the addition, variation or removal of a non-charitable purpose of the trust or for the exclusion of a non-charitable purpose from the objects of the trust.

15 Reservation or grant of certain powers that does not invalidate trust

(1) A trust is not invalidated by the reservation or grant by the settlor (whether to the settlor or to a trust official or third party) of all or any of the following powers or interests -

(a) a power to revoke, vary or amend the terms of the trust or any trusts or functions arising thereunder, in whole or in part,

(b) a power to advance, appoint, pay or apply the income or capital of the trust property or to give directions for the making of any such advancement, appointment, payment or application,

(c) a power to act as, or give directions as to the appointment or removal of, a director or other officer of any corporation wholly or partly owned as trust property,

(d) a power to give directions to the trustee in connection with the purchase, retention, sale, management, lending or charging of the trust property or the exercise of any function arising in respect of such property,

(e) a power to appoint or remove any trustee, enforcer, trust official or beneficiary,

(f) a power to appoint or remove any investment manager or investment adviser or any other professional person acting in relation to the affairs of the trust or holding any trust property,

(g) a power to change the proper law of the trust or the forum for the administration of the trust,

(h) a power to restrict the exercise of any function of a trustee by requiring that it may only be exercised with the consent of the settlor or a third party or trust official identified in the terms of the trust,

(i) a beneficial interest in the trust property.

(2) The reservation, grant or exercise of a power or interest referred to in subsection (1) does not -

(a) constitute the holder of the power or interest a trustee,

(b) subject to the terms of the trust, impose any fiduciary duty on the holder, or

(c) of itself render any trustee liable in respect of any loss to the trust property.

(3) A trustee who acts in compliance with the valid exercise of any power referred to in subsection (1) does not, by reason only of such compliance, act in breach of trust.

59 Charitable and non-charitable trusts – "*cy-près*"

Where trust property is held for a charitable or non-charitable purpose and -

(a) the purpose has been, as far as may be, fulfilled,

(b) the purpose cannot be carried out, or not according to the directions given and to the spirit of the gift,

(c) the purpose provides a use for part only of the property,

(d) the property, and other property applicable for a similar purpose, can be more effectively used in conjunction, and to that end can suitably, regard being had to the spirit of the gift, be applied to a common purpose,

(e) the purpose was laid down by reference to an area which was then, but has since ceased to be, a unit for some other purpose, or by reference to a class of persons or to an area which has for any reason since ceased to be suitable, regard being had to the spirit of the gift, or to be practicable in administering the gift,

(f) the purpose has been adequately provided for by other means,

(g) in the case of a charitable purpose, the purpose has ceased to be charitable (by being useless or harmful to the community or otherwise), or

(h) the purpose has ceased in any other way to provide a suitable and effective method of using the property, regard being had to the spirit of the gift,

the property, or the remainder of the property, as the case may be, shall be held for such other charitable or non-charitable purpose as the Royal Court, on the application of -

(i) Her Majesty's Procureur,

(ii) the trustees, or

(iii) in the case of a non-charitable purpose, the enforcer,

may declare to be consistent with the original intention of the settlor.

60 General power to vary

(1) Where trust property is held for a charitable or non-charitable purpose, the Royal Court, on the application of Her Majesty's Procureur or the trustees, may approve any arrangement which varies or revokes the purposes or the terms of the trust or enlarges or modifies the powers of management or administration of the trustees, if it is satisfied that the arrangement -

(a) is now suitable or expedient, and

(b) is consistent with the original intention of the settlor and the spirit of the gift.

(2) The Royal Court may dispense with the consideration set out in subsection (1)(b) if satisfied that the original intention of the settlor cannot be ascertained.

(3) The Royal Court shall not approve an arrangement under subsection (1) unless satisfied that any person with a material interest in the trust has had an opportunity of being heard.

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(III) CAYMAN ISLANDS TRUSTS LAW (2009 REVISION), SECTIONS 95-109

PART VIII Special Trusts – Alternative Regime (for "STAR" trusts)

95 Definitions in this Part

(1) In this Part-

"beneficiary" means a person who will or may derive a benefit or advantage, directly or indirectly, from the execution of a special trust;

"enforcer" means a person who has standing to enforce a special trust;

"ordinary", in reference to a trust or power, signifies that it is a trust or power which is not subject to this Part;

"power" includes an administrative power as well as a dispositive power;

"special", in reference to a trust or power, signifies that it is a trust or power which is subject to this Part;

"standing to enforce" means the right or duty to bring an action for the enforcement of a special trust; and

"trust" includes a trust of a power, as well as a trust of property, and "trustee" has a correspondingly extended meaning.

(2) In this Part, a power is said to be held in trust if granted or reserved subject to any duty, expressed or implied, qualified or unqualified, to exercise the power or to consider its exercise.

(3) Except as provided in subsections (1) and (2), terms and expressions defined in section 2 have the same meanings in this Part.

96 Application

(1) A trust or power is subject to this Part, and is described as special, if-

(a) it is created by or on the terms of a written instrument, testamentary or inter vivos; and

(b) the instrument contains a declaration to the effect that this Part is to apply.

(2) If a trust or power is created by written instrument in exercise of a special power, and the instrument contains no declaration as to the application of this Part, this Part shall, subject to evidence of a contrary intention, be deemed to be intended to apply; and for the purpose of subsection (1) the instrument shall be deemed to contain a declaration to that effect.

(3) A trust or power which does not meet the requirements of subsection (1), and is not deemed to do so by virtue of subsection (2), is an ordinary trust or power and is not subject to this Part.

97 Ordinary trusts and powers

Nothing in this Part affects an ordinary trust or power directly or by inference.

98 Existing law

The law relating to special trusts and powers is the same in every respect as the law relating to ordinary trusts and powers, save as provided in this Part.

99 Objects

(1) The objects of a special trust or power may be persons or purposes or both.

(2) The persons may be of any number.

(3) The purposes may be of any number or kind, charitable or non-charitable, provided that they are lawful and not contrary to public policy.

100 Enforcers

(1) A beneficiary of a special trust does not, as such, have standing to enforce the trust, or an enforceable right against a trustee or an enforcer, or an enforceable right to the trust property.

(2) The only persons who have standing to enforce a special trust are such persons, whether or not beneficiaries, as are appointed to be enforcers-

(a) by or pursuant to the terms of the trust; or

(b) by order of the court.

(3) A right or duty to enforce a trust is presumed, subject to evidence of a contrary intention, to extend to every trust which is created by or on the terms of the same instrument, or pursuant to a power so created.

(4) The court may, on the application of a trustee or an enforcer, appoint an enforcer-

(a) if the terms of the trust require the appointment of an enforcer but-

(i) it is impossible to make the appointment without the court's assistance; or

(ii) it is difficult or inexpedient to make the appointment without the court's assistance;

(b) if an enforcer with a duty to enforce is unable, unwilling or unfit to do so; or

(c) if there is no enforcer who is of full capacity and who-

(i) is a beneficiary; or

(ii) has a duty to enforce and is fit and willing to do so.

(5) In the circumstances described in paragraph (c) of subsection (4), the trustee shall, within thirty days apply, to the court for the appointment of an enforcer, or for the administration of the special trust under the direction of the court, or for such other order as the court shall think fit and, if a trustee knowingly fails to do so, he is guilty of an offence and liable on summary conviction to a fine of ten thousand dollars.

(6) Subsections (1) to (5) do not affect-

(a) the enforcement, by a trustee, an enforcer or any other person involved in the administration of a trust, of a right to remuneration or indemnity; or

(b) the enforcement of a trustee's duties by a co-trustee or a successor trustee.

(7) Section 83 does not apply to special trusts.

101 Duties of enforcers

(1) Standing to enforce a special trust may be granted or reserved as a right or as a duty.

(2) Subject to evidence of a contrary intention, an enforcer is deemed to have a fiduciary duty to act responsibly with a view to the proper execution of the trust.

(3) A trustee or another enforcer, or any person expressly authorised by the terms of the special trust has standing to bring an action for the enforcement of the duty, if any, of an enforcer.

102 Rights and remedies of enforcers

Subject to the terms of his appointment-

(a) an enforcer has the same rights as a beneficiary of an ordinary trust-

(i) to bring administrative and other actions, and make applications to the court, concerning the trust; and

(ii) to be informed of the terms of the trust, to receive information concerning the trust and its administration from the trustee, and to inspect and take copies of trust documents;

(b) in the performance of his duties, if any, an enforcer has the rights of a trustee of an ordinary trust to protection and indemnity and to make applications to the court for an opinion, advice or direction or for relief from personal liability; and

(c) in the event of a breach of trust an enforcer has, on behalf of the trust, the same personal and proprietary remedies against the trustee and against third parties as a beneficiary of an ordinary trust.

103 Uncertainty

(1) Subject to subsection (4), a special trust is not rendered void by uncertainty as to its objects or mode of execution.

(2) The terms of a special trust may give the trustee or any other person power to resolve an uncertainty as to its objects or mode of execution.

(3) If a special trust has multiple objects and there is no allocation of the trust property between them, the trustee, subject to evidence of contrary intention, has discretion to allocate the trust property.

(4) If an uncertainty as to the objects or mode of execution of a special trust cannot be resolved, or has not been resolved pursuant to the terms of the trust, the court-

(a) may resolve the uncertainty-

(i) by reforming the trust;

(ii) by settling a plan for its administration; or

(iii) in any other way which the court deems appropriate; or

(b) insofar as the objects of the trust are uncertain and the general intent of the trust cannot be found from the admissible evidence as a matter of probability, may declare the trust void.

(5) This section applies to powers as to trusts.

104 *Cy-près*

(1) If the execution of a special trust in accordance with its terms is or becomes in whole or in part –

(a) impossible or impracticable;

(b) unlawful or contrary to public policy; or

(c) obsolete in that, by reason of changed circumstances, it fails to achieve the general intent of the special trust,

the trustee shall, unless the trust is reformed pursuant to its own terms, apply to the court to reform the trust *cy-près* or, if or insofar as the court is of the opinion that it cannot be reformed consistently with the general intent of the trust, the trustees shall dispose of the trust property as though the trust or the relevant part of it has failed.

(2) Section 72 does not apply to special trusts.

105 Trust corporation

(1) Except as authorised by an order of the court, or permitted by or pursuant to this section-

Trust corporation

(a) the trustee of a special trust shall be, or include, a trust corporation; and

(b) the trustee shall keep in the Islands at the office of the trust corporation a documentary record of-

(i) the terms of the special trust;

(ii) the identity of the trustee and the enforcers;

(iii) all settlements of the property upon the special trust and the identity of the settlors;

(iv) the property subject to the special trust at the end of each of its accounting years; and

(v) all distributions or applications of the trust property.

(2) In this section-

"trust corporation" means a body corporate licensed to conduct trust business, with or without restriction, under the Banks and Trust Companies Law (2009 Revision) or registered as a private trust company under that Law.

(3) The court may authorise non-compliance with subsection (1) on such terms as it thinks fit if it is satisfied that the execution of the trust will not be prejudiced.

(4) Whoever, in the Islands or elsewhere, knowingly administers a special trust while there is a breach of paragraph (a) of subsection (1), apart from –

(a) actions intended to bring the trust into compliance with paragraph (a) of subsection (1) as soon as possible; and

(b) actions intended to preserve the trust property pending compliance with paragraph (a) of subsection (1)

is guilty of an offence and liable on summary conviction to a fine of ten thousand dollars and to imprisonment for one year, and on conviction on indictment, to a fine of one hundred thousand dollars and to imprisonment for five years.

(5) A trustee who knowingly fails to comply with paragraph (b) of subsection (1) is guilty of an offence and liable on summary conviction to a fine of ten thousand dollars.

(6) This section does not apply to the holder of a power which is granted or reserved by the terms of a special trust to a person other than the trustee of the special trust, even though the power is held in trust.

(7) This section does not apply (except as regards any antecedent offence) if the governing law of the trust has been changed from the law of the Islands.

(8) The Governor in Cabinet may make regulations subject to affirmative resolution restricting the application of subsection (1).

106 Theft

(1) Section 239(1) of the Penal Code (2007 Revision) does not apply in relation to special trusts.

(2) For the purpose of the Penal Code (2007 Revision) property held upon a special trust shall be regarded, as against the trustee of the property or of any power in relation to the trust, and against any enforcer of the trust, as belonging to others (except to the extent of the beneficial interest, if any, of the trustee or enforcer under the terms of the trust), and an intention on the part of any such trustee or enforcer to defeat the trust shall be regarded accordingly as an intention to deprive others of their property.

107 Unlawful acceptance

Whoever, as trustee, accepts a settlement of property upon a special trust without taking steps to ensure that the settlor, or the person making the settlement on his behalf, understands who will have standing to enforce the trust is guilty of an offence and liable on summary conviction to a fine of ten thousand dollars and to imprisonment for one year, and on conviction on indictment to a fine of one hundred thousand dollars and to imprisonment for five years.

108 Foreign element

Part VI of this Law applies to special trusts but as though paragraph (b) of section 89(4)[16] were repealed and the following substituted-

"(b) in the case of a change from the law of the Islands, the new governing law would recognise the validity of the trust (without any material effect on its objects) and the standing of the enforcers to enforce the trust.".

109 Land in the Islands

No land nor any interest in land in the Islands shall be subject, directly or indirectly, to a special trust, but a special trust may hold an interest in a company, partnership or other entity which holds land in the Islands, or an interest in such land for the purposes of its business.

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[16] Section 89(4) provides:

"(4) If the terms of a trust so provide, the governing law of the trust may be changed to or from the laws of the Islands provided that-

(a) in the case of a change to the laws of the Islands, such change is recognised by the governing law of the trust previously in effect; or

(b) in the case of a change from the laws of the Islands, the new governing law would recognise the validity of the trust and the respective interests of the beneficiaries."

(IV) VIRGIN ISLANDS SPECIAL TRUSTS ACT 2003 (FOR "VISTA" TRUSTS)

An Act to make special provision for trusts of shares in companies and for related matters, including provision for the retention by trustees of shares in a company irrespective of the financial advantages of disposal, for prohibiting trustees from intervening in the management of the company except in certain circumstances, and for the appointment and removal of directors of the company in accordance with the terms of the trust instrument.

ENACTED by the Legislature of the Virgin Islands as follows:

1 Short title and commencement

This Act may be cited as the Virgin Islands Special Trusts Act, 2003 and shall come into force on such date as the Governor may, by Proclamation published in the Gazette, appoint.

2 Interpretation

(1) In this Act, unless the context otherwise requires "business" in relation to a company includes the holding of shares or other assets and non-commercial activities; "business risk" in relation to a company includes:

(a) any risk attached to any business of the company, or any connected company, when conducted in the manner in which it has in fact been conducted; or

(b) any risk which can be expected to be attached to any projected business of the company;

"court" means the High Court;

"designated shares" means Virgin Islands shares comprised in a trust fund and in respect of which a valid direction under section 4(1) has been made;

"designated trustee" means a holder of a trust license under the Banks and Trust Companies Act, 1990;

"interested person" in relation to a trust means

(a) a beneficiary of the trust;

(b) an object of a discretionary power over any of the capital or income of the trust;

(c) a parent or legal guardian of any minor person falling within paragraphs (a) or (b);

(d) where any of the purposes of the trust are exclusively charitable, the Attorney General;

(e) an enforcer referred to in section 84A of the Trustee Ordinance;

(f) a protector; or

(g) an appointed enquirer.

"intervention call" means a call by an interested person under section 9(1) for a trustee to intervene in the affairs of a company;

"legal guardian" in relation to a minor person means a person legally recognised as his guardian in any jurisdiction with which the minor has a substantial connection;

"office of director rules" means rules referred to in section 7(1) and any amendments thereto for the time being in force;

"trust fund" in relation to a trust means property for the time being subject to the trust;

"Virgin Islands shares" means shares in a company incorporated under the Companies Act or the International Business Companies Ordinance which is not

(a) company which has a license under the Banks and Trust Companies Act, 1990; No. 5 of 1994

(b) company which is licensed as an insurer under the Insurance Act, 1994 or which is authorised to act as an insurance manager under that Act;

(c) company which is registered as a public fund, or recognised as a private fund, under the Mutual Funds Act, 1996

(d) company which is licensed as a manager or administrator of mutual funds under the Mutual Funds Act, 1996;

(e) company which has a license under the Company Management Act, 1990.

(2) In this Act,

(a) references to voting powers in respect of shares shall be taken to include references to powers to direct the voting of shares held by a nominee;

(b) references in relation to a trust to a protector are to any person or committee whose consent is requisite for the exercise of any powers;

(c) references in relation to a trust to an appointed enquirer are to any person who by, or under any power conferred by, the terms of the trust is appointed to make intervention calls

(d) references to the memorandum and articles of a company are to its memorandum of association and its articles of association;

(e) a company shall be taken to be connected with another company if

(i) that other company holds, directly or through a nominee, shares in it;

(ii) it is controlled directly or indirectly by that other company; or

(iii) it is connected with a company which is itself connected with that other company;

(f) a ground for complaint concerning the conduct of a company's affairs is permitted if it is specified as such in the trust instrument, and the expression "permitted ground for complaint" shall be construed accordingly.

(3) In this Act, the following definitions shall, where the context admits, apply in relation to, or in the context of a provision referring to, designated shares:

"company" means the company that has issued the designated shares;

"disposal" means

(a) the exercise of voting powers leading, or capable of leading, to the liquidation of the company or the cancellation of the shares or of any rights attached to them;

(b) the creation of any legal or equitable interest in the shares;

and "dispose" shall be construed accordingly;

"settlor" means the person by whom the trust was created;

"trust" means the trust on which the designated shares are held;

"trustee" means the trustee for the time being of the trust;

"trust instrument" means the instrument containing the terms of the trust.

3 Primary purposes of this Act

The primary purpose of this Act is to enable a trust of company shares to be established under which

(a) the shares may be retained indefinitely; and

(b) the management of the company may be carried out by its directors without any power of intervention being exercised by the trustee.

4 Designated shares

(1) Where a trust fulfils the conditions specified in subsection (4), the terms of the trust may, subject to subsection (3), direct that the provisions of this Act shall apply

(a) to all Virgin Islands shares comprised in the trust fund; or

(b) to such Virgin Islands shares comprised in the trust fund as may be specified in the direction.

(2) For the purposes of subsection (1), Virgin Islands shares comprised in the trust fund shall be taken to include Virgin Islands shares becoming so comprised at any time after the creation of the trust, whether added to the trust fund by way of additional settlement by the original settlor or any other person, acquired on a new issue by the company or in the course of management or administration of the trust fund, or acquired in any other manner.

(3) A direction under subsection (1) shall not be made in respect of shares added to the trust fund by a trustee of another trust in the exercise of a power in that other trust.

(4) The conditions referred to in subsection (1) are

(a) the trust is created by or on the terms of a written testamentary or inter vivos instrument;

(b) a designated trustee is sole trustee of the trust;

(c) the terms of the trust require that any successor trustee (mediate or immediate) is a designated trustee acting as sole trustee;

(d) the trust is not created in the exercise of a power conferred by another trust.

(5) A direction under subsection (1) may identify the shares to which it relates either specifically or by any general description.

(6) Subject to subsection (7), where a person ("the first person") is a settlor in relation to a trust of designated shares and additional property is settled on the terms of the trust by another person, the first person shall be considered for the purposes of this Act as the settlor in relation to the trust of the additional property.

(7) If the trust instrument provides that subsection (6) shall not apply, then, in the case of a trust comprising property which has been provided by more than one person, this Act shall apply as if each person had created a separate trust in relation to the property which he has provided.

5 Trustee's duties in relation to designated shares

(1) Subject to section 9, designated shares shall be held by the trustee on trust to retain them.

(2) The trustee's duty to retain designated shares shall have precedence over any duty to preserve or enhance the value of the trust fund.

(3) Without prejudice to subsection (2), the trustee shall not be accountable for losses arising directly or indirectly from holding, rather than disposing of, designated shares, including, in particular, losses arising from any of the factors specified in subsection (4).

(4) The factors referred to in subsection (3) are

(a) the absence, or inadequacy, of financial return from any designated shares;

(b) a decrease in value of any designated shares;

(c) speculative or imprudent activities of the company or depletion of the company's assets by disposition;

(d) any act or omission of the directors of the company, regardless of whether it is made or carried out in good faith;

(e) liquidation or receivership of the company;

(f) share market fluctuation;

(g) the loss of opportunity to make gains from reinvestment of the proceeds of designated shares;

(h) the liabilities and expenses of the company, including directors' remuneration and expenses.

(5) Every reference in subsection (4) to the company shall include a reference to any company connected to it.

6 Restrictions on trustee's powers

(1) Subject to the terms of the trust and to sections 7 and 8, the obligations specified in subsections (2) and (3) shall apply to a trustee of designated shares.

(2) Voting or other powers in respect of designated shares shall not be exercised by the trustee so as to interfere in the management or conduct of any business of the company, and in particular, the trustee

(a) shall leave the conduct of every such business, and all decisions as to the payment or non-payment of dividends, to the directors of the company,

(b) shall not require the declaration or payment of any dividend by the company or exercise any power the trustee may have of compelling any such declaration or payment.

(3) A trustee of designated shares

(a) shall take no steps to instigate or support any action by the company against any of its directors for breach of duty to the company;

(b) shall take no steps to procure the appointment or removal of any of the directors;

(c) subject to section 9, shall take no steps to wind up the company; and

(d) subject to the provisions of this Act, shall not apply to the court for any form of relief or remedy in relation to the company.

7 Provisions relating to directors

(1) The trust instrument may contain rules for determining the manner in which voting and other powers attributable to designated shares should be exercised by the trustee in relation to

(a) the appointment of directors of the company,

(b) the removal of directors,

(c) the remuneration of directors, or

(d) any of the matters referred to in subsection (2), and may make provision for those rules to be amended.

(2) The office of director rules may, in particular

(a) require the trustee to ensure that a particular person holds or retains office as director;

(b) require any person to be appointed to the office of director at some future date or upon some future event;

(c) require the removal of a director in specified circumstances;

(d) prescribe, subject to the requirements of the memorandum and articles of the company and the law of the Territory, the minimum and maximum number of directors (whether one or more) to hold office at any time or times;

(e) require the trustee, in relation to the appointment and removal of directors, to act, generally or in any specified circumstances, on the decision of a third person or committee;

(f) provide for the conferral of fiduciary duties on a person or committee referred to in paragraph (e); or

(g) provide for the establishment, continuance, and procedures of a committee referred to in paragraph (3).

(3) Subject to subsection (9) and to section (8), the trustee shall at all times use its voting and other powers, so far as those powers allow, to ensure

(a) that the company has at least the minimum number of directors to meet the requirements of its memorandum and articles and the law of the Territory; and

(b) that, except in an exempted case, the identity of the directors of the company conforms with the office of director rules, if any, for the time being applicable.

(4) No person becoming or remaining a director of the company, whether in consequence of the office of director rules or otherwise, shall, in the capacity of director, owe fiduciary or other obligations under the trust, or have any fiduciary or other obligations to the trustee, but

nothing in this subsection shall affect any duty which that person owes, as director, to the company.

(5) Persons for whose appointment the office of director rules may provide include
(a) any settlor or protector of the trust;
(b) both ascertained and ascertainable persons.

(6) A trustee shall incur no liability for securing, sanctioning or not opposing the appointment of a director where that appointment is in conformity with the office of director rules.

(7) Where there are no office of director rules, and in an exempted case, a trustee shall incur no liability for securing, sanctioning, or not opposing, the appointment of a director of the trustee's own selection, if
(a) the trustee concludes in good faith that the appointment in questions is consistent with the wishes of the settlor; and
(b) the selection is not motivated by a desire on the part of the trustee to reduce business risk, except to the extent, if at all, that the trustee in good faith concludes that a reduction would be consistent with the wishes of the settlor.

(8) For the purposes of this section, an exempted case is any case in which either
(a) the office of director rules make no provision in that case; or
(b) the rules make provision but the trustee concludes in good faith that it would be impossible, unlawful, impracticable, or plainly inconsistent with the wishes of the settlor, to ensure compliance with the rules in that case.

(9) A trustee shall have no duty
(a) to act pursuant to subsection (3) unless and until it receives actual notice that circumstances requiring such action have arisen; or
(b) to enquire as to whether circumstances requiring action pursuant to subsection (3) exist.

(10) Where, on any question concerning the appointment of a director, a trustee makes application to the court under section 6 of the Trustees' Relief Act, the court, in giving its opinion, advice, or direction, shall not seek to reduce business risk, except to the extent, if at all, that the court concludes that a reduction would be consistent with the wishes of the settlor.

8 Intervention by trustee in management in prescribed circumstances
(1) Where, in relation to a trust of designated shares, an interested person has a complaint concerning the conduct of the company's affairs, and the ground for that complaint is permitted, he may, in writing, call upon the trustee to intervene in the affairs of the company to deal with the complaint.

(2) A trust instrument may specify one or more permitted grounds for complaint, but need not specify any.

(3) Upon receiving an intervention call, the trustee shall, if satisfied that the complaint is substantiated, take such, if any, action as the trustee considers appropriate to deal with the complaint in the interests of the trust.

(4) Action taken under subsection (3) may include
(a) making or procuring changes in the directorship of the company in accordance with the provisions of its memorandum and articles and the law of the Territory, but otherwise on such terms as the trustee thinks fit, provided that in making, procuring or maintaining any such change, the trustee may disregard section 7(3)(b) if and for

so long as, in the opinion of the trustee, it is expedient to do so for the purposes of dealing with the complaint;

(b) procuring action by the company to recover any losses caused by the conduct giving rise to the complaint; or

(c) seeking such advice on the complaint and the manner of addressing it as the trustee considers appropriate.

(5) In considering and taking action under subsection (3), the trustee shall

(a) have regard to

(i) any wishes of the settlor; and

(ii) the efficient functioning of the company;

(b) disregard business risk, except to the extent that

(i) the ground for complaint consists of or arises from any disagreement among the directors as to the business risk, or

(ii) any wishes of the settlor require business risk to be considered.

(6) After acting pursuant to subsection (3), or deciding not to act, the trustee's obligation to intervene shall be at an end unless and until another intervention call is made.

(7) It shall be a ground for declining to act on an intervention call if, apart from any other reason for declining, the call is made on substantially the same ground as one previously made, and there appears to the trustee to be no reason to alter, or act further on, the decision previously taken by it.

(8) Where a trust instrument specifies one or more permitted grounds for complaint, the following provisions of this subsection shall apply:

(a) an interested person may request the trustee to provide such information concerning the affairs of the company and any connected company as is reasonably required for that person to judge whether an intervention call is necessary, and the trustee shall use all reasonable endeavours to provide that information and may, if considered necessary for this purpose, procure the replacement of any of the directors with the trustee's own representative;

(b) where there is an appointed enquirer he shall be under the following duties:

(i) a duty to make reasonable enquiries as to whether there is a permitted ground for complaint as often as appears appropriate in the circumstances, and not less than once in any period of twelve months;

(ii) a duty to make an intervention call under this section, and provide the trustee with evidence of the relevant ground for complaint, whenever it appears to him to be appropriate;

(c) where there is no appointed enquirer, the trustee shall use all reasonable endeavours to ensure that at all times at least one interested person of full capacity is given the following documents and information concerning the trust, but without prejudice to any right of that person to documents and information apart from this paragraph:

(i) a copy of the trust instrument and other trust documents,

(ii) the name and address of the trustee,

(iii) the name, registered office, and principal place of business, of the company,

(iv) the names and addresses of all directors of the company,

(v) the nature of the current activities of the company, provided that , where practicable, any person to whom information is given under this paragraph shall be a person who, in the reasonable opinion of the trustee, has acquired, or is likely to acquire, by appointment or otherwise, a substantial equitable interest in some or all of the designated shares or their proceeds or is the parent or legal guardian of such a person.

(9) All expenses incurred in dealing with an intervention call or considering the complaint on which it is based, including trustee remuneration where applicable, and the cost of any advice, shall be borne by the trust fund and its income in such proportions as the trustee decides, and if there is any deficiency in liquid funds the trustee may take such steps as are available to the trustee under the memorandum and articles of the company and the law of the Territory to make up the shortfall out of dividends from the company and may, if considered necessary for this purpose, procure the replacement of any of the directors with the trustee's own representative.

(10) The trustee shall, where practicable, procure the removal from office of a director appointed for the purpose specified in subsection (8)(a) or (9) when the purpose for which the director was appointed is achieved, if removal is appropriate for the purpose of any action decided upon by the trustee pursuant to subsection (3) or, subject to such action, for the purpose of compliance with the office of director rules.

9 Power to dispose

(1) This section shall apply to a trust of designated shares.

(2) Subject to subsection (3) and to the terms of the trust instrument, the trustee shall have power, in the management and administration of the trust fund, to sell or otherwise dispose of designated shares, but the existence of this power

(a) shall not carry an implied duty to exercise it for the purpose of preserving or enhancing the value of the assets of the trust or to consider its exercise for that purpose; and

(b) shall not render the trustee liable, in consequence of not exercising it, for losses of this kind referred to in section 5(3).

(3) Subject to section 11, the trustee shall not, unless the trust instrument otherwise provides, sell or dispose of designated shares in the management or administration of the trust fund without

(a) the consent of the directors of the company or of a majority of them if more than one; and

(b) such, if any, consents as are made requisite by the trust instrument.

(4) A sale or other disposal in exercise of the power conferred by subsection (2) shall be made in such manner, and upon such terms and conditions, as the trustee, acting in its fiduciary capacity, thinks fit.

(5) Section 59 of the Trustee Ordinance shall not apply to the trust to the extent that it permits the court to confer upon the trustee any power of sale or other disposal.

10 Enforcement

(1) Where in the case of a trust of designated shares there is a breach of a duty or obligation imposed on this Act on its trustee, any of the persons specified in subsection (3) may, subject to the terms of the trust, apply to the court for relief.

(2) The court shall, if satisfied that the application under subsection (1) is well founded, grant relief by

(a) making such order as it considers appropriate to attain, as nearly as may be, the outcome that the court considers would have been, or would most likely have been, attained in respect of the trust, the company, its directors and generally if the breach had not occurred;

(b) making such, if any, supplementary or incidental order as the court deems, in the circumstances of the case, reasonably required having regard to the primary purpose

of this Act state in section 3, provided that no order shall be made under this subsection to prejudice any interest in property which was acquired from the trustee in good faith, for value and without actual or constructive notice of the trust, or from the company in good faith and for full consideration, or to prejudice any interest deriving from such an interest.

(3) The persons referred to in subsection (1) are

(a) any interested person;

(b) any director of the company;

(c) any person who, under applicable office of director rules, would be a director if the trustee had complied with its obligations under section 7.

(4) Without prejudice to subsection (1) to (3), but subject to subsection (5), where in the case of a trust there is a breach of a duty or obligation imposed by this Act on its trustee, the breach shall be, and be actionable in civil proceedings as, a breach of the trust.

(5) Where civil proceedings are instituted in relation to a breach of a duty or obligation, the court shall, in granting any remedy, take account of any relief granted or available in respect of the breach on an application under subsection (1).

(6) References in subsection (4) to a breach shall be taken to include references to a prospective breach.

(7) Subject to the terms of the trust and to sections 7 and 8, where designated shares are held on trust, no act or omission of a director of the company shall be a ground for any person to seek intervention by the court in the affairs of the trust.

11 Power of court to order disposal

(1) Where it is shown to the court that the retention of the shares is no longer compatible with the wishes of the settlor, the court shall have power, on the application of any interested person, to order or authorise a sale or other disposal of any designated shares, and a sale or other disposal so ordered or authorised shall not require any consent referred to in section 9(3).

(2) In making an order, or giving authority, under this section, the court may impose such, if any, terms and conditions in relation to the sale or other disposal as it thinks fit.

12 Modification of rule in *Saunders v. Vautier*

(1) Notwithstanding any rule of equity or practice of the court to the contrary, but subject to subsection (2), neither a beneficiary who is solely interested in any designated shares, nor all the beneficiaries who together are the persons interested in any designated shares, shall be entitled, although in existence and ascertained and of full capacity, to call for or direct a transfer of those shares or to terminate or modify the trust relating to them if and so far as that entitlement is, without offending any rule of perpetuity or remoteness, excluded by the trust instrument.

(2) No such exclusion of entitlement shall have effect, or continue to have effect, after the expiration of 20 years from the creation of the trust.

(3) Where a person who receives designated shares, or an interest in them, is a person who, by virtue of such an exclusion or entitlement, has no present right to receive the shares or that interest, he shall, without prejudice to the generality of subsection (1), hold those shares or that interest on trust to transfer the same to the trustee, and the court shall order him so to do on the application by the trustee or any person specified in section 10(3).

(4) During any such exclusion of entitlement, section 58 of the Trustee Ordinance shall not apply to the trust.

13 Disqualification of trustee as a director
A trustee of designated shares shall not be, or become, a director of the company.

14 Ascertaining wishes of settlor
(1)Where it is necessary under this Act for the court or a trustee to ascertain the wishes of the settlor, the following provisions of this section shall apply.

(2) Where the settlor is alive, the settlor shall, where possible and practicable, be consulted as to his wishes.

(3) Where the settlor is dead, or it is not possible or practicable to consult him, his wishes shall be taken to be

(a) such wishes as he has most recently communicated to the trustee, or

(b) where no wishes or relevant wishes have been communicated, such as the court, or the trustee in good faith, believes most likely to have been his wishes from the evidence available to it.

15 Limitation of trustee's duties
(1) A trustee of designated shares shall have no fiduciary responsibility or duty of care in respect of the assets of, or the conduct of the affairs of, the company, except when acting, or required to act, on an intervention call.

(2) Without prejudice to the generality of subsection (1), a trustee of designated shares

(a) shall not be required to make any enquiry as to whether any facts exists which would, or may, whether with or without any other information, form the basis of an intervention call;

(b) shall not be obliged to inform any interested person of any fact of which it becomes aware, or which it suspects, concerning the assets of the company or the conduct of its affairs;

(c) shall not incur liability as accessory to a director's breach of duty by reason of any omission on the part of the trustee to take action where the trustee is aware, or suspects, that there has been or will be such a breach, or by reason of any act or omission in compliance with the provisions of section 7.

16 Regulations
The Minister may make regulations for the purpose of carrying the provisions of this Act into effect.

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(V) TRUSTEE ACT 1956 (NEW ZEALAND), SECTION 49

49 Advisory trustees may be appointed to assist responsible trustee

(1) In the administration of any trust property any trustee may act, to the extent hereinafter provided, with an advisory trustee, which term includes, in its application to the estate of a mentally disordered person, an advisory manager or advisory administrator of the estate; and also includes, in its application to the estate or any part of the estate of any person in respect of whom a property order is made under the Protection of Personal and Property Rights Act 1988, an advisory manager of the estate, or any part thereof.

(2) An advisory trustee may be appointed in respect of all or any part of the trust property—

(a) By the testator, settlor, or other creator of the trust, in the instrument creating the trust; or

(b) By order of the Court made on the application of any beneficiary or trustee or of any person on whose application the Court would have power to appoint a new trustee; or

(c) By the responsible trustee or any person having power to appoint a new trustee; or

(d) In respect of the estate of a mentally disordered person, by order of the Court made on the application of the manager or person authorised to administer the estate or of any person on whose application the Court would have power under the Protection of Personal and Property Rights Act 1988 to appoint a manager of that estate; or

(e) In respect of the estate or any part of the estate of any person in respect of whom a property order is made under the Protection of Personal and Property Rights Act 1988, by order of the Court made on the application of the manager of the protected estate or of any person on whose application the Court would have power to make the protection order.

(3) Where a trustee acts with an advisory trustee the trust property shall be vested in the first-mentioned trustee (in this section referred to as the responsible trustee), who shall have the sole management and administration of the estate and its trusts as fully and effectually as if he were the sole trustee:

Provided that—

(a) The responsible trustee may consult the advisory trustee on any matter relating to the trusts or the estate:

(b) The advisory trustee may advise the responsible trustee on any matter relating to the trusts or the estate, but shall not be a trustee in respect of the trust:

(c) Where any advice or direction is tendered or given by the advisory trustee, the responsible trustee may follow the same and act thereon, and shall not be liable for anything done or omitted by him by reason of his following that advice or direction:

(d) In any case where the responsible trustee is of opinion that such advice or direction conflicts with the trusts or any rule of law, or exposes him to any liability, or is otherwise objectionable, he may apply to the Court for directions in the matter, and the decision and order therein shall be final and shall bind the responsible trustee and the advisory trustee, and the Court may make such order as to costs as appears proper:

Provided that nothing in this paragraph shall make it necessary for the responsible trustee to apply to the Court for any such directions:

(e) Where advisory trustees are not unanimous, and tender to the responsible trustee conflicting advice or directions, the responsible trustee may similarly apply to the Court for directions.

(4) No person dealing with the responsible trustee in relation to any trust property shall be concerned to inquire as to the concurrence or otherwise of the advisory trustee, or be affected by notice of the fact that the advisory trustee has not concurred.

(5) Subject to the provisions of the instrument (if any) creating the trust and to any order made by the Court, in any case where remuneration is payable to the trustee of any trust property, remuneration or commission may be paid to both the responsible trustee and the advisory trustee, and subject as aforesaid the amount thereof shall be determined—

(a) where the responsible trustee is the Māori Trustee, by or under regulations made under the Maori Trustee Act 1953:

(aa) where the responsible trustee is Public Trust, in accordance with Public Trust's scale of charges:

(b) In any other case, by the responsible trustee if he is entitled to fix his own remuneration, or by the Court.

(6) [Repealed].

APPENDIX C

Advisory groups

I General

Alan Barr	University of Edinburgh; Solicitor, Edinburgh
Andrew Dalgleish	Solicitor, Edinburgh
Frank Fletcher	Solicitor, Edinburgh
Derek Francis	Faculty of Advocates, TrustBar
Nicholas Holroyd	Faculty of Advocates
Simon Mackintosh	Solicitor, Edinburgh
Sandy McDonald	Solicitor, Dundee
James McNeill QC	Faculty of Advocates
Scott Rae	Solicitor, Edinburgh

II Advisory group on nominees

Ruthven Gemmell	Solicitor, Edinburgh
Mark Hallam	Investment Director
Murray Mackay	Investment Director
Simon Mackintosh	Solicitor, Edinburgh
Suzanne McConville	Solicitor, London
Scott Moncur	Solicitor, Dundee

III Advisory group on apportionment

Derek Francis	Faculty of Advocates, TrustBar
John McArthur	Solicitor, Edinburgh
Gordon Wyllie	Solicitor, Glasgow

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