

Investec Trust (Guernsey) Limited v Glenalla Properties Limited – Guernsey Court of Appeal Decision

Service area / [Trusts and Private Wealth](#)

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In the second part of the appeal proceedings concerning the Tchenguiz Discretionary Trust (the “TDT”), the Guernsey Court of Appeal has handed down its judgment on the meaning and effect of Article 32 of the Trusts (Jersey) Law, 1984 (the “TJL”), which regulates the liability of a trustee of a Jersey trust when dealing with third parties.

In its earlier decision in June 2014 the Guernsey Court of Appeal held (overturning the Royal Court’s decision) that, in the circumstances of the case, Article 32 of the TJL applied so that the Guernsey-incorporated former trustees of the TDT were not personally liable in respect of loans advanced to them by certain BVI companies, notwithstanding that the governing law of the loans was not the law of Jersey. In this second part of the appeal, the Court of Appeal turned to consider the meaning and effect of Article 32 of the TJL when it is engaged.

Article 32 of the TJL

1. “Where a trustee is a party to any transaction or matter affecting the trust:
 - a. if the other party knows that the trustee is acting as trustee, any claim by the other party shall be against the trustee as trustee and shall extend only to the trust property;
 - b. if the other party does not know that the trustee is acting as trustee, any claim by the other party may be made against the trustee personally (though, without prejudice to his or her personal liability, the trustee shall have a right of recourse to the trust property by way of indemnity).
2. Paragraph (1) shall not affect any liability the trustee may have for breach of trust.”

The meaning and effect of Article 32(1)(a)

It was common ground between the parties that the relevant part of Article 32 of the TJL was Article 32(1)(a) because the BVI companies “knew” that they were dealing with a trustee when entering into the loans. The Court of Appeal concluded as follows:

Where a trustee is a party to a transaction or matter to which Article 32(1)(a) of the TJL applies (the “contracting trustee”):

- the contracting trustee is liable on the contract in that it is the trustee who is the party to the transaction or matter and who assumes the obligations under the contract in its own name (reflecting the fact that a trust is a relationship rather than a separate legal entity), but the contracting trustee is not required to satisfy a third party’s claim by recourse to the contracting trustee’s personal assets;
- a contracting trustee who is no longer in office has the right to recover from a successor trustee such trust property as is necessary to satisfy a claim against the contracting trustee;
- upon satisfying such liability to the extent of the trust property, the contracting trustee has no further liability to the third party; and
- the contracting trustee may satisfy the liability out of the trust property irrespective of whether or not there is any allegation of breach of trust, whether justified or otherwise, against the contracting trustee.

In the Court of Appeal’s view, the words of Article 32 are clear in their meaning and effect. In the case of sub-paragraph 1(a), where a third party knows that the person with whom he is transacting is acting as a trustee, the liability of the contracting trustee extends only as far as the trust assets from time to time.

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Once the contracting trustee has satisfied any liability up to the amount of the trust assets, the contracting trustee has no further liability in respect of his personal assets.

Subparagraph 1(a) is engaged where a third party “knows that the trustee is acting as trustee”. The state of knowledge of the third party is a matter of fact to be determined in each case. Nothing more is required for subparagraph 1(a) to apply (such as knowledge that the contracting trustee is empowered to enter into the transaction) and there is no obligation to take steps to ascertain the capacity of the trustee. The relevant time to consider the third party’s knowledge is the time that the contract was entered into.

This reflects the scope for the third party to enquire into the standing of the contracting trustee, whom he knows acts as a trustee. This might include an opportunity to take security in respect of the ultimate fulfilment of the contracting trustee’s obligations or any other arrangement which the third party considered prudent (for example, the third party might require an undertaking that the contracting trustee would not make distributions of trust property to beneficiaries until the liability is repaid).

Accordingly, subject to any separate precautionary measures that a third party might take, sub-paragraph 1(a) means that a person who knowingly transacts with a trustee must accept that in due course any claim he makes will be met only to the extent that there are trust assets available when the claim falls to be satisfied.

The Court of Appeal also held that a further consequence of the words that claims shall “extend only to the trust property”, is that any claim is not to be limited to the trust property held by the contracting trustee with whom the other party has contracted. Instead, it extends to all of the trust property which exists as a result of the regular administration of the trust when the claim falls to be satisfied.

Thus if at the time the claim falls to be satisfied the contracting trustee has been replaced and has handed over the trust assets to a successor trustee (rather than exercising its lien against the trust assets, as is common), the third party must still make his claim against the contracting trustee with whom he contracted. The inevitable consequence is that a contracting trustee has a right to be indemnified by the successor trustee out of, and up to the limit of, the trust assets held by the successor trustees. If it were to be otherwise, this would leave the creditor in a situation where, despite being entitled to have his claim satisfied from the entire trust property, some of that trust property would be beyond the reach of the contracting trustee who was obliged to satisfy his claim.

By virtue of Article 32(1)(a) therefore, contracting trustee now enjoys a right to be indemnified by his successor trustee up to the limit of the trust assets held by the successor trustee. This right which has been created by the statute was characterised by the Court of Appeal as being an equitable right in the form of, or, analogous to a nonpossessory lien. Although the right has been created by the statutory provision in Article 32(1)(a) in this instance, the Court of Appeal was satisfied that the general law of Jersey recognised a form of equitable interest which would justify a contracting trustee who had disposed of assets to a successor trustee having an entitlement to recover such of those assets as is necessary to satisfy a claim.

In the light of its construction of Article 32(1)(a) the Court of Appeal held that a third party does not have a direct right of recourse to the trust assets. The creditor’s claim remains against the contracting trustee who will have access to such trust assets as may be held by a successor trustee. The creditor may be entitled to a right of subrogation in respect of the contracting trustee’s right of indemnity against the contracting trustee.

The meaning and effect of Article 32(1)(b)

The Court of Appeal then turned to Article 32(1)(b). It is important to note that this provision was not engaged on the facts nor was it addressed in the arguments of the parties. As such, the Court’s observations on this aspect may be considered to be obiter and no findings have been made on this provision. Article 32(1)(b) applies when the other party does not know that the contracting trustee is acting as a trustee. In these circumstances the contracting trustee will have personal liability. Such personal liability is, however, stated to be subject to the qualification “without prejudice to his or her personal liability, the trustee shall have a right of recourse to the trust property by way of indemnity”.

The Court of Appeal observed that the provision confers a statutory right of indemnity which changes the position under Jersey law as compared to trust law as it has developed in the Commonwealth. In particular, the Jersey provision appeared to entitle the contracting trustee to an indemnity irrespective of whether the contracting trustee had committed a breach of trust.

The Court observed that, whereas paragraph 1 of Article 32 may be regarded as dealing with the external relations of a trust, paragraph 2 may be regarded as dealing with its internal relations, most obviously those between the contracting trustee and the beneficiaries. Paragraph 2 preserves any rights that beneficiaries may have in a case of a breach of trust, but it does so separately from the mechanism for the satisfaction of thirdparty claims which exists under sub-paragraph 1(a). The Court of Appeal indicated that paragraph 2 also applies to sub-paragraph 1(b) so that where sub-paragraph 1(b) is engaged, the creditor has a right to have his claim satisfied by the contracting trustee personally but the contracting trustee may still enforce his right of indemnity against the trust assets in respect of the third party liability even where the contracting trustee may be, or may be alleged to be, in default.

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Accordingly, even where the contracting trustee has personal liability under subparagraph 1(b), so long as there are sufficient trust assets to satisfy the claim, a creditor may not be prevented from having his claim satisfied by the contracting trustee (including by subrogation to the contracting trustee's right of indemnity) even though the contracting trustee may have acted in breach of trust in assuming the obligation or otherwise. Beneficiaries may have to be content with a separate breach of trust claim against the contracting trustee who is in default to recover the amount paid to the creditor. They may find in due course that the contracting trustee does not have sufficient personal assets to restore the trust fund.

Conclusion

The Court of Appeal's judgment means that Articles 32(1)(a) and (1)(b) together represent an alteration to the rights of creditors, beneficiaries and trustees as a matter of Jersey law. Creditors are entitled to have their claim settled out of such trust assets as there are, including trust assets held by a successor trustee, notwithstanding any liability the contracting trustee may have for breach of trust.

Discussion

Application to Guernsey Section 42 of the Trusts (Guernsey) Law, 2007 (the "TGL") contains the similar, but not identical, provision under the Guernsey legislation. It provides:

"42. (1) Subject to subsection (3), where, in a transaction or matter affecting a trust, a trustee informs a third party that he is acting as trustee or the third party is otherwise aware of the fact, the trustee does not incur any personal liability and a claim by the third party in respect of the transaction or matter extends only to the trust property. (2) If the trustee fails to inform the third party that he is acting as trustee and the third party is otherwise unaware of the fact—(a) he incurs personal liability to the third party in respect of the transaction or matter; and (b) he has a right of indemnity against the trust property in respect of his personal liability, unless he acted in breach of trust. (3) Nothing in this section prejudices a trustee's liability for breach of trust or any claim for breach of warranty or authority. (4) This section applies to a transaction notwithstanding the *lex causae* of the transaction, unless the terms of the transaction expressly provide to the contrary."

In its June 2014 judgment the Court of Appeal commented (at para 110) that it appeared to the members of the Court "that the provisions of Section 42(1) of the TGL are to the same effect as Article 32(1), namely that a claim by a third party, with appropriate knowledge, extends only to the trust property." (The reference to Article 32(1) appears intended to refer to Article 32(1)(a)). The Court of Appeal's decision on the meaning and effect of Article 32(1)(a) would accordingly appear to apply equally to the meaning and effect of Section 42(1) of the TGL.

However, given the express wording of Section 42(2)(b) of the TGL (whereby a contracting trustee has a right of indemnity, unless he acted in breach of trust), the Court of Appeal's observations in respect of the meaning and effect of Article 32(1) (b) of the TGL (whereby a contracting trustee has an indemnity even where there is a question of breach of trust) may give rise to a different result under Guernsey law to Jersey law. In our view, under Section 42(2) of the TGL a contracting trustee would not be able to claim an indemnity from the trust fund in circumstances where he was in breach of trust and which would otherwise deprive him of a right to an indemnity from the trust fund.

On a more practical level, the Court of Appeal's judgment may impact on the obligations of trustees involved in transactions with creditors in relation to the management of the trust funds after the transaction is entered into and until any claim arising from the transaction is satisfied. Where trust property is diminished through the 'regular administration' of the trust (paragraph 31) there is no scope for the contracting trustee to be found personally liable. Accordingly, the inference which may be drawn from this is that, if the trustee's management or administration of the trust property can be characterised as other than 'regular', the protection afforded to trustee of avoiding personal liability may be lost.

What will the Royal Court of Jersey make of the judgment? The parties to the appeal agreed that the Court of Appeal should approach construction of the TGL as if it were construing a statute of Guernsey. No expert evidence was received from Jersey lawyers as to the meaning of Article 32 as is often done where a contested point of foreign law arises.

Nevertheless, the same Judges sit on the Courts of Appeal of Guernsey and Jersey and the decisions from each Island can be expected to be highly persuasive in the other, with occasional exceptions. If the same issue arose for consideration by the Royal Court of Jersey the Court of Appeal's decision can be expected to feature heavily in argument but the Royal Court would be free to rule differently if persuaded that an alternative construction were preferable. That is particularly so in relation to the Court of Appeal's observations as to the meaning of Article 32(1)(b) of the TGL, where no finding was made as it was not necessary to resolve the issue before the Court of Appeal and the subordination of rights of the beneficiaries to those of creditors of the trustee (who did not realise that the trustee was transacting as trustee) is not free from difficulty.

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FIND US

Carey Olsen (Guernsey) LLP
PO Box 98
Carey House
Les Banques
St Peter Port
Guernsey GY1 4BZ
Channel Islands

T +44 (0)1481 727272
E guernsey@careyolsen.com

Carey Olsen Jersey LLP
47 Esplanade
St Helier
Jersey JE1 0BD
Channel Islands

T +44 (0)1534 888900
E jerseyco@careyolsen.com



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