CHANCERY BAR

Prest and Beyond – Part 2 (Trust structures)

> *"If this court now concludes that all these cases* [in the Family Division lifting the corporate veil] *were wrongly decided they present an open road and a fast car to the money maker who disapproves of the principles developed by the House of Lords that now govern the exercise of the judicial discretion in big money cases.*
>
> *Per Thorpe LJ dissenting in the Court of Appeal in Prest v Petrodel*

1. This section of this paper will consider the impact of the Supreme Court's decision in *Prest* on offshore trusts. The judgment is significant because it is standard in offshore trust structures for the underlying assets to be owned through a corporate structure.

2. The treatment of offshore trusts in English divorces has been the source of friction and controversy for years.

3. Since *White v White,* the English court needs to know about all the assets and resources of each party to the marriage in big money cases, so that it can test its conclusion against the "*yardstick of equality*". In *Charman v Charman* [2006] WTLR 20 Wilson LJ suggested that in considering whether trust assets are a resource of a party the important question is whether the spouse has "*immediate access to the funds"*. And if the trustees would, if asked, be likely to advance capital to him/her immediately or in the future the court may make an order against a spouse as "*judicious encouragement*" to the trustees to make the sums available to that spouse to satisfy the order: see *Thomas v Thomas* [1995] 2 FLR 668). The circumstances in which such an order is appropriate should, in theory, be limited; *AvA (St George Trustees Ltd and ors,)* [2007] EWHC 99(Fam). But in practice there is little evidence of restraint.

4. Quite apart from trust assets being treated as a resource of a party to the marriage, the English court has power to make orders affecting trustees, including offshore trustees,

as part of the range of orders available to it under English matrimonial legislation. In particular:

4.1 the English Court may find that in reality the trust assets are those of one spouse on the ground that the trust is a sham or device (so that the court's orders against the spouse can be enforced directly against the trust assets);

4.2 the English court can make an order setting aside any disposition of property by a spouse (including a settlement) under s. 37(2)(b) and/or (c) Matrimonial Causes Act 1973 if made with the intention of defeating a person's claim for financial relief under the Act.;

4.3 the English court has power under s. 24(1)(c) Matrimonial Causes Act 1973 to vary the terms of "a nuptial settlement". The English Court has always asserted that this power extends to foreign settlements governed by foreign law: see *Nunneley v Nunneley* (1890) 15 PD 186, *Forsyth v Forsyth* [1891] P 363, *Charalambous* v *Charalambous* [2005] Fam 250, [2004] 2 FLR 1093

5. Historically the making of such orders strained international comity.

6. The Royal Court of Jersey repeatedly complained that the assertion of jurisdiction by an English court over a Jersey trust exceeded the normal bounds of judicial comity.

> *"The court regards as unlikely that an English court would so exceed the normal bounds of comity as to purport to vary a settlement governed by Jersey … law administered in Jersey by Jersey trustees, and which has no connection with England save that some of the beneficiaries resided there".*
>
> *In Re Rabaiotti's 1989 Settlement* (2000) 2 ITELR 763

> *"We agree with counsel that as a general rule, … it would be an exorbitant exercise of jurisdiction for a foreign court to purport to either vary the terms of a Jersey settlement or to declare such a settlement a sham."*
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> *CI Law Trustees & Folio Trust Co Ltd v Minwalla* [2005] JRC 099

> *"It would, in our view, avoid sterile argument, and expense to the parties, if the English courts were, in cases involving a Jersey Trust, having calculated their award on the basis of the totality of the assets available to the parties, to exercise judicial restraint and to refrain from invoking their jurisdiction under the Matrimonial Causes Act to vary the trust. Instead they could request this Court to be auxiliary to them… It appears to us*

that this would be a more seemly and appropriate approach to matters where the courts of two civilized and friendly countries have concurrent interest. It would furthermore be likely to avoid the risk of delivery of inconsistent judgments."

In the matter of the B Trust [2006] JRC 185

7. The legislative response by jurisdictions such as Jersey and Guernsey was to enact firewall legislation. Article 14(1)(b) Trusts (Guernsey) Law 2007 provides (inter alia) that "*the validity, interpretation or effect of {a Guernsey Trust or disposition to such a trust] or any variation or termination thereof*" is to be determined according to the law of Guernsey (disregarding Guernsey rules on conflicts of law) and without reference to the law of any other country. Article 14(4) provides:

> "(4) Notwithstanding any legislation or other rule of law for the time being in force in relation to the recognition or enforcement of judgments, no judgment or order of a court of a jurisdiction outside Guernsey shall be recognised or enforced or give rise to any right, obligation or liability or raise any estoppel if and to the extent that –
> (a) it is inconsistent with this Law, or
> (b) the Royal Court, for the purposes of protecting the interests of the beneficiaries or in the interests of the proper administration of the trust, so orders."

8. In *Re IMK Family Trust* [2008] JRC 136, the Royal Court concluded that the effect of the Jersey firewall legislation was that the Royal Court cannot enforce a judgement of the Family Division varying or altering a Jersey trust under the English statute even where the trustees have submitted to the jurisdiction of the Family Division. However, it also concluded that it could invoke the court's jurisdiction to administer a trust and give directions under the Jersey equivalent of Article 68 of the Trusts (Guernsey) Law 2007 which have the effect of achieving the objectives of the English judgement. Whether it will do so in a particular case is a matter of discretion, having regard to the interests of the beneficiaries. There are, however, limits. If the trustees do not have the power to give effect to the judgment (e.g. because W is not a beneficiary) then the Court cannot direct them to take that step.

9. In Jersey, which has generated the most learning on this topic, the starting point is that to preserve flexibility for the Jersey Court, trustees should not submit to jurisdiction but that it is usually in the interests of the trust for relevant information to be provided. For example, in *Re The H Trust* [2006] JLR 280 the Royal Court of Jersey said:

"It follows that, in most circumstances, it is unlikely to be in the interest of the Jersey trust for the trustee to submit to the jurisdiction of an overseas court which is hearing divorce proceedings between a husband and wife, one or both of whom may be beneficiaries under the trust. To do so would be to confirm an enforceable power upon the overseas court to act to the detriment to the beneficiaries of a trust when the primary focus of that court is the interest of the two spouses before it. It is more likely to be in the interests of a Jersey trust and the beneficiaries thereunder to preserve the freedom of action of both the trustee and this court to act as appropriate following and taking full account of the decision of the overseas court. We have said that this is likely to be the case in most circumstances. In some cases, e.g. where all the trust assets are in England, it may well be in the interests of a trustee to appear before the English court in order to put forward its point of view because, by reason of the location of the assets, that court will be able to enforce its order without regard to the trustee or this court."

and

"It seems to us important, in this case, that the husband and the wife should have the fullest information concerning the financial affairs of the trust so that any compromise which they reach, failing which any decision of the Family Division, is based upon the true financial position."

10. Even before *Prest*, while inferences might not be drawn against a trustee simply because he did not submit to jurisdiction (particularly if he took that stance in accordance with the directions of his local court), the position was different for a trustee who failed to provide relevant information and failed to give evidence at trial; see *BJ v MJ* [2011] EWHC 2011 and *Whaley v Whaley* [2011] EWCA Civ. 617. The view being taken in England was that such steps would not prejudice the trustees' non-submission to jurisdiction.

11. The encouragement in *Prest* to judges of the Family Division to "*use their experience*" and draw adverse inferences, should reinforce the offshore attitude that trustees, even if they do not submit to jurisdiction, should make available relevant information and give evidence to the English court.

12. To date, one of the main exceptions to the approach that trustees should generally not submit to the jurisdiction in a divorce has been where significant trust assets have been located within that jurisdiction. In such circumstances it might be in the interests of the trust for the trustees to submit to jurisdiction and be heard on what orders should be made against those assets. Before *Prest*, it had to be assumed that the physical location of assets within the jurisdiction made them vulnerable to orders of the Family Division

even if there were companies interposed between the trustees and the underlying assets. In *Hope v Kreji* [2012] EWHC 1780, for example, Mostyn J observed:

> "In most overseas trust situations there will likely be an offshore company interposed between the trust and the underlying asset. This is the position here. The fact that there is an interposition of a company has to my knowledge never been argued, let alone found, to be an impediment to making an effective variation."

13. In the light of *Prest*, these assumptions need to be revisited.

14. In *Prest* itself, the Supreme Court was able to "save" the position by finding a resulting trust. Where there is a professionally run offshore trust, however, the issue is not likely to be whether or not the assets held by companies within the structure are held on resulting trust for the settlor. Provided the initial settlement of funds, and the addition of property to the trust fund, has been properly documented, any presumption of resulting trust will have been rebutted.

15. So what is the threat? How can an English court now enforce an award against the assets of a company owned by trustees who do not submit to jurisdiction?

16. There will be rare cases in which the offshore trust is a sham. And there will be slightly less rare cases where the trust can be set aside as having been set up to put assets out of reach in the event of a divorce. Less rare because the prohibited purpose need not be the sole, or even the main motivation in creating the settlement. It is sufficient if it is a substantial purpose; *IRC v Hashmi* [2002] WTLR 1027 (s. 423), *Kemmis v Kemmis* [1988] 1 WLR 1307 at 1330-1331 (s. 37); *Mubarak v Mubarik* [2007] EWHC 220 (s. 37). S. 37 cases are regarded as impropriety. The decision of *C v C* [2006] EWHC 336 makes clear that because of the fraud exception, legal professional privilege will not attach to communications between the settlor and his lawyers in relation to the creation of such a trust. So one can see that in these exceptional cases, one might actually have the right conditions to justify piercing the corporate veil of companies interposed between the trustees and the underlying assets even under the strict *Prest* principles.

17. But the real threat is the English family judge's power to vary a nuptial settlement under s. 24(1)(c) Matrimonial Cause Act 1973. The reference to "a nuptial settlement" can

mislead. It is not restricted to a settlement constituted by deed creating a conventional trust. There is no statutory definition of a nuptial settlement and the caselaw has given it a very wide meaning. It covers *"any arrangement which makes some form of continuing provision for both or either of the parties to a marriage" (DR v GR [2013] EWHC 1196).*

18. So in *N v N and F Trust* [2005] EWHC 2908 (Fam) the family home was owned by a Bahamian company, which in turn was owned by a Jersey trust. It was common ground that the Jersey settlement was not *per se* a nuptial settlement which could be varied by the court under section 24(1)(c) of the 1973 Act. But Coleridge J held that the property was subject to an ante-nuptial settlement which could accordingly be varied.

19. In *Ben Hashem v Al Shayif* [2009] 1 FLR 115 an order was made under this section in respect of property owned by a company (owned by husband as to 30% and his relatives as to the rest) where it had tolerated the occupation of the wife after she had forced her way into it.

20. IN *DR v GR* [supra] Mostyn J said:

> "Indeed it is clear to me that a family company which under an arrangement makes some form of continuing provision for both or either of the parties to a marriage is capable <u>of itself</u> of amounting to a variable nuptial settlement whether or not the company is owned by a trust of which the spouses are formal beneficiaries."

21. More controversially, he went further:

> " I am of the opinion that if under an arrangement "some form of continuing provision for both or either of the parties to a marriage" (which would include, on the authorities, the provision of accommodation) has been made from assets held by a group of family companies then the entire set-up, when viewed as a whole, is capable of amounting to a variable nuptial settlement. If the top company is owned by a trust of which the spouses are formal beneficiaries then the position is a fortiori."

22. In other words, it seems that if any property held in a trust structure can properly be regarded as subject to a nuptial settlement, then the entire structure is "capable" of being regarded as a nuptial settlement. Accordingly, in the view of Mostyn J the interposition of companies between the trust at the top of the tree and the assets at its bottom did not act as any kind of impediment to making a variation which disposed of the actual assets at the bottom. *DR v GR* was decided in between the Court of Appeal

and Supreme Court decisions in *Prest*, but it is hard to see how the Supreme Court decision affects the Mostyn "side step".

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