

Article

A Seismic Shift to Certainty: “Substratum” and the Proper Construction of Trust Deeds

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The Bermuda Court of Appeal has unanimously allowed an appeal by the Trustee of the US\$560m Global Resource Trust (“GRT”) in a significant decision which rejected the proposition that the “substratum” of the trust will prohibit the exercise of powers to add or exclude beneficiaries.

The decision will be of particular interest to trustees in the common law jurisdiction, having reaffirmed the test to be applied when determining the validity of a trustee’s purported exercise of a power.

The Court of Appeal’s decision in *Grand View Private Trust Company Ltd v Wong and Ors* (Civil Appeal No. 5A of 2019), delivered on 20 April 2020, held that there is no need to imply a trust’s substratum – described as “a metaphorical term the characteristics of which it may be difficult to define, and which may not necessarily exist” - into trustees’ dispositive powers.

In his Judgment, the President of the Court of Appeal, Sir Christopher Clarke, found that, while inappropriate in a case such as this where the Trustee was entitled to add or exclude beneficiaries, if a metaphor has to be used (which it does not) then either:

- (i) there was no substratum of GRT; or
- (ii) the substratum was one that could shift, and the beneficial core was a flexible one, since the beneficiaries were capable of alteration from time to time throughout the life of the trust.

Moreover, where trustees exercise powers in accordance with what they honestly consider to be the purpose for which a settlor created the powers, this will *not* constitute a fraud on a power.

The President laid down no less than sixteen reasons why he disagreed with the Judgment of the lower court, including:

1. Given that the initial class of discretionary beneficiaries consisted of volunteers, and that the power was a power to add or exclude beneficiaries, the starting assumption should be that the discretion could be exercised in a way which was not confined to promoting the interests of the existing beneficiaries by favouring their family or their connections.
2. The wide definition of “person” in the trust deed made it difficult to argue that the power to add and exclude any such person was only capable of being properly exercised in a manner which preserved the trust’s character as a “dynastic family trust.
3. The President did not accept that the intentions of the settlor in establishing the trust and his purpose in granting the power can only be determined by reference to the terms of the trust and nothing more. Rather, trustees are entitled to - and it is the better view that they are bound to - have regard to the settlor’s wishes expressed from time to time.

The President found that the correct approach was to construe the trust deed in the usual way. The Court therefore reaffirmed that Lord Walker’s three-step test in *Pitt v Holt* should be applied when determining whether the purported exercise by a trustee of a power is invalid, namely:

- Whether the way in which it has been exercised is not within, or contrary to, the express or implied terms of the power (the ‘scope of the power’ rule);
- Whether the trustee has given adequate deliberation as to whether and how he should exercise the power (the ‘inadequate deliberation’ rule); and
- Whether the use of the power, although within its scope, was for an improper purpose i.e. a purpose other than the one for which it was conferred (the ‘improper purpose’ rule).

This Appellate Judgment from Bermuda has provided much-needed clarity for Trustees, particularly as the concept of “substratum” is so nebulous and difficult to pin down.

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