The International Family Offices Journal

Editor: Nicola Saccardo

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STEP ADVISING FAMILIES ACROSS GENERATIONS

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The International Family Offices Journal

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Welcome to the 29th issue of The International Family Offices Journal!

Nicola Saccardo

Welcome back from the summer break and to the 29th issue of *The International Family Offices Journal*. We have another excellent selection of articles in this issue for your consideration. The return after the summer months often has a back-to-school feel for both families and professionals in the family office space, as we look to the challenges and opportunities ahead.

This issue includes interesting insights on family enterprises. Jill Barber, Torsten M Pieper and Greg McCann examine dynamics affecting family enterprises and those who serve them, including the assumptions that can hurt the dynamics and distract from the fulfilment of a family's desires. In his article "Why does family governance fail?", Dominik v Eynern looks at the importance of family governance and why family systems are more prone to behavioural risks than non-family businesses.

Barbara Ruth Hauser and Winnie Qian Peng focus on how traditionally Western-facing family offices might be tailored to meet Eastern values. They explore research undertaken by the Bank DBS Singapore and set out a thought-provoking new family office model, drawing on Confucian values from the East.

On the other side of the world, we focus on Spain. While Spain has not traditionally been thought of as an attractive jurisdiction for high and ultra-high-net-worth individuals, Florentino Carreño and Beatriz San Basilio of Cuatrecasas in Madrid, set out details of why it is a more favourable jurisdiction than people might initially assume. They focus on the 'impatriates regime', introduced for those moving to Spain for employment or investment purposes, and its interaction with other taxes.

How to engage with families on environmental, social and governance (ESG) factors is the focus of Shelly Meerovitch's article, where she draws on her experience in this space. She looks at how to integrate ESG factors when the outlook of family members to such matters can vary significantly, with a focus on the Investment Policy Statement as a key tool.

The use of private trust companies is something we see more and more in the family office sphere. A new Swiss alternative has entered the market, the dedicated trust company (DTC). Jessica Schaedler introduces this structure and provides a helpful comparison of PTCs and DTCs in the Swiss environment.

Litigation in and around wealthy families continues to be an important topic and provides lessons for those advising them. Marcus Parker and Judith Swinhoe-Standen look at recent litigation trends focusing on mental capacity and the restructuring of trusts in the UK context. They go on to examine conflicting global cases focusing on the use of trust powers for improper purposes.

As family offices grow and become more sophisticated so do their requirements for the families they serve. Christian Stewart explores the role of a chief learning officer (CLO) and how they can add to family offices and human capital of the families they serve. This article explains the purpose and function of a CLO.

Tsitsi M Mutendi then builds on earlier articles she has written for the Journal on diversity and the

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challenges raised by more global families. In her latest article, she looks at multigenerational family environments and how these result in constant flux for families and those who advise them. Her article includes an interesting case study for our consideration.

Lastly, Rebecca Eastmond and Peter Goddard draw on their vast experience of working in the philanthropic space to look at how to develop a successful philanthropic strategy. Including a discussion by Peter of his responsibility for a new foundation focusing on mental health.

The Journal closes with the usual highlights from the recent STEP News Digest.

To conclude, I am pleased to report that the third edition of the book *Family Offices: The STEP Handbook for Advisers*, edited by Barbara H Hauser and myself, has just been published by Globe Law and Business. We would like to thank all the contributors.

Recent trends in litigation

Marcus Parker and Judith Swinhoe-Standen

This article considers some of the trends that have developed in trust and probate litigation over the last year or so. Family offices need to be alert to all of these issues to ensure that they and their advisers can respond accordingly. Proactive steps and early legal advice can often reduce the threat, or the impact, of costly and uncertain litigation.

Mental capacity

There has been an unprecedented focus on mental health in recent years. Our ageing population brings about more age-related conditions, such as dementia and other conditions affecting memory. Younger people are outspoken about issues such as depression and anxiety, and a greater understanding of ADHD and autism has led to a rise in diagnoses.

Mental health conditions overlap with mental capacity where the condition in question causes an "impairment of, or a disturbance in the functioning of, the mind or brain" (Section 2(1) of the Mental Capacity Act 2005) to the extent that it affects a person's ability to make a particular decision at the time they are making it. Capacity questions can arise during a person's lifetime or after their death.

Probate

Looking first at capacity questions after death, challenges to a will's validity are often triggered by suspicious content in a will. Determining a deceased person's capacity often necessitates an examination of their medical records and sometimes a retrospective capacity assessment. Capacity claims often go hand in hand with undue influence allegations, as people can be more susceptible to this when their capacity is declining.

The earliest (Victorian) capacity cases tend to involve obvious doubts about the testator's capacity in the form of hallucinations or delusions. Recent cases involve far more nuanced psychiatric analysis. For example, the testator in *Clitheroe v Bond* [2022] EWHC 2203 (Ch) excluded her daughter from her will because she believed she was irresponsible with money and had stolen from her. Although objectively reasonable, these beliefs transpired to be untrue and were found to have resulted from a complex grief reaction to the death of the testator's other daughter. Her two latest wills (made under those mistaken beliefs) were found invalid due to lack of capacity.

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Court of Protection

Where a person lacking capacity is still living and there is a dispute about their affairs, or a decision needs to be made about their affairs which they lack capacity to make themselves, it is possible to apply to the Court of Protection (CoP). (The person lacking capacity is referred to as 'P' in the CoP for confidentiality purposes.) The CoP deals with issues including and relating to lasting powers of attorney (LPAs) and appointment of deputies (if P is unable to manage their property and affairs or make decisions about their health and welfare), statutory wills (if P is found to lack testamentary capacity) and lifetime gifts (if P lacks capacity to make them).

The CoP's paramount concern when deciding whether to authorise or decline proposed decisions is what is in P's best interests.

Insofar as LPAs are concerned, the majority of cases relate to finances. There has, however, been an uptick in health and welfare cases, especially where P is a high-net-worth individual falling outside the United Kingdom's social care regime. Large-scale proceedings have recently concluded regarding Srichand Hinduja, a wealthy businessman who had dementia and whose family could not agree on various matters, including his care arrangements (*Hinduja v Hinduja and others* [2022] EWCA Civ 1492).

If P lacks capacity to make an LPA, trusted relatives or friends can apply for a deputyship order. This carries more onerous reporting obligations than an attorney under an LPA. A deputyship application can take months to process, meaning P's affairs cannot be effectively managed in the meantime.

When considering whether it is in P's best interests to make a lifetime gift, the CoP will consider a range of factors, including whether the gift is affordable in light of P's future needs and expenses, whether P would want to make the gift if they had capacity, and whether there are tax advantages to making the gift.

Trusts

In the context of trusts, addressing capacity issues varies depending on the person's role in the trust.

If a beneficiary lacks capacity and has no LPA, the issues are largely practical, such as who will manage the bank account receiving their distributions. This can be resolved by seeking a deputyship order from the CoP.

If a trustee lacks capacity, a remaining competent trustee can facilitate their replacement (Section 36(1) of the Trustee Act 1925). If a sole trustee has lost capacity, their attorneys can step in. Realistically, their best option would be to arrange for the trustee to retire and appoint a new one. As a last resort, the court can appoint new trustees (Section 41 of the Trustee Act 1925). Again, this can be a long and expensive process, depending on what (if any) resistance there is to the appointment.

As for protectors, problems arise if they lack capacity to consent to any trustee decisions that require it. Unless the trust deed contains provision for replacing the protector, decision-making can grind to a halt entirely, and the parties will be reliant on the court's inherent jurisdiction to remove or suspend powers.

Finally, it is worth carefully considering which capacity test applies if a capacity assessment is required, as different jurisdictions have different tests. This is likely to depend on the governing law of the trust.

Practical tips

To avoid complications caused by capacity issues, family offices can consider:

- Checking in regularly with clients who are particularly susceptible to capacity issues due to age or illness;
- Advising clients to review their testamentary affairs regularly (preferably every five years). This helps avoid the risk that they become unable to update an old will due to lack of capacity, risking court proceedings before or after their death;
- Helping clients create LPAs when they have capacity;
- Regularly reviewing whether the trustees and protectors of clients' structures are still suitable and have capacity; and
- Reviewing clients' wealth structures holistically in all applicable jurisdictions, including facilitating lifetime gifts or establishing trust structures while their capacity is sound.

Trust restructuring

Another recent trend in litigation is an increased number of trust restructuring cases.

Reasons to restructure

Trusts are often family wealth holding structures. However, families are more complex than ever before. It is not uncommon to have second or third marriages or unmarried partners, meaning that several branches of a family can coexist. This can create friction or perceptions of unfairness between branches where a trust is involved. Such disputes might be best resolved by restructuring the trusts or, in certain circumstances, carving out a portion of it and settling it on a separate trust.

Some restructurings are non-contentious and result from the trustees' decision to change aspects of the trust in the beneficiaries' interests. Others are much more complex and result from a number of different factors. For instance, trustees might wish to change the trust's structure to benefit from different regulatory, statutory or tax rules. This may be prompted by the increased public focus on multi-jurisdictional wealth planning, generated in part by widely-reported data leaks, which has led to tighter regulations and additional scrutiny of trusts in some jurisdictions. Retaining anonymity, often motivated by security concerns, may also prompt a restructuring. For example, trusts must be registered in England and Wales, and the courts in some jurisdictions have shown reluctance to grant anonymity orders in trust cases unless there is a good reason to do so (see, eg, *HSBC Trustee CI v Kwong* [2018] JRC051A).

Carve-outs

In appropriate circumstances, an alternative to a full restructuring is a carve-out. This is quite common on divorce if the class of beneficiaries includes the settlor's issue and their spouses, meaning that the

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spouse who benefited from the trust during their marriage will be excluded when the divorce is finalised.

This idea was considered pre-emptively in *Re the V, W, X and Y Trusts* [2021] JRC 20. The trustee proposed to settle a new trust from the trust assets in order to meet the 'needs' element of any potential divorce by a future spouse of a beneficiary.

Process

The trustees must apply to the court for approval of their restructuring proposal as it is a "momentous decision" under *Public Trustee v Cooper*, even if the restructuring is non-contentious. The court must be satisfied that the proposal is within the trustees' powers and is not one that no rational trustee could reach.

In more straightforward and/or non-contentious restructuring arrangements, the trustees might seek court approval only when they have formulated final proposals. However, in more contentious or complex cases, restructuring applications are increasingly taking a staged approach whereby trustees are asking the court to bless in-principle decisions or certain aspects of the restructuring proposal before subsequently seeking a final blessing. For example:

- In *Re the XYZ Trusts* [2017] SC (Bda) 111 Civ, the court approved the trustees' decision to develop detailed proposals for restructuring the trusts and later approved the final proposals in *Re the XYZ Trusts* [2022] SC (Bda) 10 Civ; and
- The ongoing matter of *SG Kleinwort Hambros Trust Company (CI) Limited v B and others* [2023] JRC054 indicates that the Jersey court is willing not only to consider restructuring proposals at interim stages but also to take a more freeform and interventionalist approach than has been adopted or sought in previous cases. In this case, the court intends to consider the *Public Trustee v Cooper* test only at the final stage and meanwhile give non-binding guidance on the proposal as it stands.

Finally, it is worth bearing in mind that it is not unusual for a restructuring to result from hostile relations among the beneficiaries and/or between the beneficiaries and the trustees. Trustees should be decisive and transparent when formulating proposals while firmly managing the different groups of beneficiaries to minimise conflict and ensure the restructuring process goes as smoothly as possible.

Trustees exercising powers for an improper purpose

Those appointed as custodians of significant family wealth might be aware of two recent cases decided at almost exactly the same time, in which the courts considered whether the trustees had exercised their powers for an improper purpose or, to use the more archaic wording, committed a fraud on a power.

Grand View Private Trust Company Limited and another v Wong and others [2022] UKPC 47

This case centred around two trusts settled in 2001. The Global Resource Trust (GRT) was a discretionary trust for the benefit of the remoter issue of the two economic settlors. The Wang Family Trust (WFT) was a purpose trust with a mixture of non-charitable and charitable purposes but (despite its name) conferring no benefit on family members. Grand View was trustee of the WFT.

In 2005, the GRT trustees executed an 'irrevocable deed', which added Grand View as an object of the GRT, excluded all the existing objects of the GRT and transferred all the GRT's assets to Grand View. Consequently, all the assets of the GRT, which had been for the benefit of the Wang family, were now held on a purpose trust from which no family member could benefit. Grand View then terminated the GRT.

After learning of this, one former beneficiary of the GRT (Winston) challenged the decision on the basis that (among other things) it was in excess of the trustee's powers and was taken for an improper purpose. Winston's claim succeeded in the Supreme Court of Bermuda in June 2019 but was overturned on appeal in April 2020 (Winston having by then been joined in his challenge by Tony, another beneficiary).

Winston and Tony appealed to the Privy Council, both arguing that the transfer should be set aside but for differing reasons. Winston contended that the transfer altered the fundamental character of the trust (referred to as the substratum rule). Tony argued it contravened the proper purpose rule, ie that trustees

must exercise a trust power for the purpose for which it has been granted which, Tony argued, was to benefit the Wang family.

In a judgment dated 8 December 2022, the Privy Council found that the trustees had exercised their powers for an improper purpose because the manner in which they did so deprived the beneficiaries of benefit from the trust rather than furthering their interests (which, in the case of the GRT, was the purpose for which the power was intended to be used). Therefore, the transfer of assets was found void. The judgment makes clear, however, that the decision turned on its facts. The Privy Council declined to set down any absolute rule that a power to alter the beneficial class of a discretionary trust must be used to benefit the beneficiaries.

Legler v Formannoij [2022] NZCA 607

This case has remarkably similar facts. The settlor's second wife was a trustee of the trust in question. The settlor's children challenged their stepmother's decision to appoint a corporate trustee (of which she was sole director), exclude the children and the family trust as beneficiaries, and distribute the trust fund to herself.

The High Court of New Zealand dismissed the children's claim in June 2021, and the Court of Appeal of New Zealand dismissed their appeal on 7 December 2022. The majority of the court agreed that the appeal should not succeed because the children had not proved that the stepmother was motivated by an improper purpose or otherwise intended to act against the beneficiaries' interests. They considered that the trust deed expressly permitted a self-dealing corporate trustee. The court considered it was "a logical fallacy to contend that strict compliance with the terms of the Trust Deed can amount to a fraud on a power, absent some further evidence of intention to act improperly".

One judge did dissent, however. She disagreed that the wording of the trust deed allowed the appointment of a sole corporate trustee and believed that the intention of the trust was that the children would ultimately benefit. The stepmother's actions prevented this and, in the judge's view, was therefore an improper exercise of trustee powers and appeared to be motivated by a wish to gain control of the trust for her exclusive benefit. This was not in the best interests of the beneficiaries as a whole.

The case has been appealed again and will be heard by the Supreme Court of New Zealand in October 2023.

Comment

It is striking that the Privy Council and New Zealand Court of Appeal reached different decisions on such similar facts at a similar time.

One explanation for this is simply that each case turns on its own facts and must be viewed against the backdrop of the relationships between the settlors, trustees and beneficiaries of the trust in question.

Alternatively, the two courts might indeed have considered the claims from different perspectives. On the one hand, the New Zealand courts focused on the strict wording of the trust deed to determine the scope of the trustee's powers and their proper purpose (and, by extension, whether the trustee's actions were outside that scope). On the other hand, the conclusion in *Wong* was based on the fundamental duty of the trustees to act in the interests of the Wang family beneficiaries, notwithstanding that there was a clause in a trust instrument that ostensibly permitted the trustees to act in the way they did.

Those involved in the administration of trusts will doubtless be eagerly anticipating the Supreme Court of New Zealand's decision in the final appeal of *Legler* in October.

Marcus Parker is a partner in the Trust and Probate Litigation Team at Stewarts. Marcus has over 25 years of experience both as an English lawyer and as a former Cayman-based professional trustee. He manages multi-jurisdictional disputes involving wealthy global families and their associated structures.

Judith Swinhoe-Standen is an associate in the Trust and Probate Litigation Team at Stewarts. She advises beneficiaries, trustees and personal representatives on a variety of trust and succession disputes and on matters in the Court of Protection involving those who lack capacity. She has also acted on a number of appeals to the Judicial Committee of the Privy Council from various jurisdictions.

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