

## TRUST PROTECTOR

In recent years, the concept of trust protector has enjoyed phenomenal success in the offshore jurisdictions. This article analyses the different conceptions of the office of trust protector from the perspectives of different jurisdictions, before delving into the nature and extent of the duties owed by trust protector, and the extent of the courts' control over trust protector. This article also touches upon the serious concerns about the use of trust protector, explores its operation and relationship with the traditional parties in a trust, before arguing for a cautious approach towards admitting the concept of trust protector into onshore jurisdictions via statutory means.

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### I. Trust protector – Its function and attractions

1 The concept of trust protector<sup>1</sup> has enjoyed phenomenal success in the offshore jurisdictions.<sup>2</sup> Not too long ago, there had been no granting of such powers of beneficiary appointment or administrative powers upon non-trustees, to anywhere near the extent currently employed in offshore trusts.<sup>3</sup>

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1 There is no statutory definition of trust protector in English law. Trust protector can be defined as a person who, other than the trustee, is the holder of an office created by the terms of the trust, and is authorised or required to play a part in the administration of the trust. See Anthony Duckworth, "Protectors – Fish or Fowl? Part 1" (1996) 3 PCB 169 at 169. See also Donovan W M Waters, "The Protector: New Wine in Old Bottles?" *Trends in Contemporary Trust Law* (1996) at 63; Alexander A Bove, Jr Esq and Melissa Langa Esq, "Peter Protector in Trust Neverland: The Real Story of the Trust Protector" <<http://www.bovelaw.com/archive/Real%20Story%20Trust%20Protector.pdf>> (accessed 22 July 2007) at p 1.

2 See, eg, Waters, "The Protector: New Wine in Old Bottles?" *Trends in Contemporary Trust Law* (1996) at 71.

3 See, eg, Waters, "The Protector: New Wine in Old Bottles?" *Trends in Contemporary Trust Law* (1996) at 71.

2 The office of trust protector<sup>4</sup> was first developed<sup>5</sup> to enable settlors of offshore asset protection trusts to maximise their control over assets transferred to trusts, while still immunising them from the reach of creditors. But today it is no longer confined to the asset protection context.<sup>6</sup>

3 Increasingly, estate planners are using the office of trust protector as an important device that not only adds critical flexibility to long-term trusts, but also increases the settlor's ability to control the trustees' behaviour long after the settlor has passed away or has become incapable of directing the trustees.<sup>7</sup> There are an increasing number of cases in which supernumerary powers<sup>8</sup> are not merely add-on features to make a structure more secure and satisfactory. Instead, they constitute a critical mechanism that a settlor aims to have for a trust.<sup>9</sup>

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4 The phenomenon of trust protector is a rather recent subject, only making its first appearance in the 15th edition of *Underhill and Hayton: Underhill and Hayton Law of Trusts and Trustees* (Butterworths LexisNexis London, 15th Ed, 1995) at pp 23–5. “Protector” as a term in property law could be traced to its use in the English Fines and Recoveries Act 1833, in relation to entails: Fines and Recoveries Act 1833 (UK) s 36; Kenelm E Digby, *An Introduction to the History of the Law of Real Property* 255 (5th Ed, 1897). Although that area of law has since become obsolete, this terminology has survived into the modern law of trusts. The use of the trust protector is also not a new event – some English trusts have long used protectors to reassure settlors uneasy about the powers conferred on trustees even before the last two decades: Duckworth, “Protectors – Fish or Fowl? Part 1” (1996) 3 PCB 169 at 173.

5 From the problem-solving creativity of lawyers; see Stewart E Sterk, “Trust Protectors, Agency Costs, and Fiduciary Duty” (2006) 27 *Cardozo L Rev* 2761 at 2764.

6 Gregory S Alexander, “Trust Protectors: Who Will Watch the Watchmen?” (2006) 27 *Cardozo L Rev* 2807 at 2807.

7 Gregory S Alexander, “Trust Protectors: Who Will Watch the Watchmen?” (2006) 27 *Cardozo L Rev* 2807 at 2807.

8 Supernumeraries are “non-trustees” and that “supernumerary powers” are “powers [given] to outsiders (*ie*, supernumeraries who are neither the settlor nor a beneficiary)”: Duckworth, “Protectors and Other Supernumeraries: Part 1” (2006) 20(3) *Tru LI* 180 at 180. See also “supernumerary powers” as a generic label for “powers of one sort or another [that] are given to persons who are neither the settlor nor the trustee”: Duckworth, “The International Trust Part II: The Trust Offshore” 32 *VNJTL* 879 at 919.

9 Duckworth, “Protectors and Other Supernumeraries: Part 1” (2006) 20(3) *Tru LI* 180 at 184.

4 Since the early days in the development of supernumerary powers, there has been greater involvement of outsiders and much more varied and extensive use of powers with regard to investment and management. This is not simply a case of devising more efficient and reliable management arrangements. Instead, it is due to the fact that attitudes to the disposition of wealth, and the resultant use of trusts for that purpose, have been changing.<sup>10</sup>

5 Many have considered the office of trust protector to be an essential component of the operation of offshore trusts, one that provides the settlor and the beneficiaries a level of protection which was previously absent. The protector's ability to check the powers of trustees without compromising the tax status of the offshore trust – one of the main reasons why offshore trusts are set up in the first place – makes it even more appealing to settlors in offshore trusts.

6 The development of supernumerary powers – such as that of trust protector in offshore jurisdictions – has often been attributed to a lack of confidence in a distant trust company, or a distant jurisdiction. This is an oversimplification. The difference – between the levels of confidence reposed in an offshore unit of a major international bank and that in an onshore unit of the same bank – is negligible at best.

7 The development of the office of trust protector can be seen as a response to the difficulties and worries faced by settlors of offshore trusts. There are the obvious difficulties and problems in following the traditional English practice of adding trustees in the circumstances of many offshore trusts.

8 For the dual reasons of tax and confidentiality, the settlor would want to alienate ownership and control of part or all of his estate immediately so as to ensure that he has no interest under the settlement.<sup>11</sup> However, at the same time, the settlor also wants to make his estate available for other members of his family or other nominated beneficiaries over what might be a substantial period.

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10 Duckworth, "Protectors and Other Supernumeraries: Part 1" (2006) 20(3) Tru LI 180 at 184.

11 Howard Rosen, "The Protectors – The Role of this Little Known Breed with Particular Reference to the Operation of Offshore Trusts" (1993) LSG 90.27(19) at p 1.

9 Adding on to this original concern is the fact that trust agreements often deliberately grant trustees a wide range of powers with regard to the trust funds so as to enable the trustees to be responsive to any unforeseen circumstances.<sup>12</sup> The result is that the settlor ends up having to deal with a situation where the trustees are either geographically distant or possibly unknown. On the ground, settlors of offshore trusts by and large are from jurisdictions that are neither familiar nor comfortable with the idea of handing over complete or exclusive control to others.<sup>13</sup>

10 The settlor may be cut off from his original estate, and left with no say in either the conduct of the trustees or the distribution of the trust assets. The use of a letter of wishes to hopefully influence the conduct of the trustees is of no help to the settlor as it is not legally binding, negating its ability to proffer a solution to the problem faced by the settlor.<sup>14</sup>

11 Trust protectors are rarely found in onshore trusts as settlors are usually able to retain a comfortable level of control over the exercise of the trustees' powers. This can be done either by the settlor acting as a trustee himself or getting a family member or close relative to do so.<sup>15</sup> This solution is mostly unavailable to settlors in the case of offshore trusts, which are generally established owing to the tax advantages associated with them.

12 The nature of property settled on offshore trusts may also partially explain the enthusiasm for supernumerary powers, especially the inclusion of assets requiring active management. The placing of management control in family hands, or mixed family/outsider hands, on a suitable basis is, in some cases, the settlor's primary objective.<sup>16</sup> The appointment of a protector gives that extra layer of security to the settlor, to ensure that even after his death the trust will be administered in accordance with his wishes.<sup>17</sup>

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12 Howard Rosen, "The Protectors – The Role of this Little Known Breed with Particular Reference to the Operation of Offshore Trusts" (1993) LSG 90.27(19) at p 1.

13 Duckworth, "Protectors and Other Supernumeraries: Part 1" (2006) 20(3) Tru LI 180 at 184.

14 Gilbert Kodilinye & Trevor A Carmichael, *Commonwealth Caribbean Trusts Law* (Cavenish Publishing Limited, 2nd Ed, 2002) at p 306.

15 Ham, Campbell & Tennet, "Protectors" in *The International Trust* (John Glasson & Geraint Thomas ed) (Jordan Publishing Ltd, 2nd Ed, 2006) at p 226.

16 Duckworth, "Protectors and Other Supernumeraries: Part 1" (2006) 20(3) Tru LI 180 at 184. See also Duckworth, "Protectors – Fish or Fowl? Part 1" (1996) 3 PCB 169 at 172–173.

17 William Norris & Deborah Hartnett, "The Protector's Position – Suggesting Some Basic Principles" (1995) 2 PCB 109 at 110.

13 A trust protector may be authorised to edit or veto information that trustees propose to release. Professional trustees also welcome the protector as one who assumes some of the decision-making duties, relieving part of the trustees' burdens by, for example, interpreting the settlor's letter of wishes on the trustee's behalf and nominating among the beneficiaries those who should receive loans or advancements.<sup>18</sup>

14 Thus protectors in offshore trusts are commonly appointed to provide a level of comfort<sup>19</sup> to settlors who may not be familiar with the appointed trustees or the jurisdictions in which they are resident. Trust protectors give settlors either the critical control or at least a comfortable level of influence over trustee activity.<sup>20</sup>

## II. Trust protector – Different conceptions

### A. *The offshore perspectives*

15 As its advantages became more apparent, the use of protectors became more prevalent. This in turn led to the exercise of codification in a number of offshore jurisdictions. The Cook Islands International Trusts Amendment Act of 1989 represented the first step towards statutory recognition. The Amendment Act has since been incorporated into the International Trusts Act 1984.<sup>21</sup> "Protector" is defined in s 2:<sup>22</sup>

'Protector' in relation to an international trust means a person who is the holder of a power which when invoked is capable of directing a trustee in matters relating to the trust and in respect of which matters the trustee has a discretion and includes a person who is the holder of a power of appointment or dismissal of trustees.

16 This definition appears to be deliberately restrictive. Presumably a consent power would not qualify. Neither would a power to add or remove beneficiaries in a discretionary trust.<sup>23</sup> The phrase "and in respect of which matters the trustee has a discretion" is also perplexing. On the face of the provision, the trustee has no discretion if it is obliged to

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18 Waters, "The Protector: New Wine in Old Bottles?" in *Trends in Contemporary Trust Law* (1996) at 64.

19 Waters, "The Protector: New Wine in Old Bottles?" in *Trends in Contemporary Trust Law* (1996) at 63.

20 Waters, "The Protector: New Wine in Old Bottles?" in *Trends in Contemporary Trust Law* (1996) at 64.

21 See Pt IV of the International Trusts Act 1984 (Act 14 of 1984) for provisions on trust protectors.

22 International Trusts Act 1984, s 2.

23 Duckworth, "Protectors – Fish or Fowl? Part 3" (1996) 5 PCB 328 at 335.

comply with the directions of the protector. The definition also draws attention to the notion of power which clearly identifies the legal position of the trust protector. From this viewpoint, the trust instrument may provide for “the office of the trust protector”. The Cook Islands legislation represents the customary view of the protector.<sup>24</sup> It is also present via implication in earlier laws<sup>25</sup> that were drafted before the office of the trust protector became the huge phenomenon that it is today.<sup>26</sup>

17 Other offshore jurisdictions soon followed the lead of the Cook Islands. In Belize,<sup>27</sup> Anguilla<sup>28</sup> and Nevis<sup>29</sup>, the legislation state that the person appointed to the office of protector shall have certain powers, including the power to remove a trustee, to appoint new or additional trustees and the power to change the proper law of trust. These are in addition to “such powers as are conferred by the terms of the trust” or the provisions of the respective Acts.

18 Among the offshore legislation, the Belize legislation represents the most comprehensive effort. Section 16 deals with the protector’s obligations in the following terms:<sup>30</sup>

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24 Maurizio Lupoi, *Trusts: A Comparative Study* (Cambridge University Press, 1st Ed, 2000) at p 258.

25 As the Cook Islands legislation and earlier laws illustrate, there is nothing extraordinary about the use of trust protector. Indeed, the laws of the last century already permitted the mechanism, as the holder of powers, with means to influence the boundaries of the trustee’s activities. See, eg, s 3 of the Bahamas Trustee Act 1893.

26 For eg, Art 20(3) of the Trusts (Jersey) Law 1984 was adopted in Malta via s 24(3) of the Trusts Act 1988.

27 Section 16(2) of the Trusts Act (Cap 202, 2000 Rev Ed) provides:

The protector shall have the following powers—

- (a) (unless the terms of the trust shall otherwise provide) the power to remove a trustee and to appoint a new or additional trustee;
- (b) such further powers as are conferred on the protector by the terms of the trust or of this Act.

28 Section 15(2) of the Trusts Act (Cap T70, 2000 Rev Ed) provides:

The protector has the following powers—

- (a) unless the terms of the trust shall otherwise provide, the power to remove a trustee and to appoint a new or additional trustee;
- (b) the power to enforce the trust;
- (c) such further powers as are conferred on the protector by the terms of the trust or the provisions of this Act.

29 Section 9(2) of the International Exempt Trust Ordinance 1994 provides:

The protector shall have the following powers—

- (a) (unless the terms of the trust shall otherwise provide) the power to remove a trustee and appoint a new or additional trustee;
- (b) such further powers as are conferred on the protector by the terms of the trust or by this Ordinance.

30 Trusts Act (Cap 202, 2000 Rev Ed), s 16(4)–(5).

(4) In the exercise of his office, the protector shall not be accounted or regarded as a trustee.

(5) Subject to the terms of the trust, in the exercise of his office a protector shall owe a fiduciary duty to the beneficiaries of the trust or to the purpose for which the trust is created.

Subsection (4) appears to state the obvious. Subsection (5) appears to be entirely appropriate if it seeks to establish that it is the norm that a protector has a service obligation. Not only does s 58 of the Belize legislation<sup>31</sup> establish that a protector has the necessary standing to enforce a trust, it also appears to say that the court may appoint a

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31 Section 58 of the Trusts Act (Cap 202, 2000 Rev Ed) provides:

(1) On the application of a trustee, a beneficiary, a settlor or his personal representatives, a protector, (in the case of a trust established for a charitable purpose) the Attorney-General or, with the leave of the Court, any other person, the Court may—

- (a) make an order in respect of—
  - (i) the execution, administration or enforcement of a trust;
  - (ii) a trustee, including an order as to the exercise by a trustee of his functions, the removal of a trustee, the appointment, remuneration or conduct of a trustee, the keeping and submission of accounts, and the making of payments, whether into Court or otherwise;
  - (iii) a protector, including an order appointing a protector;
  - (iv) a beneficiary, or any person connected with a trust;
  - (v) any trust property, including an order as to the vesting, preservation, application, surrender or recovery thereof;
- (b) make a declaration as to the validity or enforceability of a trust;
- (c) direct the trustee to distribute, or not to distribute, the trust property;
- (d) make such order in respect of the termination of the trust and the distribution of the property as it thinks fit;
- (e) rescind or vary an order or declaration under this Act, or make a new or further order or declaration.

(2) Where the Court appoints or removes a trustee under this section

- (a) it may impose such requirements and conditions as it thinks fit, including provisions as to remuneration and requirements or conditions as to the vesting of trust property;
- (b) subject to the Court's order, a trustee appointed by the Court has the same functions, and may act in all respects, as if he had been originally appointed a trustee.

(3) If a person does not comply with an order of the Court under this Act requiring him to do any thing, the Court may, on such terms and conditions as it thinks fit, order that the thing be done by another person, nominated for the purpose by the Court, at the expense of the person in default (or otherwise, as the Court directs) and a thing so done has effect in all respects as if done by the person in default.

protector, but not remove one. Presumably in so doing, the court may establish the powers, obligations and rights of the protector, though perhaps what the legislative draftsman had uppermost in mind was the appointment by the court of a person to fill a vacancy in a case where the trust instrument already established the office of protector and prescribed its powers, obligations and rights.

19 The legislation in the British Virgin Islands<sup>32</sup> and the Bahamas<sup>33</sup> produce a rather similar effect, although they are worded differently. Section 81(2) of the Bahamian Trustee Act 1998 states:

The trust instrument may confer on the settlor or on any protectors any powers including (without limitation) power to do any one or more of the following:

- (a) determine the law of which jurisdiction shall be the proper law of the trust;
- (b) change the forum of administration of the trust;
- (c) remove trustees;
- (d) appoint new or additional trustees;
- (e) exclude any beneficiary as a beneficiary of the trust;
- (f) add any person (including the settlor and any private or charitable trust or foundation) as a beneficiary of the trust in addition to any existing beneficiary of the trust;
- (g) give or withhold consent to specified actions of the trustee either conditionally or unconditionally; and
- (h) release any of the protectors' powers.

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32 Section 86(2) of the Trustee Ordinance 1961 (as amended) provides:

There may be conferred on the settlor or some other person, whether named as protector, nominator, committee or by any other name, by the instrument creating the trust, any powers, and without limitation to the foregoing power may be conferred on that person to do any one or more of the following:

- (a) determine the law of which jurisdiction shall be the proper law of the trust;
- (b) change the forum of administration of the trust;
- (c) remove trustees;
- (d) appoint new or additional trustees;
- (e) exclude any beneficiary as a beneficiary of the trust;
- (f) include any person as a beneficiary of the trust in addition to any existing beneficiary of the trust; and
- (g) withhold consent from specified actions of the trustees either conditionally or unconditionally.

33 Trustee Act 1998 (Cap 176), s 81(2).



20 The trust instrument may contain provisions by which the exercise by the trustees of their powers and discretions shall be subject to the previous consent of the settlor or some other persons, whether named as protector or another person. If the trust instrument so provides, the trustees shall not be liable for any loss caused by their actions if the previous consent was given. However, it should be noted that the Bahamian Trustee Act states a further requirement that the trustees must act in good faith.<sup>34</sup>

A trust instrument may contain provisions by virtue of which the exercise by the trustees of any of their powers and discretions shall be subject to the previous consent of the settlor or of some other person as protector, and if so provided in the trust instrument the trustees shall not be liable for any loss caused by their actions if the previous consent was given and they acted in *good faith*. [emphasis added]

21 Although all of the legislation mentioned above state that a protector shall not, in the exercise of his office, be deemed to be a trustee, the statutes otherwise embrace significantly different conceptions of trust protector.<sup>35</sup> The legislation in British Virgin Islands states:<sup>36</sup>

An instrument creating a trust may contain provisions by virtue of which the exercise by the trustees of any of their powers and discretions shall be subject to the previous consent of the settlor or some other person, whether named as protector, nominator, committee or any other name; and if so provided in the instrument creating the trust the trustees shall not be liable for any loss caused by their actions if the previous consent was given.

22 This person “is not liable to the beneficiaries for the *bona fide* exercise of the power”.<sup>37</sup> The provision embraces a different relationship between the trust protector and the trustees. First, the settlor is identified as a potential protector. Although this is a minority solution, it is not new since the Belize legislation already provides for it.<sup>38</sup> More importantly, it is the relationship between protector and trustee that is influenced by a context absent in other legislation, such as that in Anguilla,<sup>39</sup> Belize,<sup>40</sup>

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34 Trustee Act 1998 (Cap 176), s 81(1).

35 Gilbert Kodilinye & Trevor A Carmichael, *Commonwealth Caribbean Trusts Law* (Cavenish Publishing Limited, 2nd Ed, 2002) at p 308.

36 Trustee Ordinance 1961 (as amended), s 86(1).

37 Trustee Ordinance 1961 (as amended), s 86(3).

38 Section 16(3) of the Trusts Act (Cap 202, 2000 Rev Ed) provides:

The protector of a trust may also be a settlor, a trustee or a beneficiary of the trust.

39 Section 15(5) of the Trusts Act (Cap T70, 2000 Rev Ed) provides:

Subject to the terms of the trust, in the exercise of his office a protector shall owe a fiduciary duty to the beneficiaries of the trust or to the purpose for which the trust is created.

40 Section 16(5) of the Trusts Act (Cap 202, 2000 Rev Ed) provides:

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Nevis<sup>41</sup> and St Vincent,<sup>42</sup> which declare that the trust protector owes a fiduciary duty to the beneficiaries of the trust or the purpose for which a trust is created. In the British Virgin Islands, the assent of the protector has the effect of removing the trustee's responsibilities for their actions, which arguably reverses the role of the trustee, making him in substance an agent.<sup>43</sup>

23 In Barbados, statutory recognition of trust protector exists only in relation to international purpose trusts, where his role is equivalent to that of the "enforcer" mentioned in other jurisdictions:<sup>44</sup>

Notwithstanding any law to the contrary but subject to this section, a *valid international trust* may be created for a non-charitable purpose, if

- (a) The purpose is specific, reasonable and capable of fulfilment;
- (b) The purpose is not immoral, unlawful or contrary to public policy;
- (c) *The terms of the trust provide for the appointment of a protector to enforce the trust and for the appointment of a successor to such a protector;* [emphasis added] and
- (d) The terms of the trust specify the event upon the happening of which the trust terminates and provides for the disposition of surplus assets of the trust upon its termination.

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Subject to the terms of the trust, in the exercise of his office a protector shall owe a fiduciary duty to the beneficiaries of the trust or to the purpose for which the trust is created.

41 Section 9(5) of the International Exempt Trust Ordinance 1994 provides:

Subject to the terms of the international trust, in the exercise of his office a protector shall owe a fiduciary duty to the beneficiaries of the trust or to the purpose for which the trust is created.

42 Section 16(5) of the International Trusts Act 1996 (Act 20 of 1996, Act 39 of 1996) provides:

Subject to the terms of the international trust which may provide to the contrary, in the exercise of his office a protector shall owe a fiduciary duty to the beneficiaries of the trust or to the purpose for which the trust is created.

43 Maurizio Lupoi, *Trusts: A Comparative Study* (Cambridge University Press, 1st Ed, 2000) at p 258.

44 International Trust Act 1995 (Cap 245), s 10(1).

24 The Barbados International Trust Act also provides generally for the office of trust protector in relation to other international trusts.<sup>45</sup> However, it should be noted that s 26(2) of the Barbados International Trust Act appears to fetter the settlor's freedom to determine the number and content of the powers he wants to confer on trust protector.<sup>46</sup> It seems that under the Barbados International Trust Act, although a settlor can confer powers on trust protector, these powers are confined to those stated in s 26(2) of the Act:<sup>47</sup>

*The following or any of them* [powers] may be conferred on the protector by the terms of the trust:

- (a) the power to appoint and remove trustees;
- (b) the power to change the proper law of the trust;
- (c) the right to receive notice in advance of specified actions of the trustees;
- (d) the right to receive information relating to or forming part of the accounts of the trust. [emphasis added]

### **B. The American perspectives**

25 For a major part of the American legal history, there had been no mention of trust protectors. This has since been subject to rapid changes. Over the last nine years, (at least) five American states have enacted statutes explicitly authorising or defining trust protectors. These changes can be seen in South Dakota,<sup>48</sup> Idaho,<sup>49</sup> Alaska<sup>50</sup> and Wyoming.<sup>51</sup> For example, the legislation in Alaska states:<sup>52</sup>

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45 Section 26(1) of the International Trust Act 1995 (Cap 245) provides:

The terms of a trust may provide for the appointment of a protector of the trust whether called protector, guardian, advisor or by whatever name called.

46 Kodilinye & Carmichael, *Commonwealth Caribbean Trusts Law* (Cavendish Publishing Limited, 2nd Ed, 2002) at p 309.

47 International Trust Act 1995 (Cap 245), s 26(2).

48 Section 55-1B-1 of the South Dakota Codified Laws provides:

'Trust protector', any disinterested third party whose appointment is provided for in the instrument.

49 Section 15-7-501(1)(e) of the Idaho Code Ann (2005) provides:

'Trust protector' means any disinterested third party whose appointment is provided for in the trust instrument.

50 Alaska Stat (2005), s 13.36.370.

51 Section 4-10-710(a) of the Wyo Stat Ann (2005) provides:

The powers and discretions of a trust protector shall be provided in the trust instrument or may be established or modified by a judicial order, and may, in the best interests of the trust, be exercised or not exercised. The powers and discretions may include, but are not limited to the following ...

52 Section 13.36.370 of the Alaska Stat (2005).

- (a) A trust instrument may provide for the appointment of a disinterested third party to act as a trust protector.
- (b) A trust protector appointed under (a) of this section has the powers, delegations, and functions conferred on the protector by the trust instrument, which may include the power to
- (1) Remove and appoint a trustee;
  - (2) Modify or amend the trust instrument to achieve favourable tax status or to respond to changes in 26 USC (Internal Revenue Code) or state law, or the rulings and regulations under those laws;
  - (3) Increase or decrease the interests of any beneficiary to the trust; and
  - (4) Modify the terms of a power of appointment granted by the trust.

26 Some American states, such as Idaho, South Dakota and Wyoming also insulate trustees from liability for following the directions given to them by trust protectors.<sup>53</sup> For example, the legislation in Wyoming states:<sup>54</sup>

Unless the trust instrument appointing, designating or providing for a method for appointing a trust protector or trust advisor or the court order appointing a trust protector states otherwise, the excluded fiduciary is not liable for any loss resulting from any action or inaction of the trust advisor or protector.

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53 Section 15-7-501(5) of the Idaho Code Ann provides:

If an instrument appoints a trust protector, the excluded fiduciary is not liable for any loss resulting from any action taken upon such trust protector's direction.

Section 55-1B-5 of the South Dakota Codified Laws provides:

If an instrument appoints a trust protector, the excluded fiduciary is not liable for any loss resulting from any action taken upon such trust protector's direction.

54 Wyo Stat Ann (2005), s 4-10-717.

27 However, unlike the three American states mentioned above, the Alaskan statute contains no comparable provision. The Alaskan statute also differs from the statutes of the other four states, which directs that a protector should be treated as a fiduciary unless the trust instrument provides to the contrary.<sup>55</sup>

28 The Alaskan statute provides the converse:<sup>56</sup>

Subject to the terms of the trust instrument, a trust protector is not liable or accountable as a trustee or fiduciary because of an act or omission of the trust protector taken when performing the function of a trust protector under the trust instrument.

29 The Uniform Trust Code also provides for trust protectors, in a Comment.<sup>57</sup> It provides:<sup>58</sup>

If the terms of a trust confer upon a person other than the settlor of a revocable trust power to direct certain actions of the trustee, the trustee shall act in accordance with an exercise of the power unless the attempted exercise is manifestly contrary to the terms of the trust or the trustee knows the attempted exercise would constitute a serious breach of a fiduciary duty that the person holding the power owes to the beneficiaries of the trust.

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55 Section 15-7-501(4) of the Idaho Code Ann provides:

[W]hen one (1) or more trust advisors are given authority by the terms of a governing instrument to direct, consent to, or disapprove a fiduciary's investment decisions, or proposed investment decisions, such trust advisors shall be considered to be fiduciaries when exercising such authority unless the governing instrument provides otherwise.

Section 4-10-711 of the Wyo Stat Ann (2005) provides:

Trust protectors are fiduciaries to the extent of the powers, duties and discretions granted to them under the terms of the trust instrument.

Section 55-1B-4 of the South Dakota Codified Laws provides:

If one or more trust advisors are given authority by the terms of a governing instrument to direct, consent to, or disapprove a fiduciary's investment decisions, or proposed investment decisions, such trust advisors shall be considered to be fiduciaries when exercising such authority unless the governing instrument provides otherwise.

56 Alaska Stat (2005), s 13.36.370(d).

57 Section 808 cmt of the Unif Trust Code (2005) provides:

Subsections (b)–(d) ratify the use of trust protectors and advisers. Subsections (b) and (d) are based in part on Restatement (Second) of Trusts § 185 (1959). Subsection (c) is similar to Restatement (Third) of Trusts § 64(2) (Tentative Draft No 3, 2001). 'Advisers' have long been used for certain trustee functions, such as the power to direct investments or manage a closely-held business. 'Trust protector', a term largely associated with offshore trust practice, is more recent and usually connotes the grant of greater powers, sometimes including the power to amend or terminate the trust. Subsection (c) ratifies the recent trend to grant third persons such broader powers.

58 Unif Trust Code (2005), s 808(b).

It does not provide trustees with absolute immunity from liability following the directions of a trust protector, but requires that the trustee exercises “minimal oversight responsibility” before following the protector’s directions.<sup>59</sup> It further creates a presumption that the holder of a “power to direct” is a fiduciary.<sup>60</sup>

30 It should be noted, however, that most American states have made no statutory provisions for protectors and have yet to develop case law defining the relationships among settlors, trustees, beneficiaries and protectors. Also, even in the states that have labelled protectors as fiduciaries, the scope of the duties owed by protectors still remains unclear at best.<sup>61</sup>

31 From the different conceptions of the office of trust protector in the different jurisdictions, it can be seen that the nature and extent of the duties owed by the trust protector, and the extent of the courts’ control over the trust protector, vary.

### III. Duties of the trust protector

32 The scope of the duties owed by a trust protector, especially in relation to the powers he holds, has always been a thorny issue. I shall elaborate on the limited case law from the offshore jurisdictions, before referring to the legal principles that could be extrapolated from the onshore jurisdictions to handle the concept of trust protector.

33 The much criticised Bermudan case of *Von Knieriem v Bermuda Trust Co Ltd*<sup>62</sup> held that protector’s power to appoint and remove trustees is a fiduciary power on the basis that protector could not exercise the power for his own benefit, but only for the interests of the beneficiaries. In arriving at this conclusion, the court looked at the wording of the trust deeds and the scheme of the trusts in order to interpret and apply the powers of the protector. Arguably, it was wrong for the court in deciding that in order to determine if a power is fiduciary, one looks only at the wording or limitations in the trust instrument, determining whether a particular power is fiduciary, and one is concerned with case law only if

59 Unif Trust Code (2005), s 808(b).

60 Section 808(d) of the Unif Trust Code (2005) provides:

A person, other than a beneficiary, who holds a power to direct is presumptively a fiduciary who, as such, is required to act in good faith with regard to the purposes of the trust and the interests of the beneficiaries. The holder of a power to direct is liable for any loss that results from breach of a fiduciary duty.

61 For example, there are no specific provisions in the statutes of Wyoming, South Dakota and Idaho stating the exact scope of the duties of the protectors as fiduciaries.

62 *Butterworths Offshore Cases and Materials* vol 1 (1996) at p 116 at p 124, Supreme Court of Bermuda, *per* Meerabux J.

the trust instrument is silent.<sup>63</sup> Neither were the motives of the protector sufficiently analysed in the judgment.<sup>64</sup>

34 It referred to *Rawson Trust v Perlman*<sup>65</sup> and *Re Skeats' Settlement*, in which Kay J in the latter decision considered that a power to appoint new trustees was a fiduciary power and thus could not be exercised by the appointor to appoint himself. The court in *Von Knieriem* distinguished *Rawson Trust* on the basis that the powers of appointment and removal in the Star Trusts were conferred on the protector himself and were not actions of the trustees that were controlled by the protector as they were in *Rawson Trust*.

35 On whether the protector had exercised his powers capriciously, Meerabux J in *Von Knieriem* held that the pension cases such as *Mettoy Pension Trustees v Evans*<sup>66</sup> were irrelevant as they applied only to pension schemes. The judge also held that a person could only avoid an appointment if he could prove a corrupt purpose on the part of the appointer. The mere possibility of an improper motive was insufficient. Thus the court concluded that the powers of appointment and removal had been validly exercised by the protector.

36 The *Von Knieriem* decision is important as it reinforces the view that, in general, protectors owe fiduciary duties to beneficiaries. This is a correct view. The decision also contains a clear statement of the tests to be applied in determining whether a protector owes fiduciary duties in exercising a particular power.

37 Although the standards expected of a protector remain unclear, this decision is of significant guidance to other jurisdictions grappling with the trust protector concept, as it is the first case in the Commonwealth in which there had been a full discussion of such an issue.

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63 See also Andrew Penney, "Rights and Powers of Trust Protectors: *Rahman* Revisited" (1995) 1 J Int'l P 31.

64 See also John Conder, "Some Judicial Guidance on Protectors: The *Star Trusts* Case" (1995) 4 PCB 288 at 290.

65 (25 April 1990) (unreported) Supreme Court of the Bahamas, Smith J, *Butterworths Offshore Cases and Materials* vol 1 (1996) at pp 31–55, esp 51.

66 [1990] 1 WLR 1586 at 1613 *per* Warner J; *Butterworths Offshore Cases and Materials* vol 1 (1996) at p 116 at p 124, Supreme Court of Bermuda, *per* Meerabux J.

38 The case of *Steele v Paz Limited*,<sup>67</sup> which arose in the Isle of Man, concerned the failure of a declaration of trust to nominate a protector, where certain powers of the trustees could only be exercised with the protector's consent. On appeal, the court reversed the judgment of the judge at first instance that the trust was void for uncertainty. The court held that as the protector's powers were fiduciary powers, it had – by analogy with the case of trustees – inherent jurisdiction to appoint a person to exercise these powers. Thus the trust was held valid.

39 In the Bahamas, *Rawson Trust v Perlman*<sup>68</sup> stands for the proposition that a protector's power to consent to the proposed resettlement was not a fiduciary power if the settlement gave the protector the power to further his own interests.

40 The general picture that emerges from the above cases seems to be that trust protectors are in a fiduciary position. They must exercise their powers and functions *bona fide* in the way they consider to be in the interests of the beneficiaries including, in this context, persons whom the settlor may reasonably be expected to have intended to be added to the class. The direct authority for the first part of this is the Bermudan case of *Von Knieriem v Bermuda Trust Co Ltd*,<sup>69</sup> the reasoning and conclusion seem persuasive. There is no authority for the second part; yet it seems inevitable, since the power to add beneficiaries can seldom, if ever, be exercised in the interests of existing ones. It also seems there can seldom, if ever, be a fiduciary duty or obligation without a corresponding right or interest.

41 It is important to clarify the extent of the duties owed by trust protectors so as to prevent trust protectors from becoming “a law unto themselves” – with no one watching over the watchmen. Taken to the extreme, a protector could be left as the principal beneficiary of a trust, as he could agree to exercise his powers in accordance with the preferences of the highest bidder for his services.<sup>70</sup> This is to be avoided. Even if a settlor was prepared to accept such behaviour from the first protector which the settlor had personally chosen, it is unlikely that the settlor would endorse such behaviour from a successor protector.<sup>71</sup>

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67 (10 October 1995) (unreported) CA of Isle of Man, *Butterworths Offshore Cases and Materials* vol 1 (1996) at pp 338–418.

68 (25 April 1990) (unreported) Supreme Court of the Bahamas, Smith J, *Butterworths Offshore Cases and Materials* vol 1 (1996) at pp 31–55.

69 *Butterworths Offshore Cases and Materials* vol 1 (1996) at pp 116 at 124, Supreme Court of Bermuda, *per* Meerabux J.

70 Sterk, “Trust Protectors, Agency Costs, and Fiduciary Duty” (2006) 27 *Cardozo L Rev* 2761 at 2783. See also Duckworth, “Protectors – Fish or Fowl? Part 1” (1996) 3 *PCB* 169 at 178, offering examples of the abuse of power which may follow.

71 Sterk, “Trust Protectors, Agency Costs, and Fiduciary Duty” (2006) 27 *Cardozo L Rev* 2761 at 2783.



42 The answer to this depends on the construction of a particular trust instrument.<sup>72</sup> It is dependent upon the language used, and the surrounding circumstances. The creation or exclusion of duties in relation to the protector's powers, and the nature of those duties, must depend upon the intention of the creator of the power, either expressed or inferred. There seems to be no clear basis for a court to decline to give effect to the intentions of the creator in this respect.<sup>73</sup>

43 There are a few exceptions to that view. The first is when public policy is involved. If it were provided that the trustees required the trust protector's consent before applying to court for directions on any matter,<sup>74</sup> this would be considered against public policy since it purports to oust the jurisdiction of the court. The second is when there is a lack of authority.<sup>75</sup> Such a situation could arise where the creator of the power was not settling his own property, but was himself executing a trust or exercising a power, or purporting to do so; and in creating the power in such terms he breached or exceeded his duty. The third concerns repugnancy – where the intentions of the creator with regard to the protector's duties are inconsistent with the other provisions of the trust instrument or their legal consequences, notably the provisions creating the trust, whose legal consequences include the courts' jurisdiction. This has been described by Lord Walker as “fundamental to the law of trusts”, to “supervise and if appropriate intervene in the administration of trusts”.<sup>76</sup> The last pertains to unenforceability. This applies to situations in which the intended duties of the trust protector are of a kind which the courts cannot, or do not, enforce.

44 A protector's position may also be regulated by statute<sup>77</sup> or public policy – if a protector clause is drafted so as to oust the court's jurisdiction, the offending part of the clause may be struck down on the basis that it is contrary to public policy.<sup>78</sup> Different jurisdictions may provide different answers to this question.

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72 Ham, Campbell & Tennet, “Protectors” in *The International Trust* (John Glasson & Geraint Thomas ed) (Jordan Publishing Ltd, 2nd Ed, 2006) 225 at 225.

73 Duckworth, “Protectors and Other Supernumeraries: Part 2” (2006) 20(4) Tru LI 235 at 235.

74 Duckworth, “Protectors and Other Supernumeraries: Part 2” (2006) 20(4) Tru LI 235 at 235.

75 Duckworth, “Protectors and Other Supernumeraries: Part 2” (2006) 20(4) Tru LI 235 at 235.

76 *Schmidt v Rosewood Trust Limited* [2003] 2 WLR 1442 (PC) at [51] *per* Lord Walker.

77 For example, the Belize Trusts Act 1992 and the Cook Islands International Trusts Amendment Act 1989.

78 See, eg, *Re Wynn* [1952] Ch 271.

45 There are two approaches to the role of protectors. The wider view states that whether a protector is in a fiduciary position should depend on the circumstances.<sup>79</sup> In contrast, the narrow view<sup>80</sup> maintains that a protector is the holder of a fiduciary office *per se* and thus has an irreducible core of duties imposed upon him.

46 The differences between the two views may well be largely semantic. The adoption of either view should not be the end of story. Even if the protector is not in a fiduciary position, “the court’s general jurisdiction to secure the good administration of trusts should, in principle, enable the court to intervene”<sup>81</sup> – even if, for example, the trust instrument lays down that the protector owes no fiduciary duties.

47 Many have questioned whether a trust protector owes fiduciary duties and if so, to whom he owes fiduciary duties.<sup>82</sup> Given that a trust protector is in a position of trust, there is no doubt that the duties owed by a trust protector are in most cases, fiduciary ones<sup>83</sup> that are owed to the beneficiaries.<sup>84</sup> It should be noted that there is a very wide range of fiduciary duties – ranging from the minimum duty to act in good faith to the maximum duty to act like a proper trustee would – the application of which depends on the trust instrument and the circumstances under which the settlor chooses the protector.<sup>85</sup>

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79 Ham, Campbell & Tennet, “Protectors” in *The International Trust* (John Glasson & Geraint Thomas ed) (Jordan Publishing Ltd, 2nd Ed, 2006) 225 at 227.

80 *Underhill and Hayton Law of Trusts and Trustees* (Butterworths LexisNexis London, 15th Ed, 1995) at pp 23–5.

81 Ham, Campbell & Tennet, “Protectors” in *The International Trust* (John Glasson & Geraint Thomas ed) (Jordan Publishing Ltd, 2nd Ed, 2006) 225 at 228. See also *Schmidt v Rosewood Trust Limited* [2003] 2 WLR 1442 (PC) at [51] *per* Lord Walker:

Their Lordships consider that the more principled and correct approach is to regard the right to seek disclosure of trust documents as one aspect of the court’s inherent jurisdiction to supervise, and if necessary to intervene in, the administration of trusts. [emphasis added]

82 Howard Rosen, “The Protectors – The Role of this Little Known Breed with Particular Reference to the Operation of Offshore Trusts” (1993) LSG 90.27(19) at 3.

83 See Duckworth & Richard Lyle Finlay, *Asset Protection: Domestic and International Law and Tactics* vol 3 (Duncan E Osborne ed) (2nd Ed, 1997) at §33:45, 33–30. Duckworth and Finlay state that unless the protector is a beneficiary to whom powers are given so that he can protect his own interests, the protector is likely to be categorised as a fiduciary.

84 See John Conder, “Some Judicial Guidance on Protectors: The *Star Trusts* Case” (1995) 4 PCB 288 at 292; The Step International Committee, “Colloquium on Protectors: Part I” (1996) 1 PCB 24 at 28 *per* Hayton; William Norris and Deborah Hartnett, “The Protector’s Position – Suggesting Some Basic Principles” (1995) 2 PCB 109 at 111 and 118.

85 See The Step International Committee, “Colloquium on Protectors: Part I” (1996) 1 PCB 24 at 28 *per* Hayton.

48 A protector does not have such duties towards a trustee as that will turn the relationship between protector and trustee on its head, given that a protector is primarily appointed to monitor trustee's activities.

49 The claim that a protector owes a fiduciary duty to a settlor remains a moot point, especially if the settlor could force the protector to act. However this has the potential of "unravel[ing] the basic intention of an irrevocable trust, namely: that once the declaration is made, the settlor loses control directly or indirectly over the assets concerned".<sup>86</sup> This also has the potential of bringing into question whether the "trust" is really a sham – an agency rather than a genuine trust to perpetuate the settlor's control over the trust even though the settlor is supposed to "drop out of the picture" after the trust is created. An interesting parallel may be drawn with executive directors in a corporate context, where the non-executive director has a fiduciary duty to the shareholders.<sup>87</sup>

50 However, it should be noted that a "routine transplantation to trust protectors of the same fiduciary standards applied to trustees would be a mistake".<sup>88</sup> Not only are trust protectors not co-trustees, there are also some doubts, depending upon the scope of powers granted to protector, over whether protector is a fiduciary at all.<sup>89</sup> It is submitted that Sterk's proposed deferential standard of behaviour<sup>90</sup> and the concomitant standard of review<sup>91</sup> should be adopted in this situation.

51 This would mean that in most circumstances, the most likely alternative is that the settlor intends for the protector to defer to the trustee's judgment.<sup>92</sup> The settlor gives powers to the protector which has the effect of constraining the trustee's management decisions, not because the protector is expected to exercise those powers, but because their existence will make the trustee more responsive to the interests of the trust beneficiaries, and ultimately to the settlor's wishes. This should not be interpreted as an attempt on the settlor's part to shift all decision-making responsibility from the trustee to the protector. Instead, the

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86 Howard Rosen, "The Protectors – The Role of this Little Known Breed with Particular Reference to the Operation of Offshore Trusts" (1993) LSG 90.27(19) at 3.

87 Howard Rosen, "The Protectors – The Role of this Little Known Breed with Particular Reference to the Operation of Offshore Trusts" (1993) LSG 90.27(19) at 4.

88 Sterk, "Trust Protectors, Agency Costs, and Fiduciary Duty" (2006) 27 Cardozo L Rev 2761 at 2785.

89 Alexander, "Trust Protectors: Who Will Watch the Watchmen?" (2006) 27 Cardozo L Rev 2807 at 2811. See also The Step International Committee, "Colloquium on Protectors: Part I" (1996) 1 PCB 24 at 29 *per* Hayton.

90 Sterk, "Trust Protectors, Agency Costs, and Fiduciary Duty" (2006) 27 Cardozo L Rev 2761 at 2783–2784.

91 Sterk, "Trust Protectors, Agency Costs, and Fiduciary Duty" (2006) 27 Cardozo L Rev 2761 at 2785.

92 Sterk, "Trust Protectors, Agency Costs, and Fiduciary Duty" (2006) 27 Cardozo L Rev 2761 at 2783–2784.

settlor simply expects the protector to monitor trustee behaviour without affecting the level of discretion that the trustee possesses. The protector is expected to assume a monitoring role similar to that of a court, but without the litigation costs commonly involved in court actions. Therefore, the protector is expected to intervene only in situations where the trustee has abused the discretion reposed in him.<sup>93</sup>

52 The adoption of a more deferential standard of review than that conferred on the trustees will help to induce trust protectors to function as settlors intend them to function – as monitors of trustee behaviour. The exact standard will, of course, fluctuate according to the powers that the settlor has conferred on the protector.<sup>94</sup>

53 It is, of course, possible to have situations where a more activist standard of behaviour and a concomitant higher standard of review may be appropriate. Such situations may arise where a trust protector is given extensive powers, such as directive powers over investments and distributions and a power to replace the trustee. In such situations, a protector's role is similar to that of a co-trustee and this justifies a higher standard of behaviour and standard of review.

54 One size will not fit all. Courts will continue to find it difficult to come up with the precise fiduciary rules which should be applied to trust protectors.<sup>95</sup>

55 Arguably, although the label of trust protector may be relatively new, there is nothing new in the concept of a non-trustee having powers in relation to trust property.<sup>96</sup> Courts in England and other major jurisdictions have been dealing with this phenomenon for ages. As a result, there is a significant amount of authority on the duties owed by donees of powers,<sup>97</sup> from which a useful analogy can be drawn. Trust protectors are generally in the similar situation of holding certain powers, such as the power to appoint and remove a trustee.<sup>98</sup>

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93 Sterk, "Trust Protectors, Agency Costs, and Fiduciary Duty" (2006) 27 *Cardozo L Rev* 2761 at 2783–2784.

94 Sterk, "Trust Protectors, Agency Costs, and Fiduciary Duty" (2006) 27 *Cardozo L Rev* 2761 at 2785: "... to the extent settlors expect protectors to play a role distinct from trustees, the standard of review applied to the protector's actions must reflect that distinction".

95 Alexander, "Trust Protectors: Who Will Watch the Watchmen?" (2006) 27 *Cardozo L Rev* 2807 at 2811.

96 Duckworth, "Protectors – Fish or Fowl? Part 1" (1996) 3 *PCB* 169 at 173.

97 Ham, Campbell & Tennet, "Protectors" in *The International Trust* (John Glasson & Geraint Thomas ed) (Jordan Publishing Ltd, 2nd Ed, 2006) 225 at 228.

98 For example, Alaska Stat. s 13.36.370(b)(1) (2005) provides:

(cont'd on the next page)

56 The protector's duties should be considered in relation to each power that has been given to him. More importantly, even if the protector is a fiduciary in relation to a particular power, it does not mean he is automatically a fiduciary in relation to the other powers.<sup>99</sup>

57 The case of *Mettoy Pension Trustees v Evans*<sup>100</sup> in which the court propounds a four-fold classification of powers, should give us a good starting point for analysis. For our purposes, only the first two categories are needed: (A) A power given to a person to determine the destination of trust property without that person being under any obligation to exercise the power or to preserve it; and (B) Any power conferred on the trustees of property or on any other person as a trustee of the power itself. Such a power is a fiduciary power in the full sense. Such a power cannot be released. The donee owes a duty to the objects of the power to consider, as and when it may be appropriate, whether, and if so how, he ought to exercise it. Thus, he is to some extent subject to the control of the courts in relation to its exercise. The court in *Mettoy Pension Trustees v Evans* emphasised that whether a power falls into one category or another is a matter of construction of the trust in light of the surrounding circumstances.

58 This analysis can be extrapolated. The powers of a protector are likely to fall under either category (A) or (B). However, regardless of the category into which the relevant power falls, the protector will owe a duty to abide by the terms of the settlement and not to commit a fraud on the power.<sup>101</sup> As Hammond J notes in the New Zealand Court of Appeal case of *Wong v Burt*:<sup>102</sup>

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A trust protector appointed under (a) of this section has the powers, delegations, and functions conferred on the protector by the trust instrument, which may include the power to

(1) remove and appoint a trustee ...

99 This can be seen in the context of a settlement where the settlor is given: (a) a special power of appointment over the capital of the trust funds; and (b) the power to appoint new trustees, the former is seldom seen as a fiduciary power, while the latter is a fiduciary power. See *In re Skeats' Settlement* (1889) LR 42 Ch D 522 *per* Kay J.

100 [1990] 1 WLR 1586 at 1613 *per* Warner J. Also see Robert Flannigan, "The Adulteration of Fiduciary Doctrine in Corporate Law" (2006) 122(Jul) LQR 449 at 457:

No power is fiduciary *per se*. ... [P]owers are merely capacities or authorities. They are only fiduciary in the sense that they attract fiduciary accountability when exercised by fiduciaries.

101 *Duke of Portland v Lady Topham* (1864) 11 HL Cas 32 *per* Lord Westbury and Lord St Leonards. See also *Vatcher v Paull* [1915] AC 372 at 378 *per* Lord Parker.

102 *Wong v Burt* [2005] 1 NZLR 91 (CA) *per* Hammond J.

The notion of a fraud on a power itself rests on the fundamental juristic principle that any form of authority may only be exercised for the purposes conferred, and in accordance with its terms. This principle is one of general application. The particular expression, 'a fraud on a power', applies to both a power and a discretion. The word 'fraud' here denotes an improper motive, in the sense that a power given for one purpose is improperly used for another purpose.<sup>103</sup>

59 However, classification of a power under category (B), instead of (A), would have far-reaching consequences which include, for example, the power generally cannot be released, other than pursuant to the exercise of a power to release the former power, which latter power is also likely to be fiduciary; in the exercise of the power, the donee must have regard to all relevant considerations and disregard all irrelevant considerations, *etc.* As the power under category (B) is of a fiduciary nature, the donee must not place himself in a position where his personal interest conflicts with his duty – unless permitted by the settlement – and he must not derive any unauthorised profit from the settlement.

#### IV. Control over the trust protector

60 There are two schools of thought on the issue of whether protector, as a power holder, should be subject to the court's control and be made to account to the court.<sup>104</sup> The first views that holders of powers should be subject to the courts' control, and that is pegged at the same level of control that the courts have over trustee of discretionary trusts.<sup>105</sup> Thus accountability is called for on all occasions, save for the narrow band of powers that is granted in order to further the grantor's benefit solely. This means that if the exercise of the power will almost certainly affect the existing beneficial interests of others, the law would intervene to impose accountability obligations on the protector. It would require the grantee to prove that his act or omission is within the scope of the power conferred upon him. The grantee would also have to show that his conduct does not abuse the behaviour expectations that the law imposes on those who are exercising discretions.<sup>106</sup>

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103 *Wong v Burt* [2005] 1 NZLR 91 (CA) at [27]–[28].

104 Waters, "The Protector: New Wine in Old Bottles?" in *Trends in Contemporary Trust Law* (1996) at p 67.

105 Waters, "The Protector: New Wine in Old Bottles?" in *Trends in Contemporary Trust Law* (1996) at p 68.

106 Waters, "The Protector: New Wine in Old Bottles?" in *Trends in Contemporary Trust Law* (1996) at p 68.

61 The second views that where the opportunity to act is given to the power-holder who is not a trustee of trust property,<sup>107</sup> or a settlor has described the power as a personal privilege, the power-holder need not be accountable to any person. The justification is this. The law already confers upon the settlor the freedom to create personal privilege powers. Since this has always been sound law which has created no problems, it should be kept as it is. Thus the second school of thought does not challenge the duty of the trustees to account. Instead, its main argument is that the settlor already has an existing right to create the personal confidence (right or privilege).<sup>108</sup>

62 It has also been questioned whether a settlor can effectively confer powers that give to an outsider, such as the protector, the beneficiary's right to information and to receive accounts, to sue for breach of trust and to release the trustees from liability.<sup>109</sup> If the essential characteristics of a trust are the fiduciary relationship between trustee and beneficiary and property under the control of trustee, then these powers arguably do violate the dichotomy of rights and duties that link trustee and beneficiary. These powers do not render a protector an agent of beneficiary. Just like trustees and beneficiaries themselves as to their rights and duties, the protector looks to the instrument as the sole source of his authority. He is not bound to answer to the beneficiary and cannot be called upon to account in the courts unless his actions make him an independent fiduciary to the beneficiary.

63 A protector is also not exposed to the remedies that the beneficiary has against a trustee to compel good quality administration, and the performance of property disposition obligations set out in a trust instrument. As a non-fiduciary power-holder, he is only subject to the courts' judgment in that he has to act within the scope of his powers. Beyond that, he is accountable to no one, thus "a law unto himself".

64 It is an assurance to know that the court's power of control extends to ensuring that a protector complies with the terms of the settlement and does not commit a fraud on the power.<sup>110</sup> But it is submitted that the court's powers should go beyond that. The court's general jurisdiction to secure the good administration of trusts<sup>111</sup> should,

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107 For example, he may intervene in the exercise by the trustees of their administrative discretions, or he may appoint or delete beneficiaries.

108 Waters, "The Protector: New Wine in Old Bottles?" in *Trends in Contemporary Trust Law* (1996) at p 68.

109 Duckworth, "Protectors – Fish or Fowl? Part 1" (1996) 3 PCB 169 at 170. See further, Duckworth, "The Trust Offshore" (1999) 32 Vand J Transnat'l L 879 at 920.

110 Ham, Campbell & Tennet, "Protectors" in *The International Trust* (John Glasson & Geraint Thomas ed) (Jordan Publishing Ltd, 2nd Ed, 2006) 225 at 234.

111 See *Mettoy Pension Trustees v Evans* [1990] 1 WLR 1586 and Robert Flannigan, "The Adulteration of Fiduciary Doctrine in Corporate Law" (2006) 122(Jul) LQR 449.

in principle, enable it to intervene even if a trust instrument states that the protector is to owe no fiduciary duties.<sup>112</sup>

65 Justifications can be made for such an expansive view. Protectors are a fairly recent development. Just as new judicial principles were developed to control power-holders in other contexts, it is likely that the same will, and should, eventually apply to control protectors.<sup>113</sup>

66 Case law lends support to an assertion, that in appropriate circumstances the court could control protectors by declaring that the exercises of particular powers are invalid.<sup>114</sup> This would include situations where the protector's purported exercise of its power exceeds its limits – as to the acts authorised, or with regard to the purpose of those acts, also known as the fraud on the power doctrine. However, this does not mean that the court will unravel everything that has been done by the protector based on the fact that the power was invalidly exercised.<sup>115</sup> Moreover, if the exercise of the power was partly good and partly bad, severance may be effected so that the valid portion of the exercise of the power will be retained. It also seems, as a matter of principle, that any person affected by the invalid exercise of the protector's powers will have standing to bring an action for that purpose.<sup>116</sup> In such a situation, the trust protector may then be held liable to reinstate the trust fund, if the court regards his conduct to be dishonest.

67 The expansive view also requires that the court controls the trust protectors by the following methods. First, the court can appoint, remove or replace the protector as donee of the power pursuant to its inherent jurisdiction.<sup>117</sup> This move will be particularly appropriate where the protector is guilty of recurrent breaches of fiduciary duty. In the Manx case of *Rawcliffe v Steele*,<sup>118</sup> the court was faced with a trust instrument in

112 See also Ham, Campbell & Tennet, "Protectors" in *The International Trust* (John Glasson & Geraint Thomas ed) (Jordan Publishing Ltd, 2nd Ed, 2006) 225 at 234.

113 *Imperial Group Trust v Imperial Tobacco Ltd* [1991] 1 WLR 589 (Chancery Court) *per* Browne Wilkinson VC.

114 *Turner v Turner* [1984] Ch 100.

115 Duckworth, "Protectors and Other Supernumeraries: Part 2" (2006) 20(4) Tru LI 235 at 246.

116 Duckworth, "Protectors and Other Supernumeraries: Part 2" (2006) 20(4) Tru LI 235 at 246.

117 Ham, Campbell & Tennet, "Protectors" in *The International Trust* (John Glasson & Geraint Thomas ed) (Jordan Publishing Ltd, 2nd Ed, 2006) 225 at 234. See also, *Re the A Irrevocable Trust* [2000] 2 ITEL 482 (High Court of the Cook Islands) at 490, paras (f)–(g) *per* Quilliam CJ. The editor (Philip Baker) noted at 483, para (g)–(h) that: "... this is probably one of the first reported instances of a court deciding that it had power to appoint a protector to a settlement. There is no doubt that a court has power to appoint a trustee to prevent a trust otherwise failing for the absence of a trustee. It is less well settled that the court has power to appoint a protector".

118 *Rawcliffe v Steele* [1993–95] MLR 426 (CA).



which a protector was to play a central role but in which no protector had been appointed. The Manx Court of Appeal held that in such a situation, the court could, and should, appoint a protector. The basis of the decision was that the principle that a trust would not fail for want of a trustee applies equally if the trust machinery would fail for want of a trust protector.

68 In the more recent case of *Re Papadimitriou*,<sup>119</sup> the court was asked to remove a trust protector who allegedly had a conflicting interest, as he was both the beneficiary and also a party to a serious dispute with the plaintiff beneficiary. The court held that it could, and if necessary should, appoint a protector in the same circumstances as it would appoint a trustee if a trustee was either not appointed or declined to act. With regard to the court's power to remove a protector, the court observed that the power to appoint a protector arose out of the principle that a trust will not fail for want of trustee. By analogy, the court would only remove a protector if that was essential to prevent a trust from failing. However, the court also cautioned that it would only so act in exceptional circumstances.

69 Second, the court can direct a protector as to the manner in which he should exercise his powers on a particular occasion, or by nominating a person to prepare a scheme as to the manner in which those powers ought to be exercised. Lastly, if the trustees act in breach of trust, there is also the possibility that the protector may incur liability for wrongfully assisting in that breach of trust under the principles enunciated in *Royal Brunei Airlines v Tan*.<sup>120</sup>

## V. Other concerns over the use of trust protector

70 Besides the serious uncertainties regarding the scope and extent of duties owed by trust protector, the use of trust protector also raises other serious concerns. First, unless the settlor clarifies what exactly his intentions are when appointing a trust protector,<sup>121</sup> the legal consequences might hang in the balance. It could swing either way, depending on the arguments raised in courts.<sup>122</sup>

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119 *Re Papadimitriou* [2004] WTLR 1141.

120 *Royal Brunei Airlines v Tan* [1995] 2 AC 378.

121 For example, stating the purpose or purposes the protector's powers may be used for.

122 Duckworth, "Protectors and Other Supernumeraries: Part 2" (2006) 20(4) Tru LI 235 at 238, states:

The common difficulty with regard to duties is not that the settlor has expressed himself in a way that encounters one of the exceptional difficulties discussed above, but that he has failed to express himself at all, or has not done so comprehensively.

(cont'd on the next page)

71 Second, when the duties of a trust protector – who holds powers which constitute a crucial element of a trust – are exempted or excluded, it could give rise to serious difficulties, and thus warrants particular care.

72 A settlor might grant a trust protector power free of duties when:<sup>123</sup>

(a) the power is being given by the settlor for the benefit or protection of the holder, or as a privilege or right of patronage;

(b) or the settlor's intention is to enable the [protector] to assist, not to require him to do so – a moral duty, perhaps, but not a legal duty. The absence of a legal duty may reflect either the [protector's] unwillingness to accept duty – and the consequent risk of litigation and liability. Or it may reflect a view on the part of the settlor that the prospects of achieving the settlor's objectives are improved by excluding duty.

73 The wisdom of such a move by the settlor can be questioned, especially if the power granted to the protector is such that he could, by his misguided action or inaction, disrupt the administration of the trust or compromise the achievement of the settlor's objectives. Here, as a solution, perhaps a parallel can be drawn with exemption clauses for trustees. Generally, if a trustee can prove that the settlor knew, and approved of, the clause in a trust instrument which exempts the trustee from liability for a breach of trust upon a fair and non-restrictive construction of the clause, then the trustee will be able to escape liability for such a breach, unless it was a dishonest or reckless breach of trust.<sup>124</sup>

74 Similarly, when determining the scope of a protector's duty, a court will need to consider the purposes of the settlor in conferring particular powers on the protector, as well as the terms of any exemption or other clause in the trust instrument that relates to the protector's position. A court may well be of the view that if the protector is an unpaid friend or relative of the settlor then the extent of the fiduciary duty is to act in good faith. However, if the protector is a paid professional he should be subject to the full extent of fiduciary responsibilities applicable to trustees.<sup>125</sup> There is little reason to allow

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For example, with reference to the classification of powers in *Mettoy Pension Trustees v Evans* [1990] 1 WLR 1586, the resultant duties of the protector would depend on the category of power under which the power is classified.

123 Duckworth, "Protectors and Other Supernumeraries: Part 2" (2006) 20(4) Tru LI 235 at 250–251.

124 See also *Hayton and Marshall: Commentary and Cases on the Law of Trusts and Equitable Remedies* (London: Sweet & Maxwell Ltd, 12th Ed, 2005) at p 659; *Armitage v Nurse* [1998] Ch 241 at 253–254.

125 See also Underhill and Hayton, *Law of Trusts and Trustees* (London: Buttersworth LexisNexis, 16th Ed, 2003) at p 31.

professional trustees, whether corporate or individual, in selling their skilled services, to exempt themselves from liability for grossly negligent breaches of trust, or even ordinarily negligent breaches.<sup>126</sup>

75 Third, the appointment of a supernumerary based solely on the idea that he will be the settlor's "hands", and do as the settlor bids, is likely to lead to trouble of various kinds. One is as regards agency costs. The settlor's interests, and those of the beneficiary, are normally closely aligned in most trust situations. This means that agency costs would be minimised if the protector acts according to the settlor's instructions. However, the problem is that there is no guarantee that the protector would do so, especially when we are talking about professional protectors who enjoy no close personal bond with the settlor.<sup>127</sup>

76 There is no obvious market mechanism for assuring that the protector follows the settlor's instructions.<sup>128</sup> Moreover the protector's performance will often be impossible to measure. Even when the enforcement duties fall to the beneficiaries, there are familiar difficulties. One difficulty is that even when the interests of the beneficiaries are perfectly aligned with the settlor's, beneficiary enforcement replicates the costs associated with fiduciary duty litigation against trustees.<sup>129</sup>

77 Fourth, the grant of powers to the trust protector may result in uncertainty for some trustees about the effect of such powers on their own duties and protections. This could result in the reduction of the incentives for the trustee to exercise prudence in managing the trust assets.

78 Fifth, the trust protector's supernumerary powers come at a price which, if not paid at the outset (for careful planning and drafting) may well have to be paid later in sorting out difficulties and disputes.<sup>130</sup>

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126 See United Kingdom, Law Commission Report, *Trustee Exemption Clauses* (No 301, 2006) at para 4.1. The Law Commission approved of "the approach to trustee exemption clauses set out in the CP [which] built upon a distinction between professional trustees and lay trustees. In principle, the case for regulation of the former in their reliance upon exemption provisions was felt to be considerably stronger than the case for regulation of the latter".

127 Sterk, "Trust Protectors, Agency Costs, and Fiduciary Duty" (2006) 27 *Cardozo L Rev* 2761 at 2774.

128 Gilson and Kraakman made similar observations with respect to outside corporate directors. See Ronald J Gilson & Reinier Kraakman, "Reinventing the Outside Director: An Agenda for Institutional Investors" (1991) 43 *Stan L Rev* 863 at 875–76 (noting absence of evidence that market for outside directors exists at all).

129 Sterk, "Trust Protectors, Agency Costs, and Fiduciary Duty" (2006) 27 *Cardozo L Rev* 2761 at 2772.

130 Duckworth, "Protectors and Other Supernumeraries: Part 2" (2006) 20(4) *Tru LI* 235 at 253, 258.

79 A protector's supernumerary powers may complicate the administration of trust, thereby increasing administrative expenses. Issues about costs and expenses which arise from giving such powers to trust protectors need to be considered, even before a trust instrument is drafted.<sup>131</sup>

## VI. Admitting the concept of trust protector into the onshore jurisdictions?

80 I shall elaborate on the many arguments advanced to admit the concept of trust protector into the onshore jurisdictions by statutory means, before setting out the reasons why a cautious approach is required.

81 Many reasons could be advanced to admit the concept of trust protector into the onshore jurisdictions. The benefits that the office of trust protector brings – achieving clients' objectives and in making the institution of trust more useful and versatile – are undeniable. In an environment where changes are frequently made, the core of any long-term efficient property arrangement for the benefit of others must be a suitable, reliable, efficient and flexible system of discretionary powers or duties.<sup>132</sup> Therefore, a system that deposits all these powers into the hands of a single person is taking on risks which are unnecessary, and should be avoided.<sup>133</sup>

82 The traditional English solution to such problems in private trusts has been to appoint multiple trustees, with the intention that between the trustees some of them should at least possess the necessary knowledge, expertise and inclination to handle satisfactorily all aspects of trust administration, and meet all eventualities, while keeping an eye on one another to prevent breaches of duties and abuse of powers.<sup>134</sup> The multi-trustee approach does have some potential, and it has been occasionally adopted. But in most cases it is unappealing. It brings with it certain fundamental flaws: (a) the cost and complication of involving several trustees in all aspects of the administration, especially if the trustees are in different countries; (b) tax problems or concerns if the

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131 See Peter T Wendel, "The Evolution of the Law of Trustee's Powers and Third Party Liability for Participating in a Breach of Trust: An Economic Analysis" (2005) 35 SHLR 971 at 1028; Andrew H Prussack, "Creation, Administration, and Effectiveness of the 'Failsafe' Trust for Nonresident Aliens" (1987) 17 Ga J Int'l & Comp L 121 at 145.

132 Duckworth, "Protectors and Other Supernumeraries: Part 1" (2006) 20(3) Tru LI 180 at 182.

133 Duckworth, "Protectors and Other Supernumeraries: Part 1" (2006) 20(3) Tru LI 180 at 182.

134 Duckworth, "Protectors and Other Supernumeraries: Part 1" (2006) 20(3) Tru LI 180 at 182.

trustees are not all in the same jurisdiction; (c) the vulnerability of the trust structure if trustees reside in jurisdictions that take a different view of trusts, or of the particular trust; (d) the difficulty in finding suitable persons willing to serve as trustees; (e) the desire of many settlors to create powers for themselves or their beneficiaries – and sometimes outsiders – which are free of fiduciary duties.<sup>135</sup>

83 As settlor's watchdog over the trustees, the trust protector sets the settlor's mind at ease. The settlor can provide in the trust instrument that the trust protector will have the "powers to remove the trustee; to name a successor trustee; to approve any investments made by the trustee; to approve distributions of the trust income and capital, and to transfer the *situs* of the trust and/or the trust assets to a new jurisdiction".<sup>136</sup> This would also be applicable in the context of an onshore trust – even though the benefits would be smaller since the settlor may be able to watch over the trustee personally – since not all settlors will be willing to spend much of their time checking on their appointed trustees

84 Arguably, the lack of statutory recognition of the role of protector also provides a benefit to the settlor. He can determine what kind of, and how much, powers to grant to the protector. In reaching a decision, the settlor will be able to weigh the cost and possible dislocation of bringing in a third party to be directly involved in the trustee's operation, against the advantages of having a protector involved in the decisions of the trust.<sup>137</sup>

85 Trustees who, for whatever reasons, under-perform can be removed quickly without much fuss and the liaison between trustee and distant beneficiaries can be made smoother, thus preventing the potential for disputes to arise in the future. In situations where the trust assets consist of an active offshore business, the local protector/power-holder will play the role of the onshore settlor's supervisor who can deal with employee problems and contingencies. A protector, who is holding power on the spot, will also be the best man for the task if emergencies arise. This is also the case if it is decided that movement of the trust elsewhere would be desirable, and this needs to be accomplished with maximum speed and minimum fuss. This would include situations such as where the jurisdiction that the trustees are located in is no longer appropriate due to perhaps the dramatic increase of the tax rates in that jurisdiction, or if a trust company itself can no longer continue to act as a trustee

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135 Duckworth, "Protectors and Other Supernumeraries: Part 1" (2006) 20(3) Tru LI 180 at 182.

136 See Andrew H Prussack, "Creation, Administration, and Effectiveness of the 'Failsafe' Trust for Nonresident Aliens" (1987) 17 Ga J Int'l & Comp L 121 at n 152.

137 Howard Rosen, "The Protectors – The Role of this Little Known Breed with Particular Reference to the Operation of Offshore Trusts" (1993) LSG 90.27(19) at 2.

perhaps because of a conflict or potential conflict of interest within the group or even because the trust company is facing financial difficulties. The presence of the trust protector ensures that these problems can be overcome quickly.<sup>138</sup> This is a benefit of having a protector, in contrast with a trustee who may be unable to carry out the move himself because of local legislation or peculiar conditions.

86 Moreover, arguably, the appointment of professional protectors does not generally require huge expenses. Typically, they will only charge a small annual fee for acting and then time costs for any actual work done. Arguably, unless there is a crisis in the management of trust, these additional costs will be relatively small – the protector, who plays and exercises a general supervisory function, would unlikely be required to be involved in the day-to-day management of the trust.<sup>139</sup>

87 A trust protector can be employed either for the benefit of beneficiaries or only for the purposes of protecting the wishes and intentions of settlor. Thus, the potential benefits from the greater employment of protector in onshore jurisdictions can thus be analysed through the perspectives of the beneficiaries as well.

88 When the powers of trust protectors are designed to protect the interests of beneficiaries, it is likely that some of these protectors will be able to improve the management of trusts. It is a call for the settlor to make. When the trust instrument provides that the function of the protector is to protect the interests of the beneficiaries, it is reasonable to presume that the settlor has made a correct judgment that the beneficiaries will be better off because of the presence of the protector.<sup>140</sup> This is notwithstanding the counter-productive effects catalogued by Sterk:

The protector may have reasons – rooted in the beneficiaries' best interests – for deferring to the trustee's decision even if the protector believes that those decisions reflect a breach of fiduciary duty. Especially if the trustee is solvent, the protector may conclude that the beneficiaries will be better off as a result of the trustee's decision. The protector (like the settlor) may have confidence in the trustee's investment instincts, however inconsistent with modern portfolio theory, and may conclude that allowing the trustee's decision to stand will leave the beneficiaries better off: if the trustee's instincts pay off, the beneficiaries profit, while if they do not, the trustee is liable for breach.

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138 Howard Rosen, "The Protectors – The Role of this Little Known Breed with Particular Reference to the Operation of Offshore Trusts" (1993) LSG 90.27(19) at 2

139 Howard Rosen, "The Protectors – The Role of this Little Known Breed with Particular Reference to the Operation of Offshore Trusts" (1993) LSG 90.27(19) at 3.

140 Jeffrey Evans Stake, "A Brief Comment on Trust Protectors" (2006) 27 Cardozo L Rev 2813 at 2814.

The trustee's liability itself is a mechanism for diversifying the beneficiaries' risks.<sup>141</sup>

89 There are a few possible roles a protector may play, different from that of the trustee overseer, which could give beneficiaries additional benefits and also improve social welfare. One possibility is the casting of protector in the judicial role of hearing and resolving disputes between beneficiaries and trustees. This, among others, should produce the advantage of having a protector who knows the beneficiaries' interests and needs better than any court to resolve disputes, thus ultimately serving the beneficiaries' interests better. The benefit to social welfare is also self-evident, as the substitution of the protector for the court means society on a whole would benefit from the reduced workload of the publicly supported judicial system.<sup>142</sup>

90 Moreover, when a settlor is alive, there are clear benefits to him when the protector is appointed to protect his goals that differ from that of the beneficiaries.<sup>143</sup> However, the more common situation we find ourselves in is likely that the settlor has passed away and his interests have thus dropped out of the social welfare equation. It is also likely that a protector would only work when he is paid and derives no other benefits from his work. In this case, the societal viewpoint clearly tilts towards not having a protector, as the deceased settlor has caused a person to forgo opportunities for productive behaviour in favour of protecting a dead man's interest. Thus society is left with the task of paying the continuing and probably escalating costs of the settlor's whims and fancy, even though he may have passed away.<sup>144</sup> The counter-argument that honouring the settlor's intention when he is dead makes him happier than when he is alive can be criticised for placing heavy emphasis on the subjectivity of the settlor's emotions to the detriment of societal welfare.

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141 Sterk, "Trust Protectors, Agency Costs, and Fiduciary Duty" (2006) 27 *Cardozo L Rev* 2761 at 2789.

142 Stake has highlighted the problems with this approach: Stake, "A Brief Comment on Trust Protectors" (2006) 27 *Cardozo L Rev* 2813 at 2815. Furthermore, the most obvious case is where there is a divergence between the goals of settlor and that of beneficiaries. The *Clafin* doctrine (*Clafin v Clafin* 20 NE 454 at 456 (Mass, 1889)) which prevents beneficiaries from collectively terminating the trust while a material purpose of the settlor remains unfulfilled, is proof that there are judicially cognizable interests of the settlor separate from those of the beneficiaries. See also Jessica L Lacey, "The Dead Hand Loses its Grip in Virginia: A New Rule for Trust Amendment and Termination?" (1995) 29 *URMDLR* 1235 at 1235; Paul Matthews, "The Comparative Importance of the Rule in *Saunders v Vautier*" [2006] *LQR* 266 at 283.

143 See Stake, "A Brief Comment on Trust Protectors" (2006) 27 *Cardozo L Rev* 2813 at 2815.

144 Stake, "A Brief Comment on Trust Protectors" (2006) 27 *Cardozo L Rev* 2813 at 2815.

91 Although the potential welfare benefits are less apparent in the second situation, nevertheless, when the two situations are seen as a whole, arguably, the office of the trust protector does have the potential to provide welfare benefits not only to the players in the trust relationship, but also to society at large.<sup>145</sup>

92 The New Zealand Law Commission has also recommended that statutory intervention – that provides for trust protector – is required in the interests of certainty. This serves to clarify the protector’s liabilities and obligations, and their impact on the trustee’s liabilities.<sup>146</sup> The tentative view is that “the existing law is sufficiently robust to solve most but not all of the obvious problems”.<sup>147</sup> This conclusion is reached with the aid of s 49 of the Trustee Act 1956, which provides for the role of “advisory trustee”;<sup>148</sup> with the only difference being that a trustee may elect to consult an advisory trustee, but is under an obligation to act under the directions of the protector.<sup>149</sup>

## VII. Justified reluctance

93 The reluctance of onshore jurisdictions to formally introduce the concept of trust protector by statutory means is mainly down to the potential disadvantages and uncertainties that such a move could bring.

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145 Stake, “A Brief Comment on Trust Protectors” (2006) 27 *Cardozo L Rev* 2813 at 2815.

146 New Zealand Law Commission, *Some Problems in the Law of Trusts* (Preliminary Paper No 48, January 2002) at para 1.

147 New Zealand Law Commission, *Some Problems in the Law of Trusts* (Preliminary Paper No 48, January 2002) at para 19.

148 Section 49(1) of the Trustee Act 1956 (No 61 of 1956) provides:

In the administration of any trust property any trustee may act, to the extent hereinafter provided, with an advisory trustee, which term includes, in its application to the estate of a [mentally disordered person], an advisory [manager] or advisory administrator of the estate; and also includes, in its application to the estate or any part of the estate of any person in respect of whom a [property order] is made under the [Protection of Personal and Property Rights Act 1988], an advisory manager of the estate, or any part thereof.

149 It should be noted that the New Zealand government has since responded by stating that it would consider the issues raised by the Commission and undertake further work on their recommendations.



94 The Law Reform Committee of the Singapore Academy of Law in its 2003 Report on the *Reform of Certain Aspects of the Trustees Act*<sup>150</sup> submitted persuasively that no changes should be made to the Trustees Act to regulate the relationship between trust protectors and trustees, expressing concerns on the different roles played by the trust protector; the ability of the common law and equity to focus on the actual functions – rather than the form – of the protector in determining the incidence of legal liability; and the difficulties this may create in the context of collective investment schemes, like unit trusts, where the respective roles of managers and trustees have been developed to suit the needs of financial markets. The Singapore Committee's more conservative approach is that of wait-and-see – developments in the common law and statutory developments elsewhere should be monitored before this issue is revisited. This is in contrast to the approach of its New Zealand counterparts.<sup>151</sup>

95 The Singapore Law Reform Committee has rejected the New Zealand Law Commission's move on the rationale that the Trustees Act of Singapore does not have a comparable provision of s 49 of the Trustee Act of New Zealand, and that the issue is not confined to trust protectors alone, and it is not clear how a new provision on trust protectors would impact on the relationship between the fund manager and the trustee in a unit trust situation.<sup>152</sup> As the Law Reform Committee of the Singapore Academy of Law rightly pointed out in 2003, the danger from the point of legal certainty is that the trustee's role may be seen by the court to have been usurped by the protector. That in turn has the potential of bringing about serious consequences in the allocation of legal liability, and the lack of certainty and predictability in such allocation.<sup>153</sup>

96 It should also be noted that, thus far, jurisdictions such as Canada and England have remained silent as to the possible reform of their respective Trustee Acts to encapsulate the concept of trust protector.

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150 Law Reform Committee, Singapore Academy of Law, *Report of the Sub-Committee on the Reform of Certain Aspects of the Trustees Act* (31 March 2003) at para 42.

151 New Zealand Law Commission, *Some Problems in the Law of Trusts* (Preliminary Paper No 48, January 2002) at para 17.

152 Law Reform Committee, Singapore Academy of Law, *Report of the Sub-Committee on the Reform of Certain Aspects of the Trustees Act* (31 March 2003) at para 41.

153 Law Reform Committee, Singapore Academy of Law, *Report of the Sub-Committee on the Reform of Certain Aspects of the Trustees Act* (31 March 2003) at para 37.

97 In addition to the arguments above, it is also clear that a protector can be given a “roving commission to supervise and approve trustee actions of all kinds”,<sup>154</sup> and also to initiate matters pertaining to a trust. Moreover, as a non-trustee, the protector is not subject as a trustee is, to the beneficiary’s call for an accounting on reasonable demand.<sup>155</sup>

98 Since a protector may be given any type of power, there is the fear that the office of trust protector may be used by a settlor as a way to conceal his continued control over the trust assets. This fear arises as once a declaration of trust is made, the settlor loses both direct and indirect control over the assets concerned.<sup>156</sup> In such a case, the trust protector clearly represents the introduction of a “settlor-friendly” intervention into the trust management when tax considerations rule out both the presence of the settlor in the trust structure<sup>157</sup> and the conferment of reserved powers upon the settlor.<sup>158</sup> Consequently, tax authorities or disgruntled beneficiaries may try to have the apparent trust declared wholly invalid on the basis that no trust exists or that it is contrary to public policy for the courts to uphold such a trust.<sup>159</sup>

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154 Waters, “Protectors and Enforcers: Drafting the Trust Instrument” (2000) 8(4) J Int’l P 237 at 238.

155 Waters, “Protectors and Enforcers: Drafting the Trust Instrument” (2000) 8(4) J Int’l P 237 at 238.

156 See Rosen, “The Protectors – The Role of this Little Known Breed with Particular Reference to the Operation of Offshore Trusts” (1993) LSG 90.27(19) at 3.

157 Waters, “The Protector: New Wine in Old Bottles?” in *Trends in Contemporary Trust Law* (1996) at p 66. Waters notes that this is especially the case when:

[S]ome protectorships ... control completely who shall receive income or capital as beneficiaries of the particular trust, and others have a right of intervention and veto in the exercise by the trustees of any of their portfolio-management powers, in particular when there is a favoured family business as part of the settlor’s wealth.

See also Peter Willoughby, “International Trust under Fire – The Increasing Scope for Litigation Part I” (1996) 4 PCB 226 at 234:

[A] trust under which the settlor retains a power of revocation and other wide powers relating to the control and distribution of assets which override those of the trustees is probably in equally serious danger of being set aside as a sham or classified as creating a legal relationship such as a bailment, agency or nominee ship rather than a trust. This will be particularly so where the trustees have done very little to administer the trust other than to record and act upon the instructions of the settlor or a protector appointed by the settlor who takes instructions from the settlor.

158 See also R P Meagher and W M C Gummow, *Jacobs’ Law of Trusts in Australia* (Butterworths Sydney, 6th Ed, 1997) at p 71, para 323:

One question that may arise is whether, in a given case, the selection of the ‘protector’ by or pursuant to the trust instrument is but a sham, in the true sense of that term, so that the ‘protector’ is to be treated as bearing the full measure of the duties and liabilities, if not also the rights, the protector would have if expressly designated as trustee.

159 Waters, “Protectors and Enforcers: Drafting the Trust Instrument” (2000) 8(4) J Int P 237 at 238.

99 Moreover settlors of onshore trusts, who are likely to know and consequently have confidence in their chosen trustees, are unlikely to see the need for the appointment of a trust protector. Onshore trustees are likely to be susceptible to the influence of the settlor and the beneficiaries,<sup>160</sup> thus reducing the chances of the trustee acting contrary to the wishes of the settlor or the beneficiaries. This can be contrasted with the offshore trusts, which require locally based trustees whom neither the settlor nor the beneficiaries would know and trust, thus resulting in the frequent utilisation of the office of trust protector. The conclusion is that although trust protectors may be an important component of the offshore trust structure, such an office is actually unnecessary in onshore trusts, which are functioning perfectly well with the traditional trust structure. Indeed, introducing the trust protector in onshore trusts may introduce much uncertainty into the existing trust structure, which would be undesirable to all concerned.

### VIII. Risks of conceptual muddle

100 The fact that a trust protector may be given any kind of power, and that in at least some circumstances, it is uncertain whether a trust has indeed been created, highlights the paramount importance of a correct analysis of the nature of the position of trust protector.

101 We need to be clear on several matters regarding the office of trust protector, such as the standards of behaviour required of the office of trust protector, the accountability of that office holder, and to whom he should be accountable, and the remedies available when the protector either abuses his office or refuses to exercise his powers. It is precisely the lack of clarity, and certainty, in these matters that calls for caution.

102 It is an unsatisfactory situation that no court in the onshore jurisdictions, thus far, has had the opportunity to consider and clarify such issues. It is also dissatisfying that the nature of protectorship appears to be simply what the settlors and their advisors come up with, to suit their own purposes.

103 As different jurisdictions seek to develop a flexible trust concept which will satisfy the needs of the increasingly competitive commercial trust and wealth management industry, caution has to be exercised so as to prevent the law in this area from becoming overly flexible. Certainty and predictability are important issues in the equation. If the concept is not properly grasped, and its complications are not satisfactorily worked

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160 See also A J Oakley, Parker & Mellows, *The Modern Law of Trusts* (Sweet & Maxwell London, 7th Ed, 1998) at p 166.

out, before it is abruptly introduced formally, it could result in adverse effects on the very foundations of trust law. The concept of trust protector brings with it considerable risks of conceptual muddle.

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