

Dealings with third parties: the new BVI legislative solution

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Personal liability of the trustee and the uncertainty faced by third parties in terms of being paid has inhibited the use of trusts for trading purposes. Recommendations by the Trust Law Committee in England, where the changes have not yet been made, have been the basis of the amendments to the BVI laws. These changes are intended to encourage the use of BVI trusts in a commercial context. This article describes how these changes have made BVI trusts internationally more useful for this purpose.

The Trustee Act of the British Virgin Islands (previously amended in 1993) has once again been amended by the passage of the Trustee Amendment Act, 2003 (“the Amendment Act”).

The Amendment Act seeks to address a number of problems faced by practitioners and proposes a legislative solution to those problems. This article is concerned with the problem of third party liabilities of a trustee and will look at the legislative solution to this problem which the BVI Government has adopted.

The problem

BVI trusts (ie, trusts created under the laws of BVI) do not have a legal personality separate and distinct from their trustees and, therefore, like English trusts, cannot incur liabilities. Instead the liabilities must be incurred by the trustees, and in their own names, not as agents for the trust fund. Further, the persons to whom the trustees have incurred liabilities (the third parties) will have no direct right to demand payment out of the trust estate. Their primary remedy is against the trustee and, if circumstances allow, a possible right to have recourse to the trust fund by way of subrogation to the trustee’s right of reimbursement, that is, a right to be put in the place of the trustee and thereby receive payment from the trust fund.

This right of subrogation, however, is dependent upon and, therefore, limited by the right of the trustee to reimbursement. Where the trustee has incurred a liability to a third party but has no right to be reimbursed (for example, because the trust is declared invalid, the liability was incurred improperly or the trustee, by reason of breach of trust or otherwise, is himself indebted to the trust fund to an extent exceeding his claim to indemnity) the third party will be in no better position and will have no claim against the trust fund. In addition, recourse cannot be made to the right of subrogation where the trustee is insolvent or circumstances are such as to lead to the reasonable conclusion that a judgment against the trustee would be pointless.

From the standpoint of each of the parties, this state of play was unsatisfactory:

(a) for the trustees: they were personally liable and, therefore, even if acting properly, could be personally at risk if the assets of the fund were insufficient to meet the liability; and

(b) for the third party: he is required to put his faith in the trustee that he will be, or will be able to be, repaid either by the trustee or out of the trust estate and even that the trustee will administer the trust in such a manner as would not be prejudicial to his interests.

The Trustee Act currently in force sought, in at least some small measure, to address some of the concerns of the trustees by excusing them from personal liability in certain limited circumstances,¹ and of some of the concerns of third parties, by providing that they need not be concerned about the application of monies paid to trustees on a sale or mortgage purportedly made under any trust or power vested in the trustees.²

These provisions, however, were felt not to have gone far enough to address these concerns. In an attempt to address some of these difficulties in commercial transactions, trustees frequently have been given the power in the trust instrument to create a fixed charge over specific assets in the trust fund or even to create floating charges over the trust fund generally. While the propriety of a fixed charge is not really questioned, there is some doubt as to whether floating charges can properly be created under the present law and if so, whether they can survive a change of trustee, without novation of the charging document in favour of the new trustee.

The existing state of the law therefore was viewed as creating serious practical difficulties for trustees and third parties and was felt to seriously inhibit legitimate commercial dealings by trustees with third parties.

The BVI solution

In considering a solution to these difficulties faced by trustees and third parties, the BVI considered, and in large part sought to implement, by legislative amendment, several of the recommendations for reform put forward by the Trust Law Committee in England in its report³, notwithstanding that these reforms have not yet been implemented in England. However, the BVI did not adopt these proposals in their entirety, but made certain departures, whether simply to achieve better accord with local requirements, or as a more cautious step as it attempted to venture out and lead in this area of the law.

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The Amendment Act therefore introduces a whole new section to the Trustee Act regarding “Trustees and Dealing with Third Parties”, which is now contained in Part X of the Act. Some of the important provisions introduced by the Amendment Act are:

- (a) It seeks to prescribe exactly how a third party can satisfy itself that a transaction will be regarded as properly entered into by the trustee and provides that if so entered into, any property acquired by the third party in, or by virtue of, the transaction is taken free and discharged from the trust and the third party need not be concerned to see that it was properly acquired;⁴
- (b) It provides that if (but only if) the terms of the trust expressly state that:
 - (i) a trustee, who has disclosed his fiduciary capacity in the contract with any party, which was properly entered into by the trustee, or the other party was otherwise aware of that capacity, will not (subject to the terms of the contract) be personally liable under, or by virtue of, such contract;⁵ and
 - (ii) a third party may assert a claim against the trustee in the trustee’s fiduciary capacity, whether or not the trustee is personally liable for the claim, and be entitled to satisfaction directly out of the trust fund rather than by way of subrogation to any right of indemnity of the trustee;⁶
- (c) It provides that if the trust deed does not include the provision which is referred to in paragraph (b) above, although the trustee remains personally liable, his liability will be limited only to the extent of the value of the trust fund when the payment falls due if the contract was properly entered into by him and he has disclosed, or the other party was aware of, his fiduciary capacity;⁷
- (d) It provides that the trustee will only be personally liable for torts committed in the course of administering the trust, or for obligations arising from ownership or control of trust property, if the trustee is personally at fault;⁸
- (e) It provides that if (and only if) the terms of the trust expressly so provide, a trustee may, by declaration in writing, if so required by a person lending money to a trustee of a trust, vary the trust to restrict or impose conditions in the exercise of the trustee’s powers of investment or management and administration of the trust, or the rights of the beneficiaries, including objects of powers to receive trust property to which they have or may become entitled;⁹
- (f) It provides, if the terms of the trust expressly so provide, for the creation of fixed legal or equitable mortgage or charges over all or any of the property of the trust

or of a “trustee statutory change” (similar in effect to a floating charge over the entire or a part of the fluctuating pool of assets) provided that the contract was properly entered into by the trustee and with a person acting in good faith and for value. The Amendment Act also sets out the order of priority of the trustee statutory charge, unless otherwise agreed by the parties concerned.¹⁰

Conclusion

The BVI therefore has considered the serious impediments to trustees seeking, in the interests of their beneficiaries under the trust, to engage in any commercial dealings, and has sought in large measure to address these concerns in a manner designed to instil a greater sense of certainty and thereby encourage the use of BVI trusts in the commercial context. Although the amendments made by the Amendment Act are in many ways groundbreaking in that no such, or very little, statutory force has ever before been given to these issues anywhere in the world, the BVI has decided to step cautiously, preferring to leave some of these matters to the parties themselves to be decided at the time of the creation of the trust. This, therefore, promotes great flexibility and enables greater protection for all concerned, in such manner as is appropriate in each particular circumstance. It is important to note also that this new Part X introduced by the Amendment Act will only apply to trusts created on or after the date on which Part X comes into force.

Endnotes:

1. See Sections 27 and 28 of the Trustee Act.
2. See Section 18 of the Trustee Act.
3. Rights of Creditors against Trustees and Trust Funds (June, 1999).
4. See Section 95 of the Amendment Act.
5. See Section 97 (3) of the Amendment Act.
6. See Section 97 (4) of the Amendment Act.
7. See Section 98 (2) of the Amendment Act.
8. See Section 99 of the Amendment Act.
9. See Section 101 of the Amendment Act.
10. See Section 102 of the Amendment Act. The Trust Law Committee Report had recommended the creation of such charges, but the BVI has taken a more cautious line by giving the power to trustees only when the trust instrument expressly provides for them to have it.

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“... if the trust deed does not include the provision which is referred to in paragraph (b) above, although the trustee remains personally liable ...”

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