

Institute of Law Jersey
Insights into Trust Law: The Channel Islands and beyond
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Le best of onshore and offshore trusts

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Ladies and Gentlemen

At some time this past summer a judge on the Seychelles Court of Appeal told me that an Irish law professor had been asked to prepare new trust legislation for the Seychelles. The judge would get me a copy. I received a “White-Paper Memorandum” (19 February 2011) together with the *Trusts Bill, 2011*. The Memorandum reports that the new legislation has been “heavily modelled” on Jersey’s trust law. It goes on to say: “Jersey trusts are regarded as one of the most respected offshore trust structures and, importantly, the Jersey Trusts Act has been evolved and improved over time as a result of a thorough testing in the Jersey courts.” This is a high compliment.

The States of Jersey in its Report and explanatory notes introducing the *Draft Trusts (Amendment No. 5) (Jersey) Law 201-* self-congratulates. The Report says: “Jersey is considered one of the finest trusts jurisdictions in the world. The trust industry is firmly established as a market leader, offering a sophisticated and established product backed up by a strong body of case law. This is coupled with the high quality of service offered by Jersey’s trust company business to their clients worldwide.” [Let’s remember this word — product — for later.]

The Bar Association of Seychelles commented (25 February 2011) on the draft Bill. Its position, it said, was that “any move to tinker with our system of property ownership laws or any other aspect of our private law should be done with great caution and wider and intensive consultation with the public.” The Bill, it also said, was “most disturbing [it] undermines our property

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laws (and in particular individual property rights) and the coherence of our legal system.” The Seychelles Bill has not moved forward.

Going back in time, the Commissioners in their 1859 Report published in 1860 (and republished in 1861) had this to say about the introduction of trusts in Jersey: “There is no law in Jersey expressly forbidding the creation of trusts by an act *inter vivos* ... Serious questions, as yet unsolved, arise as to the validity of the trusts declared in the deeds of conveyance ... The legal title ... to the land conveyed ... is not questioned or doubted. The whole subject at present is involved in doubt: there is neither express law, custom, nor judicial decision to lead to a satisfactory conclusion.” The Commissioners concluded that “legislation is imperatively required to settle important questions” one of which, the Commissioners observed, was whether “trusts will prevail against and supersede the ordinary liabilities and incidents of property in Jersey.” At the time the Commissioners were focussing on trusts for chapels and trusts of a public nature, such as trusts for gas or water works. They were not thinking of the modern-day international trust.

In 1984 the Trusts (Jersey) Law was enacted. Then and today, the coherence of Jersey’s legal system has not prevented the birth of a thriving trusts regime. Of course, Jersey land cannot be settled in trust, but in Jersey, as in Guernsey, the reasoning underscoring the Seychelles Bar Association’s outright rejection of new international trust legislation does not resonate. The Channel Islands care naught for the debate still raging in other civil and mixed legal property systems as to the nature of the trustee’s and beneficiaries’ interests in the trust property. In the *chemins* of Jersey and Guernsey the trustee has legal title and the beneficiary has an equitable interest, and if you care to call their respective interests “legal ownership” and “equitable ownership”, you are free to do so. Local lawyers and judges have long recognised that the terms “legal” and “equitable” are trust mannerisms — ways of expressing and metaphors for a series of rights, powers, duties and entitlements. In an important way, both Jersey and Guernsey know, as F. H. Lawson famously suggested, that you need not care about legal estates nor about equitable estates if your legal system does not need or desire to

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have a doctrine of estates¹. In the events, both Jersey and Guernsey know that one can — indeed one must — do away with ownership as a necessary starting point for the introduction of trusts into civil or mixed legal systems. Enjoyment, management and control are the starting points.

In truth, a modern, international offshore trust seated in a compact private law dealing with the limited events of a small population and land mass must not be frustrated by discussions relating to the conceptual underpinnings of the trust. Jersey and Guernsey trusts can be understood on their own terms and as fundamental legal categories unto themselves. To a certain extent, therefore, they are self-referential and self-reverential. Like the Quebec civil law trust, the Islands' property picture is problematic because this picture is terse to the point of mystery. Jersey and Guernsey do not manifestly formulate and do not positively define property interests in the trust. There is no categorical scheme for an understanding of the content of the trust container. Yet, notwithstanding the absence of any overarching theoretical construct, our trusts can be merchandised as discrete products, and so they have been. To some extent, Jersey and Guernsey trusts have done what Lionel Smith, in another context, stated might be done, that is to say that they have described “all of the law of trusts in ... precise juridical terminology that [does] not depend on historical distinctions between the common law and Equity.”²

Jersey and Guernsey trusts are hot and, as products, they must be attractive and competitive. The Consultation Group leading up to the *The Trusts (Guernsey) Law, 2007* cautioned, in relation to firewall provisions relating to non-enforcement of certain personal relationships, as follows: “The Group received evidence that the current position in Guernsey makes the jurisdiction unattractive for some advisers and their clients, and therefore uncompetitive.” The Group was determined to change that unfortunate

¹ F. H. Lawson, *A Common Lawyer Looks at the Civil Law* (1953, University of Michigan Law School) at 197 et seqq.

² L. Smith, “Common Law and Equity in R3RUE”, (2011) 68 *Washington & Lee Law Review*, pp. 1185-1202 at 1202.

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perception, and arguably did. Guernsey now has hot firewall legislation — to some observers, extravagant³ — but hot.

Attractive, competitive, hot products — bespoke and boutique — are responses to the trust deal, and it is the trust deal that underscores my remarks this afternoon. The following question might be asked: “Is contemplation of the trust an exercise in theory, a matter of knowledge, a speculative venture or mere memorization of specific rules?” In Jersey and Guernsey, the trust is not a speculative venture but a practical venture, or co-adventure of the settlor-client and trustee. Here, as elsewhere in the offshore, the trust is more than a relationship. It is a deal. The trust is, as John Langbein has said, “a deal, a bargain, about how the trust assets are to be managed and distributed.”⁴ The conception of the trust, as a contract, as a deal and as “functionally indistinguishable from the modern third-party-beneficiary contract”⁵ has been robustly criticized by Ming-wai Lau but as Lau admits in his exciting book *The Economic Structure of Trusts*⁶: “The contractarian account of trusts is wrong in many regards, but it has got one thing right: it candidly captures the mindset of the trust industry and its clients — that the trust is a management contract between the settlor and the trustee.”⁷ We might say, therefore, that the centre of gravity lies between the settlor and the trustee. Lau further states that modern trusts are often characterized by several features amongst which three are striking: the settlor’s transfer of assets to strangers “in faraway lands”; the boilerplate nature of most trust deeds; and the “central role settlors play in trust creation and, sometimes, operation.”⁸ The trust talk of offshore jurisdictions is a lively rhetoric of administrative skill and legislative rectitude, and yet the hard reality is that settlors of offshore trusts are most often driven by tax, privacy and asset protection considerations.

³ J. Harris, “Guernsey’s Private International Law Rules for Trusts — Model Offshore Solution or Recipe for Conflict?”, (2008) 12 Jersey & Guernsey Law Review, pp. 289-317 at 315-317.

⁴ J. H. Langbein, “The Contractarian Basis of the Law of Trusts”, (1995) 105 Yale Law Journal, pp. 625-675 at 627.

⁵ *Ibid.*

⁶ M. W. Lau, *The Economic Structure of Trusts* (2011, Oxford University Press) at 21-35.

⁷ *Ibid.* at 30.

⁸ *Ibid.* at 31.

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In sum, today's Jersey and Guernsey trusts are very often trust deals managed, maintained and benefiting, at least in the first instance, the settlor, and there is a legislative projection of these trusts as such. The Bailiwicks' States know this to be true, and every new amendment is targeted to improving the deal, striving for the "best" and owning the podium. Once again, in the worlds of the trust, each trust has merit considered on its own terms for its own purposes and in its own culture. The "best trust" for one system is not the "best trust" for all. There is no trans-jurisdictional "best". In the future, the "best" trust for the Bailiwicks is the trust that we will wish to make of it — best (and happily) divorced, as I will suggest later, from the laws of England.

Let me open a parenthesis. One does not have to love the trust to practice trust law. One can be guardedly seduced. Indeed, one can believe, as I do, in forced heirship, community property and the rules on remoteness of vesting or duration. One can assert, as I do, that ownership is for the living.⁹ In fact, in my world, the trust is "the enemy of the people", as Christopher McCall has suggested elsewhere might be the case¹⁰, and in my world, we are called to cooperate one with another in our relations between ourselves and with respect to things. Cooperation and happiness are the two principal ideological objectives underscoring codified civil law systems. Their civil codes have been drafted to secure cooperation, foster happiness through absolute ownership of property and provide complete statements of rules for the proper conduct of the citizenry. I hope that you will agree with me that much of law is ideological and much also is mediated, subjective and experiential. My perception of the trust idea and my appraisal of the trust deal are a result of my experience with the trust. This experience extends way back to the day on or before the day on which the international trust was first hatched. Welcome to my world!

By like token, the Guernsey and Jersey trusts must be assessed in context as institutions of *a kind of law* and *a type of legal system* that is losing interest, if ever it was interested, in the Enlightenment principle that wealth is

⁹ M. McAuley, "Of Hurricanes and Me", (2006) 39-1 New York State Bar Association Trusts and Estate Section Newsletter, pp. 15-19.

¹⁰ C. H. McCall, "The trust as an enemy of the people", a paper presented at the Future of Trusts conference at King's College London, 13 April 2012.

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for the living. The abolition of forced heirship in Guernsey is a striking, recent example of this loss of interest.

Let me end this parenthesis by relating this short anecdote. In 2005, as best I recall, a group of Peruvian scholars visited me and others in Baton Rouge, Louisiana where I was teaching. They were interested in the trust. I told them that if a system is convinced that wealth is for the living, then the trust — as a paternalizing device — should have little, or no, part to play in it. They left discouraged.

Preparing for today I surveyed the literature. I wanted to see how others look at the trust of the modern era and how they see its future. All of the authorities admire Jersey and Guernsey trusts for what they are. Yet, no authority suggests that they are the best examples of modern trust legislation. Indeed, no authority I consulted has proposed the legislation of this or that system as being the best. Instead, every authority is concerned with the scope of one particular feature of the international trust, that is to say, the power of the settlor over the trustee — not over the trust property, but over the trustee.

For Lau, allowing settlors to be paternalistic and thereby to dictate what is good for beneficiaries is an important aspect of the incentivizing function of trusts.¹¹ “[C]ourts,” he says, “rely on the fictitious presumption that whoever is appointed as trustee will act in the best interest of the beneficiaries and will not be influenced by his appointor.”¹² Donovan Waters is concerned that since the 1970s the trust has moved towards quasi-agency where the settlor is dominant. On the topic of reserved powers, he says: “... this statutory move also brings the trust within a hair’s breath of agency.”¹³ If the irreducible core of the irreducible core is that it is sufficient that the core consists of the duty to perform the trusts honestly and in good faith for the benefit of beneficiaries, then how, in settlor reserved power trusts, can it be said that the exercise of these powers have the benefit of the beneficiaries in mind? This is the issue that the authorities have endeavoured to tackle.

¹¹ M. W. Lau, *op. cit.*, at 171.

¹² *Ibid.* at 176.

¹³ D. Waters, “Models of the Trust Ideas and Uses of those Models”, Chapter 13 in D. Brownbill (ed.), *International Trust Laws* (2011, Jordan Publishing Limited, Bristol) pp. B13-1-B13-66 at B-13-52.

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However, all authorities are suspicious of settlor reserved power trusts. For Donovan Waters and others, the *problématique* is how minimal a trustee's control might be for a trust to be a trust. Where do you draw the line? For me, the question is whether the trustee needs control. I ask the following — Is control by the trustee an indispensable element of the modern offshore statutory trust? I answer — It is not (apparently)!

The *communis opinio* is that there has been, and remains, an over-healthy — to the point of unhealthy — interest in the offshore in asset protection, forced heirship protection, protective and spendthrift trusts, non-disclosure to and disenfranchisement of beneficiaries, and settlor reserved powers. Some of the same developments have also occurred in the United States. The American scholar Joel Dobris says: “The view that trusts are there to beat somebody out of something is in the ascendancy.”¹⁴ Dobris also says: “The trust is being pulled and stretched like a piece of taffy. The high-minded want to modernize it and the low-minded want to turn it into a high-pressure product. Some traditional trust people are bound to get the vapors.”¹⁵ Dobris wrote this in the late 90s. He had not yet seen the settlor reserved powers in our Laws. To use Dobris' words, are Jersey and Guernsey low-minded?

How can Jersey and Guernsey comfort the professors and calm the authorities? In my view, the answer is to be found in creating new trust conceptions that are manifestly not part of the traditional framework of our trust legislation but are separately regulated. The answer lies in un-jumbling. Settlor reserved powers (and some other things such as spendthrift and protective trusts) should be yanked from the Trust Laws and repositioned in discrete legislation. In this way, gravity will make our trusts more beneficiary-centred and less agreement-based. We will return to the more traditional trusts contemplated here in Jersey in 1984 and yonder in Guernsey in 1989.

Borrowing John Langbein's way of looking at things, we could have one *kind of* trust that has more *intent-defeating* rules restricting the settlor's autonomy and another *kind of* trust with *intent-serving* rules implementing the

¹⁴ J. C. Dobris, “Changes in the Role and the Form of the Trust at the New Millennium, or, We Don't Have to Think of England Anymore”, (1998) 62 Albany Law Review, pp. 543-578 at 547.

¹⁵ *Ibid.* at 566.

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settlor's true intentions.¹⁶ The new kind of trust I envision will subscribe to the intention theory, that is to say, first, that the intention of the settlor is the law of the trust and, second, that the beneficiaries have to take the whole disposition including restrictions and conditions imposed by the settlor. As has been said, the settlor-trustee agreement will not launch the trust. It is the trust. Indeed, one of the great benefits of settlor-focussed trusts is that they more faithfully represent the deal and the reality of the client-trustee relationship without fear of sham — sham in the sense that the reality of the relationship does not match up with the documentation. The intention theory also has the merit of estopping beneficiaries from accepting some, but not all, of the benefits of a trust. I hope that this does not startle you. It should not, for it is one of the theoretical underpinnings of the new Guernsey foundation (although no one has yet identified it as such).

Let us now merchandise. There are two ways of achieving this objective. One is to draft a new trusts statute for a new *kind of* family wealth management trust. This is inconvenient and will result in much duplication. The other is to do what Cayman did with its STAR trusts. Cayman drafted a special series of provisions and then later blended them into a general trusts statute. I recommend this approach. J-STARS and G-STARS will be special trusts, and they will be alternative regimes. They will also be attractive and competitive products.

Clients want control. In a world of vast prosperity for some, people may have and eat their cake. There are numerous cakes for consumption, and they are all by American bakers. It has been observed that the Americans are moving away from the contractarian conception of the trust where the settlor has maximum flexibility and are moving towards the propertarian conception where the property rights of the beneficiaries are better protected. Thomas Gallanis, in a recent paper *The New Direction of American Trust Law*, believes that US trust law is reasserting the interests and rights of the beneficiaries.¹⁷ Gallanis remarks that although the organizing principle of the *Restatement (Third) of Property: Wills and Other Donative Transfers* is that

¹⁶ J. H. Langbein, "Mandatory Rules in the Law of Trusts", (2004) 98 Northwestern University Law Review, pp. 1105-1128.

¹⁷ T. P. Gallanis, "The New Direction of American Trust Law", (2011) 97 Iowa Law Review, pp. 215-237.

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the donor's intent is given effect to the maximum extent allowed by law, the *Restatement (Third) of Trusts* stresses that a private trust must be for the benefit of the beneficiaries.¹⁸ Notwithstanding this new direction, there is much in American trust law today that is pre-packaged for our consideration especially revocable and directed trusts. There are also statutory business trusts — another good idea from over the pond. It has been said that “[I]n terms of maximizing settlor control and minimizing beneficiary's rights, the American revocable trust simply puts even the most exotic Cayman Island STAR trust to shame.”¹⁹ Yet, to my mind, the revocable trust — although not necessarily revocable — or incidents and features of the revocable trust — and the directed trust — constitute dynamic ways forward for our Islands' trust industries.

Revocable trusts are widely used in the United States by a certain class of people as lawful means to avoid the costs of probate and to increase privacy. They also have distinct tax advantages. In a revocable trust the settlor retains extensive rights such as a beneficial interest for life, powers to revoke and modify and the right to serve as or control the trustee. A true, traditional trust may only come into effect at the death of the settlor. The validity of the revocable trust as an inter vivos trust is not affected by the fact that the interests of all beneficiaries other than the settlor do not take effect in possession or enjoyment before the settlor's death. The Missouri Court of Appeals has recently reviewed this type of trust in the matter of the *Stephen M Gunther Revocable Living Trust*.²⁰

The facts are simple. In 1997 Stephen established his trust and named Barry as his initial trustee. In 2006 he amended the trust and named himself as trustee. He also changed the beneficiaries upon his death to his then living descendants to be held in trust for them if they were under 25. He died in 2009 leaving his wife and two minor children. The minor children asked for an accounting from Barry for his administration while trustee for the period 1997-2006. The court held that the trustee had no fiduciary relationship with the beneficiaries before the settlor's death and that the beneficiaries were not

¹⁸ *Ibid.* at 216.

¹⁹ M. W. Lau, *op. cit.* at 32.

²⁰ *In re: Stephen M. Gunther Revocable Living Trust*, 350 S. W. 3d 44 (Missouri Court of Appeals, 4 October 2011)

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entitled to an accounting while the settlor still lived and the trust was revocable. The court referred to the *Missouri Uniform Trust Code* which provides as follows: “[w]hile a trust is revocable and the settlor has capacity to revoke the trust, rights of the beneficiaries are subject to the control of, and the duties of the trustee are owed exclusively to, the settlor.”²¹

Revocable is a tag. One might have an irrevocable trust with the same provisions or one which gives the settlor a power of revocation. A revocable trust satisfies all the essential elements of a trust. There is a transfer with the *intention* of creating a relationship. It is funded with property *title* to which is held by a trustee to be administered for a lawful trust purpose or for the *eventual benefit* of appropriately ascertainable beneficiaries but, in the words of the Restatement, a revocable trust is “primarily and properly for the settlor while alive”.²² The words “properly for the settlor” are telling and important.

Revocable trusts have spawned directed trusts. A number of American states have enacted directed trusts statutes. Virginia was the 13th such state earlier this year and was followed in August by Illinois. So, this is fairly new stuff. The focus of a directed trust is not the settlor but the trustee. Under a directed trust, the settlor gives any person not a trustee, called a trust director, the power to direct the trustee on any matter including, in most circumstances, matters that would ordinarily involve the exercise of judgment or discretion. The trustee has no liability to the beneficiaries of the trust for losses from actions taken or not taken by the trust director. Under most statutes, the trust director is presumed to be a fiduciary. Additionally, the trustee, called “an excluded fiduciary”, in Illinois, has no duty, as the statute says, “to monitor, review, inquire, investigate, recommend, evaluate or warn” the beneficiaries of any inaction or action of the trust director.²³ No duty. Under a directed trust the trustee effectively becomes a custodial caddie, occasionally offering insightful advice.

I have very little time to tell you what else is happening of interest and of profit. However, out of duty, I must tell you about the statutory business trust. This trust is an entity and, as such, has a type of legal personality. It is

²¹ *Ibid.* at 46.

²² Restatement (Third) of Trusts § 25 (General Comment a.)

²³ Section 5/16.3 (f), 760 Illinois Compiled Statutes (in force 1 January 2013)

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separate from its trustees and beneficial owners, has capacity to sue and be sued, own property and transact in its own name. A comprehensive statute — *Uniform Statutory Trust Entity Act* — with extensive comments and notes has been published by the Uniform Law Commission in the United States. These business trusts are particularly useful for the organization of unit trusts and for asset securitization.

I have no time today to tell you about developments in the Bahamas. There, there is a new trustee entity under legislative mandate to be and to remain insolvent. The executive entity, as it is called, must not hold assets other than assets necessary to pay its on-going administrative expenses.²⁴ This takes the private trust company trustee idea to a whole new level and destroys the traditional principles of trustee liability.

Clearly, in the world of deals and products, the offshore does not need England anymore.

Thank you.

²⁴ Section 4, Executive Entities Act, 2011 (Bahamas)