

Creditor v beneficiary enforcement actions against interests under Jersey trusts

Briefing Summary: Can a creditor enforce a judgment debt against the interests of a beneficiary under a Jersey discretionary trust?

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Jersey's Royal Court has now addressed this question, although not necessarily answered it for good. It declined to order enforcement by way of arrest of such an interest, but in doing so the Court was itself exercising a discretion. It is therefore unclear whether the Court held that such interests are incapable of being arrested as a matter of law, raising the possibility of further development of the law in a future case.

Circumstances of the decision

The case in question was *Kea Investments Limited v Watson* [2021] JRC 009. Kea was a judgment creditor of Eric Watson. Watson was one of several beneficiaries under three Jersey trusts. The terms of these trusts were not spelt out in the judgment, but it was clear that the trustee had the usual discretion to appoint trust property to the beneficiaries of each trust, including Watson. Further, at the expiration of the trust period (for two of the trusts 100 years, subject to the trustee appointing an earlier date, and indefinite for the third trust), the trust fund was to be held for the beneficiaries in such proportions as the trustee would appoint or otherwise in equal shares.

Kea accordingly sought to obtain payment of its judgment by the Jersey enforcement procedure known as an *arrêt entre mains* – explained below – against Watson's interests in the trusts.

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It is trite law that the beneficiary of a discretionary trust has no property interest in the trust assets themselves. Unless and until the trustee has exercised its discretion to appoint such property to the beneficiary, the beneficiary has only a hope or expectation that the trustee will do so. However, the beneficiary does have rights to require the trustee to consider doing so from time to time. Kea accepted this, and did not seek direct enforcement against the trust assets. Instead, it sought to enforce by arresting or attaching the beneficiaries' rights against the trustee by way of an *arrêt entre mains*.

Jersey enforcement mechanism – the *arrêt entre mains*

The *arrêt entre mains* is a Jersey law remedy (Guernsey has similar) for attaching or arresting property belonging to a debtor which is in the hands of a third party. Although it is available for tangible property or chattels, it has been held to apply to intangible movable property or choses in action, such as debts and shares. In those circumstances, the creditor can circumvent the debtor, and enforce directly against a person against whom the debtor in turn has rights.

As described by the Court in Kea^[1]:

An *arrêt* is a customary law remedy for the satisfaction of a debt by appropriating the debtor's movable property. It may be made against the debtor and his or her property directly, or against a third party over property owed by the third party to the debtor (an *arrêt entre mains*, or "arrest in the hands" of such a third party).

The effect of the arrest is to charge the thing arrested and create a proprietary security interest in it in favour of the arresting creditor.

The flexibility of the *arrêt* continues after its confirmation in respect of the precise benefit it confers on the arresting creditor in execution of his or her charge.

An arrest may be effected against future property, where that future property can be identified with precision.

Applying these principles, the Court has previously arrested intangibles such as debts owed to the debtor, and shares owned by the debtor. However, until now the Court had not ruled on the availability of the *arrêt* against a beneficiary's interest under a discretionary trust.

Application to discretionary trusts

Kea argued that the Trusts (Jersey) Law 1984 provides that the interests (and, in particular, the rights) of a beneficiary in a trust – including a discretionary trust – are movable property. The Trusts Law also provides that subject to the terms of a trust, the interest of a beneficiary can be sold, charged, and otherwise dealt with in any manner. Therefore, it was argued, it is capable of arrest.

Kea accepted that by arresting Watson's interest it would not acquire a property interest in the trust assets and that it could be in no better position than Watson in respect of that interest – in other words, it could not compel the trustee to make an appointment in its/Watson's favour any more than Watson himself could have done. But it argued that it could arrest and therefore enjoy all Watson's rights as a beneficiary against the trustee, including to compel it to consider exercising its discretion from time to time, as well as to obtain copies of trust accounts to evaluate the trust property available to be appointed. In effect, Kea would become a beneficiary or quasi-beneficiary of the trusts.

However, the Court declined to order an arrest. First, it noted that the beneficiaries' interests under a trust are not free-standing but defined by the terms of the trust itself. It then considered the nature of such terms in the context of a discretionary trust. In particular, the Court concentrated on the doctrine of fraud on a power, which applies to regulate the trustee's exercise of its discretions under the trust.

A fraud on a power is committed where the trustee does something which is apparently within the four corners of the power as drafted, but for a purpose collateral to that for which the power was granted. So, in the case of the discretionary power to appoint to or for the benefit of beneficiaries, the power must be truly exercised for the benefit of those beneficiaries.

Unsurprisingly, it is well recognised that the payment of a debt owed by a beneficiary can be of benefit to him. However, the Court did not consider that to be the end of the matter. It observed that cases where it is appropriate for a trustee to discharge the debt of a beneficiary notwithstanding their objection must be very rare. Further, it considered that the fraud on the power doctrine requires the trustee to consider the benefit of the beneficiary him or herself – the trustee cannot act for the purpose of benefitting the beneficiary's creditor. Therefore, the Court held, the discretionary beneficiary's rights to be considered and compel such consideration are personal to him or her alone, and therefore incapable of transmission to a third party voluntarily or by way of an *arrêt*. It therefore declined to confirm an *arrêt* of those rights.

Conclusion

As it stands, the decision in Kea is a clear impediment to enforcement by creditors whose debtors are beneficiaries under Jersey law discretionary trusts. This is of course, disappointing to creditors who may feel aggrieved that their debtor has apparent access to means, but does not discharge the debt.

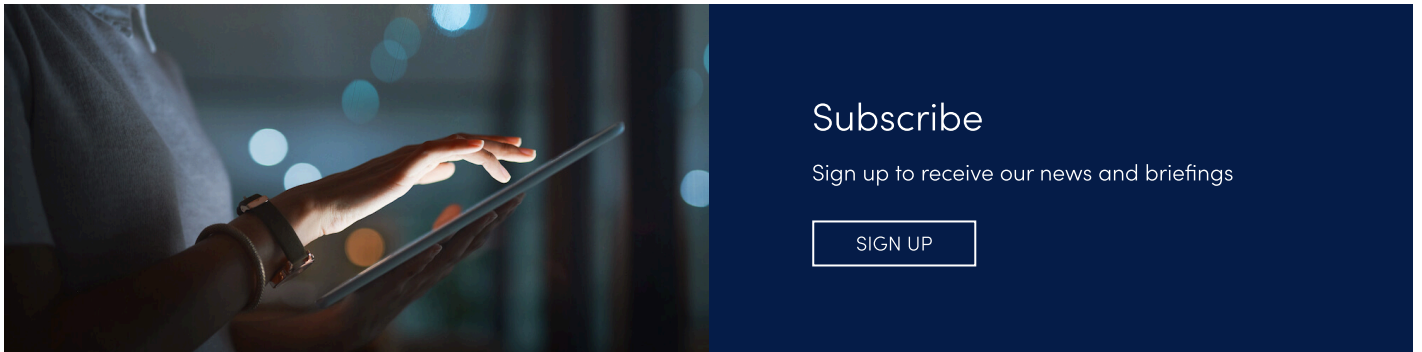
On the other hand, beneficiaries may feel that their interests in such trusts are protected, and trustees may feel relieved that they are spared the complication of having to consider whether a distribution is in the beneficiary's interest when it is liable to be taken by a creditor. Even then, the specific circumstances of each trust need to be considered carefully. For instance, in this case Watson had lent money to the trustee and to a company in the structure – Kea's application to arrest Watson's right to repayment of those loans was successful.

It may be, however, that the Court's judgment is not the last word. Although the Court found that the discretionary beneficiary's rights in this case were incapable of arrest, it stressed that such rights are always determined by the terms of the trust in question, rather than as a matter of general law. Further, the Court did not go further to consider whether or not future distributions or appointments from the trusts that the trustee might resolve to make to Watson could be arrested now as his future property.

^[1] Citing with approval Richard Holden (co-author of this note) *Offshore Civil Procedure* published by Sweet & Maxwell.

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