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An offshore perspective: reservation of powers in BVI trusts

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What is a 'trust', how are they established and, more importantly, how are they controlled? This article explores how the BVI Trustee Act 1961 and the Trustee (Amendment) Act 2021 strengthen the British Virgin Islands' (the **BVI**) trust law by reserving powers for the settlor of a trust and providing an attractive, flexible jurisdiction for trust formation.

An introduction to trusts and the concept of reserving powers

A 'trust' is a legal relationship which is created by a person (known as a settlor) for the benefit of a person or charity (known as beneficiaries), or for a particular purpose. A trust can be created in life or on death and involves the trust assets being controlled by another person (known as a trustee). Trust instruments can also appoint a protector, who may have other powers including authorising trustees to exercise their powers. Trusts are often a popular choice to allow individuals to divest their ownership and control of assets for various reasons, including for tax or succession planning purposes.

The BVI is an established international financial centre which sees a significant amount of trust creation and resulting litigation. In the BVI, the general principles of trust law derive from English common law. This is supported by statute, including the BVI Trustee Act 1961 and the more recent Trustee (Amendment) Act 2021.

Traditionally, the creation of a trust would involve a settlor relinquishing their power over the trust assets and when a trust is established, it is usual for the settlor to transfer the legal title to their assets to a trustee, to be held for the benefit of the beneficiaries or for a particular purpose. However, this concept has not always been viewed favourably by settlors and there has been a movement towards settlors seeking to retain control of the trust assets. This is a global issue which has been considered by Courts in different jurisdictions and, by way of illustration, two examples of recent case law on this topic are briefly considered below.

Reservation of powers in the BVI

A settlor would often prefer to retain control over their assets and the BVI was the first offshore jurisdiction to introduce reservation of powers legislation, which affords settlors this flexibility. In support of this approach, Article 2 of the Hague Trusts Convention clarifies that "*the reservation by the settlor of certain rights and powers, and the fact that the trustee may himself have rights as a beneficiary, are not necessarily inconsistent with the existence of a trust.*"[1]

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BVI trust law was strengthened by the introduction of the Trustee (Amendment) Act 2021, which came into force on 9 July 2021. Section 86 of the Trustee (Amendment) Act 2021 replaced section 86 of the BVI's Trustee Act 1961 and expressly states that settlors are able to reserve extensive powers, including powers to:

1. revoke the trusts in whole or in part;
2. vary or amend the terms of a trust instrument or any of the trusts, purposes or powers arising thereunder in whole or in part;
3. advance, appoint, pay, apply, distribute or transfer trust property (whether income, capital or both) or to give directions for the making of any such advancement, appointment, payment, application, distribution or transfer;
4. act as, or give binding directions as to the appointment or removal of, a director or an officer of any company wholly or partly owned by the trust or to direct the trustee as to the manner of exercising voting rights attaching to any of the shares held in such company;
5. give binding directions in connection with the purchase, retention, holding, sale of or other commercial or investment dealings with trust property or any investment or reinvestment thereof or the exercise of any powers or rights arising from such trust property;
6. appoint, add, remove or replace any trustee, protector, enforcer or any other office holder or any advisor, including any investment advisor or any investment manager;
7. add, remove or exclude any beneficiary, class of beneficiaries or purpose;
8. change the proper law of the trust;
9. change the terms of the trust which specify which courts have exclusive or non-exclusive jurisdiction in any proceedings involving rights or obligations under the trust; and
0. restrict the exercise of any powers, discretions or functions of a trustee by requiring that they shall only be exercisable with the consent, or at the direction, of any person specified in the trust instrument.[2]

The powers listed above can be reserved by the settlor without invalidating the trust, preventing the trust taking effect according to its terms or cause any of the trust property to be part of the estate of the settlor for the purposes of succession on death.[3] This is one example of the flexibility which makes the BVI an attractive jurisdiction for trust formation.

A second example of this flexibility is the BVI's VISTA trusts which were created by the Virgin Islands Special Trusts Act, 2003. There are several requirements for such trusts, including that the assets of these trusts may only include shares in certain BVI companies

VISTA trusts are unique to the BVI and the trust instrument may allow the settlor and/or directors of the underlying company to retain control. In such trusts, the responsibility of the trustees can be limited to the duty to retain (rather than a duty to preserve or enhance the value of the trust asset). This allows the settlor and directors the ability to utilise their skills to manage the trust asset, whilst also affording protection to trustees.

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Reservation of powers in other jurisdictions

The position in other jurisdictions, including England and Wales, is different. English law affords settlors the opportunity to retain some control (for example, the ability of settlors to retain a power of appointment), but the settlor's ability to retain control is more limited, as has been seen in recent case law.[4]

JSC Mezhdunarodniy Promyshlenniy Bank v Pugachev & ors

The English High Court decision of *JSC Mezhdunarodniy Promyshlenniy Bank v Pugachev &* ors [2017][5] was a high profile decision which has been publicised at length on this topic and may make it easier for discretionary trusts to be unwound where the settlor retains control over the trust assets. In that case, Mr Pugachev retained the role of undisclosed settlor, beneficiary and protector of five discretionary trusts which gave him extensive powers over the trust assets. It was held that Mr Pugachev set up the discretionary trusts with the intention of retaining control over the assets whilst misleading third parties by hiding his control. It was therefore ultimately determined that the trusts could be attacked for the benefit of Mr Pugachev's creditors.

Webb v Web

The decision of the Privy Council in *Webb v Web* [2020][6] provides further insight into risks settlors may face in certain jurisdictions when retaining control. This was an appeal to the Privy Council from the Court of Appeal of the Cook Islands in relation to a dispute between a husband and wife about the division of matrimonial property.

The husband, Mr Webb, arranged and established two trusts: the Arorangi Trust and the Webb Family Trust (the **Trusts**). Mrs Webb argued, amongst other things, that the Trusts were shams and the settlors never intended to relinquish control over the beneficial interest in the assets which were subject of the Trusts. Mr Webb denied this to be the case.

In relation to the Arorangi Trust, Mr Webb retained extensive powers, including the power to nominate himself as sole beneficiary in place of existing beneficiaries, and therefore had the power to become settlor, trustee, consultant (who, amongst other things, was to assist the trustee on all matters relating to the trust's investment and who had the discretion to remove the trustee and appoint a replacement) and the sole beneficiary.

Mr Webb was not the purported settlor of the Webb Family Trust, although the Court found that this was immaterial and it was considered the named settlor (Mr Ellison) acted as Mr Webb's nominee and under his direction. Mr Webb was expressed to be trustee, consultant and a beneficiary of the Webb Family Trust.

The Trusts were held to be ineffective. The Court found that "*the trust deeds failed to record an effective alienation by Mr Webb of any of the trust property. The bundle of rights which he retained is indistinguishable from ownership*."[7]

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Conclusion

This is an area which continues to develop. If you would like to discuss matters arising out of this update, please contact a member of our Private Client and Corporate Disputes team.

This article is intended to provide a general update in respect of the reservation of powers of the settlor in trusts in the the BVI. It does not constitute legal advice and if you are considering creating a BVI trust, or if you are involved in a dispute in relation to a BVI trust, then please contact a member of our team who would be happy to assist.

References

[1] Hague Convention on the Law Applicable to Trusts and on their Recognition, Chapter 1, Article 2

[2] Trustee (Amendment) Act 2021, section 86(2)

[3] Trustee (Amendment) Act 2021, section 86(1)

[4] We are unable to opine on matters of English law and appropriate advice from English qualified lawyers should be sought

[5] *JSC Mezhdunarodniy Promyshlenniy Bank v Pugachev & ors* [2017] EWHC 2426 (Ch)

[6] *Webb v Webb* [2020] UKPC 22

[7] *Webb v Webb* [2020] UKPC 22, at paragraph 89

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