In The Supreme Court of Bermuda

CIVIL JURISDICTION

2019: No. 085 & 086

IN THE MATTER OF A TRUST ESTABLISHED BY A DECLARATION OF TRUST DATED 14 JANUARY 2000 AND KNOWN AS THE FA TRUST

IN THE MATTER OF A TRUST ESTABLISHED BY A DECLARATION OF TRUST DATED 14 JANUARY 2000 AND KNOWN AS THE FB TRUST

Before:	**Hon. Chief Justice Hargun**
Appearances:	**Mr Keith Robinson, Carey Olsen Bermuda Limited, for the Plaintiff** **Mr Steven White and Ms Hannah Tildesley, Appleby (Bermuda) Limited, for the Defendants**
Date of Hearing:	**2 October 2019**
Date of Ruling:	**7 November 2019**

RULING

Application to remove the Protector; construction of an express provision granting the Protector all costs and expenses on a contemporaneous basis; whether Protector entitled to costs prior to trial of action.

Introduction

1. These are consolidated proceedings in relation to the FA Trust and the FB Trust ("the Trusts"). Both trusts are materially identical in terms of trust provisions and the relevant facts for the purposes of the application before the Court. The present application relates to the issue whether the trustee (the "Trustee") is obliged to indemnify the First Defendant, the protector of the Trusts ("the Protector"), in respect of his costs and expenses of these proceedings and to do so on a contemporaneous basis. This application made by the Protector is made by Summons dated 7 May 2019.

Background

2. The Trusts were established by Declarations of Trust dated 14 January 2000, made by Bermuda Trust Company Limited ("BTCL") and the First Defendant as the "Original Trustee". The First Defendant was also named as the Protector of Trusts. The Trusts were established upon the division into two halves of an earlier trust of which BTCL was a trustee and known as the F Trust. The First Defendant retired as trustee leaving only BTCL as the trustee of the Trusts. By deed dated 8 April 2016, the Plaintiff was appointed as the Trustee of the Trusts.

3. The Trusts are irrevocable and governed by Bermuda law. The Trusts are in a discretionary trust form with clause 3 providing an overriding power of appointment for any member of the "Specified Class". Clause 4 provides that in default of and subject to any appointment under clause 3, the Trustee has broad discretion to benefit any member of the Specified Class.

4. The Trustee's powers in clause 3 and 4 are each subject to the consent of the Protector. There are a number of other powers and functions of the Trustee which can only be exercised either in consultation with or the prior approval of the Protector. The Trustee is required to consult with the Protector prior to making

investments under the Trustee's broad investment powers under clause 6(a). The Protector has the power to veto Trustee's exercise of its powers to exclude or add persons as members of the Specified Class. The Protector has the power to veto the Trustee's entry into contracts, mortgages, charges or undertakings in connection with the Trustee's exercise of its power to borrow on the security of the Trust fund. The Protector has the power to direct the Trustee, vary, and or exclude powers of an administrative or management nature. The Protector has the power to appoint and remove trustees. The Protector has the power to declare (1) a change of the proper law of the Trust; (2) that the courts of such proper law shall thereafter the forum for the administration of the Trust; and (3) in conjunction with the above declaration, that the Perpetuity Period shall thereafter endure for such lesser period as the Protector may determine.

5. Clause 18 of the Trust deals with Protectorship and provides:

> *"(1) The Protector shall have the power to appoint a successor protector by written instrument delivered to the Trustees and to the successor named therein and such appointment shall take effect on the date of receipt by the Trustees of confirmation in writing from the successor of his acceptance of such appointment or such later date as may be specified therein.*
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> *(2) If at any time there shall be no Protector of the trusts hereof or no effective appointment has been made as aforesaid then the power of appointing a Protector shall vest solely in the Trustees and after such an appointment should have been made the provisions of sub-clause (1) of this Clause shall again have the effect but so that should there be no Protector appointed by the Trustees all powers exercisable by the Protector shall be treated as if these were vested solely in the Trustee.*

(3) The Protector shall be wholly indemnified and held harmless out of the Trust Fund from any losses damages judgment debt or expenses, including attorney's fees, which shall be paid on a contemporaneous basis."

6. I should note that it is in fact an issue in these proceedings whether the First Defendant continues to be the Protector of the Trusts. This is so because by a letter dated 24 July 2009 and addressed to BTCL, the First Defendant exercised the power pursuant to Clause 18(1) to appoint the Second Defendant as his Successor Protector. The Second Defendant is the First Defendant's wife, and the two Defendants are in practice together as attorneys.

7. In accordance with Clause 18(1), the appointment as Successor Protector was to take effect on the date of the receipt by BTCL of written confirmation from the Second Defendant that she accepted the Successor Protector. The Second Defendant duly provided such confirmation of the letter dated 24 July 2009.

8. However, by further deed dated 8 April 2016, the present Trustee was appointed as trustee of Trust in place of BTCL. The following month, the First Defendant purported to revoke his prior appointment of the Second Defendant as Successor Protector and instead to make the Second Defendant's appointment effective only "*at such time as [the First Defendant] shall die in office or resign as Protector"*. The Trustee contends that there is doubt whether or not the First Defendant remains the Protector or whether the Second Defendant is in fact the Protector. This issue will have to be resolved by the Court in due course but for purposes of this application, I will assume that the First Defendant remains the duly appointed Protector.

9. The factual background to the underlying dispute is that historically, trustee-beneficiary communication has only been conducted indirectly, using the First Defendant as a conduit. The present Trustee took the view, on legal advice, that it

would be sensible to have a direct line of communication with the two named beneficiaries who remain alive. During the course of providing this advice, the Trustee's legal advisers became aware that on 15 January 2019, the First Defendant had been "Publicly Censured" (a term of art) by the Attorney Grievance Committee for the First Judicial Department of New York State because he had counselled the client to engage in conduct he knew was illegal or fraudulent and suggested that lawyers in the United States can act with impunity.

10. The First Defendant failed to disclose the fact of the disciplinary proceedings against him or its outcome to the Trustee or the beneficiaries. On 16 March 2018, First Defendant completed a "Personal Declaration and Self Certification" form at the Trustee's request for regulatory compliance purposes. In the form, the First Defendant confirmed that he "had never been subject of a judicial or other official enquiry".

11. In light of these issues, the Trustee informed the First Defendant that it considered that his resignation as Protector would be appropriate in the circumstances. When this position was conveyed to the First Defendant during a telephone call on 26 February 2019, the First Defendant responded that he would instead remove the Plaintiff as the trustee. The First Defendant reiterated his intention to replace the Trustee "with all deliberate speed" in an email sent the following day.

12. It is in these circumstances that the Trustee has commenced these proceedings seeking the removal of the Protector on grounds of misconduct and the Protector has made the present application that the Court order the Trustee to indemnify the First Defendant respect of his legal costs of the removal proceedings on a contemporaneous basis pursuant to Clause 18(3).

The rival contentions

13. Counsel for the Protector recognises that a protector exercising fiduciary powers will generally be able to avail himself the benefit of an *implied indemnity* in like terms as a trustee and as such will have an implied right to be indemnified against the costs and expenses reasonably incurred in the course of his duties (see *Trust Protectors, Andrew Holden* at 7.32 (Jordans, 2011)). However, Counsel argues, that these principles have no application where there is an express indemnity in the trust deed. The scope of indemnity, Counsel argues, will be a matter of construction and relies upon *Bogg & Ors v Raper* (1998) 1 ITELR 267 and in particular the judgment of Millett LJ, at para 30:

> *"[In the case of will or settlement…]. The document is the unilateral work of the testator or settlor through whom beneficiaries claim. There is no inherent improbability that he should intend to absolve his executors or trustees from liability from the consequences of their negligence. They accept the office on the terms of the document for which they are not responsible, and are entitled to have the document fairly construed according to natural meaning of the words used"*

14. Accordingly, Counsel for the Protector argues, the usual contractual principles surrounding exemption and indemnity clauses do not apply, as the trust instrument is (i) not individually negotiated, (ii) there is "*no inherent improbability*" that a settlor should "… *intend to absolve his executors or trustees from liability*" and (iii) trustees/protectors "*accept office on the terms of* the *document for which they are not responsible*"; as such, the words used in the trust deed should be "*fairly construed according to [their] natural meaning*" and, further to that, the trustee/protector is "*entitled*" to have the words so construed.

15. Adopting this approach, it is said on behalf of the Protector, Clause 18(3) provides a broad and mandatory entitlement to indemnification out of the Trust funds,

payable on a contemporaneous basis. In particular, Counsel for the Protector rejects the submission that Clause 18(3) only responds if the costs and expenses are properly and reasonably incurred both in terms of entitlement and in terms of quantum. Counsel argues that to assert that the indemnity can only be relied where the Protector has a strong case on the merits, and to defer the issue of entitlement to indemnification until the end of the case, is both an extraordinary limiting clause and also defeats the settlor's clear purpose in providing the Protector with a full indemnity.

16. Counsel for the Trustee submits that the entitlement of a Protector to litigation costs is no different than the rights of indemnity of a trustee to such costs. A trustee's right of indemnity is very often expressed as a positive entitlement in express terms in the trust deed just as Clause 18(3) expresses the entitlement Protector of the Trust.

17. However, Counsel for the Trustee argues, the express terms Clause 18(3) are restricted by the requirement that all costs and expenses sought to be visited upon the Trust Fund be properly incurred, a question that can only be determined when the substantive removal application is heard and determined. Counsel argues that Clause 18(3) does not give the Protector the right to litigate at the expense of the Trust Fund in circumstances where pursuit of such litigation would be considered unreasonable by a court.

Discussion

18. The issue of an indemnity provided by an express term of a trust deed is considered in *Lewin on Trusts* , 19th ed, at 27-116:

> :…*The extent to which the terms of the trust may enhance the trustees' right of indemnity, for example by conferring a right of indemnity in respect of the defence, whether or not successful, of claims in respect of*

non- fraudulent breaches of trust, or claims in respect of other non-fraudulent acts or omissions of the trustees, is not clear. Given that the trust may contain an exemption so as to exclude a trustee's personal liability except for his own fraud, it is difficult to see why a trust should not contain a provision allowing a trustee costs in respect of non-fraudulent acts or omissions, though questions of public policy arise in relation to provisions which purport to allow costs unreasonably incurred or unreasonable in amount….Terms of the trust entitling the trustee to indemnity in respect of costs incurred by him will be construed so as to cover only costs which are reasonably properly incurred and so do not operate to enhance the trustee's rights of indemnity under the general law".

19. The above passage in *Lewin* supports the contention that express clause in a trust deed providing for indemnity for legal costs incurred by a trustee are subject to the overriding requirement that such costs are reasonably or properly incurred both as a matter of entitlement and as a matter of quantum. In support of the legal proposition contained in the last sentence of paragraph 27-116 above, *Lewin* cites the cases of *Holding and Management Ltd v Property Holding and Investment Trust PLC* [1989] 1 WLR 1313 at 1325, CA; and *Gomba Holdings (U.K.) Ltd v Minories Finance Ltd and Others (No.2)* [1993] Ch 171.

20. In *Holding and Management*, the trustee of the maintenance fund commenced proceedings in a manner hostile to the tenants, to whom alone, together with the landlord the trustee owed a fiduciary duty, to ratify proposed expenditure for which the tenants, would have to pay by way of increased maintenance contributions but to which they were opposed and which the landlord did not support. The Court of Appeal held that the costs incurred had been improperly incurred so that the trustee was not entitled to reimbursement either under the statute or under the express clause of the lease providing an indemnity. Nicholls

LJ dealt with the claim for indemnity under the statute and under an express clause at 1324F as follows:

> *"… To be entitled to an indemnity [under section 30 (2) of the Trustee Act 1925] the costs and expenses in question must have been properly incurred by the trustee. This is axiomatic, but if authority is needed it can be found in Turner v Hancock (1882) 20 Ch. D. 303, 305, where Sir George Jessel M.R. refers to the trustees' right to receive out of the trust fund "all the proper costs incident to the execute the trust". In the present case the plaintiff did not bring proceedings to protect the maintenance for the benefit of the beneficiaries. The beneficiaries of the fund, as I have sought to indicate, are the tenants plus the landlord. The proceedings were brought against the tenants to establish whether they were obliged to enlarge the fund to be applied for the benefit beyond what they and the landlord wished. I do not think that the costs incurred were properly incurred. So long as a trust continues, beneficiaries may not control the trustee in the exercise of his powers: In re Brockbank [1948] Ch. 206. But that is a far cry from saying that if the trustee incurs costs without regard to the wishes of the beneficiaries, he will always be entitled an indemnity out of the trust fund.*
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> *Mr Price also sought to rely on paragraph 9 of schedule 5 to the leases. Under this paragraph one of the purposes for which the maintenance fund is applied is:" to make provision for the payment of legal costs incurred by the maintenance trustee…(a)… in the enforcement of the covenants… contained in the leases granted of the flats in the building.."*
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> *I can deal with this very shortly. Read fairly, this paragraph embraces reasonably or properly incurred by the plaintiff in the enforcement of the covenants. I have already indicated by the costs were not reasonably or properly incurred in this case"*

21. The above passage in *Holding and Management* case supports the view that, as a matter of construction and indemnity clause in a trust deed, a court is likely to read into that clause that an entitlement to an indemnity is dependent upon the litigation costs having been incurred reasonably or properly.

22. This view is supported by the observations of the Court of Appeal in *Gomba Holdings*. In that case by clause 2 of the mortgage deed, the mortgagor guaranteed to pay the bank on demand: *"(c) All costs charges and expenses howsoever incurred by the Bank or any Receiver under or in relation to this mortgage….. on a full indemnity basis including (but without prejudice to the generality of the foregoing) all costs charges and expenses which the Bank or any Receiver may incur in enforcing this security….."*

23. In considering the scope of this express term providing indemnity to the bank the Court of Appeal construed clause 2(c) as only responding where the costs had been reasonably incurred and were reasonable in amount. Scott LJ dealing with the proper construction of this clause said at 186C:

> *"Clause 2(1)(c), Clause 7 and Clause 8 of the 18th February 1985 mortgage deed have already been set out. The question is whether, on their true construction, these clauses entitle the Defendants to retain out of the fund that now represents the mortgaged property costs charges or expenses which have been reasonably incurred or which are unreasonable in amount.*
>
> *In our judgment, treating the question simply as one of construction, they clearly do not. It would appear from the judgment of Vinelott J that this opinion is one which corresponds with his own. At page 14 of the transcript the learned judge said that "No doubt the Court can disallow……costs, charges and expenses which are wholly unreasonable in amount." At page 16 he expressed the opinion that the 1st Defendant would be in breach of its duty to the Plaintiffs "if it were to agree to pay*

remuneration to the receiver which was plainly excessive". Indeed the contrary seems to us almost unarguable. The reference in Clause 2(1)(c) to "all costs charges and expenses however incurred…." cannot, in our opinion, be read as "all costs charges and expenses, whether or not unreasonably incurred….."'"

24. Scott LJ also dealt with the suggestion that the mortgagee or the trustee might be entitled to recover legal costs under the express clause providing for indemnity even if those costs were improperly and unreasonably incurred. He said at 187H:

> *"We would only add this. It is difficult to contemplate that a mortgage deed would ever be construed as entitling a mortgagee to charge against the mortgaged property, or to require the mortgagor to pay, all costs charges and expenses even if properly or unreasonably incurred or improper or unreasonable in amount unless the mortgage deed had expressly in terms so provided. But if a mortgage deed did expressly so provide, the enforceability of such a provision would, in our opinion, be open to serious question on public policy grounds. However, we do not think any of the security documents in the present case should be so construed."*

25. The approach illustrated by the English cases is supported by the Manx case of *IFG International Trust Company v French* [2012] Manx LR 637, where the issue faced by the court was whether a protector who had retired was entitled to indemnity in respect of certain proceedings commenced against him in the United States by the US Securities and Exchange Commission ("the SEC"), alleging, inter alia, that the trust had been used as the apparatus of an alleged fraud and that the protector had aided and abetted an alleged fraudulent scheme. The trust deed contained in a clause which provided that "*Each person occupying the office of Protector shall be entitled to exoneration and an indemnity out of the Trust Fund for any liability loss or expense incurred hereunder and for any judgment recovered against and paid for such person other than liability loss expense or judgment arising out of his own wilful and individual dishonesty."* The proper

approach for the court to take in the circumstances is set out in the judgment of Deemster Corlett at [87],[88]:

> *"[87] The principle that where reasonably well founded allegations of personal fraud are made against a trustee a decision as to whether the trustee should be indemnified out of trust funds should properly await the outcome of the proceedings seems to me to be particularly apposite to the case of Mr French. Certainly in my view the trustees cannot be criticised for adopting a stance based on this principle.*
>
> *[88] In this case it seems to me that until the outcome of the SEC complaint is known, the trustees cannot determine whether there has been any "disqualifying wrongdoing" by Mr French such that he is entitled to an indemnity"*

26. These authorities in my judgment provide ample support for the proposition that an express provision in a trust deed providing for an indemnity in favour of a protector in respect of litigation costs must be construed as providing for an indemnity for litigation costs which are properly and reasonably incurred both in relation to entitlement under the clause and in relation to the quantum of such costs. In my judgment Clause 18(3) must be construed subject to this general qualification.

27. Cases such as *Turner v Hancock* (1882) 20 Ch.D. 303 and *Holding and Management* show that a trustee may be deprived of the benefit of an express indemnity provision on the grounds of unreasonableness or misconduct.

28. In certain cases where there are allegations against protector, it may well be that the court can only determine the protector's entitlement to indemnity for litigation costs after the litigation has been concluded. This was the course adopted by Deemster Corlett in the Manx case of *IFG International v French.*

29. In the present case, there are allegations of alleged misconduct on the part of the Protector which the Trustee asserts warrant his removal as a protector. The validity of these allegations can only be determined after the conclusion of the underlying litigation. Furthermore, the removal application made by the Trustee is supported by both beneficiaries who are alive . No doubt the Court will be asked to consider whether the Protector's opposition to his removal in the circumstances is reasonable. It follows therefore that the Protector's entitlement to be indemnified under Clause 18(3) is dependent upon the findings made by this Court following the trial of the underlying proceedings.

30. In my judgment the provision in Clause 18(3) requiring that legal costs "*shall be paid on a contemporaneous basis"* is only applicable in cases where there is no credible allegation of factual circumstances or misconduct on the part of Protector which may disqualify the Protector from making a claim under this provision.

31. In the circumstances, I refuse to make an order sought at this stage that the Trustee be required to indemnify the Protector in respect of the litigation costs incurred by the Protector in these proceedings and that these costs be paid contemporaneously pursuant to Clause 18(3).

32. I will hear the parties in relation to the issue of costs and in relation to further directions relating to the underlying proceedings, if required.

Dated 7th November 2019

NARINDER K HARGUN

CHIEF JUSTICE