

UPDATE

STAR Trusts: The Grand Court interprets the meaning of the word 'obsolete' in the *Cy-près* doctrine

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Recently, the Chief Justice of the Grand Court of the Cayman Islands, handed down his written reasons for his decision in the case of *CIBC Bank and Trust Co v (1) T and (2) S* (unreported, 16 July 2021). The decision clarifies the meaning of the word 'obsolete' in the statutory *cy-près* rule found in section 104(1) of the Trusts Act (2021 Revision) (the **Trusts Act**). It is the first time the Grand Court has been asked to consider a trustee's application to reform the terms of a Special Trusts Alternative Regime (STAR) Trust pursuant to the *cy-près* rule in section 104(1) of the Trusts Act.

Background

At common law, the *cy-près* doctrine, which developed in the context of charitable trusts, allows a Court to alter a trust's objectives, so that they can be performed as closely as possible to how the settlor intended them to be performed, in circumstances where the settled charitable objective has become impossible or impractical to achieve.

STAR trusts are a unique kind of Cayman Islands trust, established under Part VIII of the Trusts Act, which, *inter alia*, can be settled to further non-charitable purposes and/or charitable purposes and can exist for an indefinite duration because they are not subject to the perpetuity rules.¹ Section 104(1) of the Trusts Act transplants the common law doctrine of *cy-près* to the STAR Trusts regime, and allows a trustee to seek an order of the Court to reform a STAR Trust, including those without charitable purposes.

Section 104(1)(c) of the Trusts Act provides:

'104. (1) If the execution of a special trust in accordance with its terms is or becomes in whole or in part —

(a) impossible or impracticable;

(b) unlawful or contrary to public policy; or

(c) obsolete in that, by reason of changed circumstances, it fails to achieve the general intent of the special trust.

*the trustee shall, unless the trust is reformed pursuant to its own terms, apply to the Court to reform the trust *cy-près* or, if or insofar as the Court is of the opinion that it cannot be reformed consistently with the general intent of the trust, the trustees shall dispose of the trust property as though the trust or the relevant part of it has failed.'*

¹ Pursuant to section 5 and section 13 of Perpetuities Act (1999 Revision), trusts, other than STAR trusts, established on or after 1 August 1995 are subject to a statutory maximum perpetuity period of 150 years.

The Trusts

The trustee of two Cayman Islands STAR trusts (the **Trusts**) sought orders to reform the Trusts in accordance with section 104(1)(c) of the Trusts Act, on the basis that the execution of the Trusts in accordance with their terms had become obsolete due to changed circumstances.²

The Trusts were settled in 2010 for the benefit of the settlor, the settlor's second wife (**Madam S**), their son (**T**), and any children of T. The settlor passed away three years after settling the Trusts. The assets of one trust were valued at US\$ 1 billion and the assets of the other at more than US\$ 135 million. The purposes of both Trusts were described in each trust deed as follows:

'The purposes of the trust...shall be to hold the trust income and principal for the benefit of the Donor, the Donor's wife, [Madam S] (sic), the Donor's son, [T], the individual issue of such son and charitable organizations and any other beneficiaries in accordance with the terms set forth in this Agreement'.³

The trustee explained in its application that the settlor wished for the Trusts to benefit his son and his children to the maximum extent possible, regardless of their place of residence or domicile.⁴ He specifically chose to establish the Trusts in the Cayman Islands due to its *'political and economic stability, adherence to the rule of law, and the fact that Cayman is a tax neutral jurisdiction'.⁵*

At the time the Trusts were established the settlor had not contemplated that T would relocate to the US. T and Madam S had been living in the UK and had maintained residences in France, Switzerland and in T's country of birth. However, in 2018, in pursuit of business and entrepreneurial opportunities, T decided to relocate to the US and sought taxation advice about his proposal to relocate. That advice concluded that his US tax residency would cause substantial adverse tax consequences that could be substantially mitigated by the appointment of the assets onto appropriate new trusts.

Cy-près doctrine and Cayman Islands STAR Trusts

The common law meaning of *cy-près* applies to charitable trusts however STAR Trusts may be created for both charitable and non-charitable purposes. As a result, the Chief Justice undertook an analysis to consider whether the common law meaning of *cy-près* could be applied to Cayman Islands STAR trusts under section 104 of the Trusts Act. The Chief Justice noted that, *'section 104, like much else about the STAR trusts regime, is innovative because at English common law, it is long settled that there is no question of a cy-près application of property subject to trusts which are not strictly deemed charitable'.⁶* Notwithstanding this, the Chief Justice found that at common law, *cy-près* means 'as near as possible to' in the context of reform of gifts for charitable purposes and that when section 104 was drafted, it must have been intended for the provision to take on a similar meaning in the context of reform of STAR trusts.

Obsolescence

The term 'obsolete' is not defined in the Trusts Act, nor has any prior case law considered the meaning of the term in section 104 of the Trusts Act. The Chief Justice considered that its meaning could be gleaned from the surrounding words, namely that:

'a. First, the obsolescence has to be by reason of changed circumstances, i.e.: the changed circumstances have to have caused it.

b. Secondly, the execution of the trust must have become obsolete, "in that ... it fails to achieve the general intent of the special trust". The pronoun "it" is thus referring to the noun "execution" rather than the expression "special trust," so the section is concerned with the execution of the trust becoming obsolete, rather than the trust itself.

² The application was decided by the Chief Justice on 29 October 2020, however the written reasons were published in July 2021.

³ At para 20(i) and (iii).

⁴ At para 20(ii).

⁵ At para 12.

⁶ At para 25.

*c. Thirdly, the execution will become obsolete if, "it fails to achieve the general intent of the special trust." It is not the case, therefore, that the execution of the special trust has to be obsolete in the sense of being impossible or redundant. Indeed the existence of subparagraph (a) shows that this cannot be its meaning. Rather, I accept as the Plaintiff submits, that the term obsolete in section 104 means, no longer suitable for the present circumstances, or in the context of the present circumstances, or some such cognitive meaning.*⁷

The Chief Justice then considered the meaning of obsolescence in reported cases in other common law jurisdictions where it was applied in different contexts, including in relation to:

- whether a covenant was obsolete in the meaning of the UK Law of Property Act 1925, where in that context, by reference to the New Oxford Dictionary it had been found to mean 'fallen into disuse' or 'out of date' or that an 'original purpose can no longer be served'; and
- in section 62(l)(a)(ii) of the UK Charities Act 2011 in which the *cy-près* doctrine applies 'where the original purposes, in whole or in part, cannot be carried out, or [cannot be carried out] according to the directions given and to the spirit of the gift'.⁸

The Chief Justice concluded that under section 104(1)(c) of the Trusts Act, the term 'obsolescence' meant that the basic intention underlying the gift into trust, or the substance or spirit of the gift, could no longer be carried out.

Reform of the Trusts

Under section 72 of the Trusts Act, variation of the terms of a Cayman Islands trust are possible on application to the Court by any person 'having directly or indirectly an interest, whether vested or contingent under the trusts'. Section 72 therefore allows a beneficiary of a Cayman Islands trust to seek variation of the terms of the trust. However, section 72 does not apply to STAR trusts and the settlor's son could not bring an application to vary the terms of the Trusts.

The trustee's application was brought on the basis that the general intent of the Trusts could not be achieved should T become a US taxpayer, unless each of the trust deeds were reformed. The trustee therefore sought reform to the trust deeds *cy-près* to insert a provision enabling the trustee to appoint assets of the Trusts to new trusts or to distribute the Trusts' assets directly to T. The purpose of the amendment was to reduce substantially the US tax treatment of T's deemed beneficial interest in the assets of the Trusts resulting from his relocation to the US.

The Chief Justice held that section 104 does not require the Court to identify a specific intent which can no longer be achieved, but rather whether the execution of the STAR Trust fails to achieve the 'general intent', because STAR Trusts are likely to have 'a number of general or interconnected intents'. The Chief Justice clarified that as section 99 of the Trusts Act expressly permits STAR Trusts to have objects of both persons and purposes, which are charitable and non-charitable, and therefore the term 'general intent' was not the same as 'purposes'.

The Court found that the circumstances that existed at the time of settlement of the Trusts no longer existed and the extensive restructuring advice T had received from his advisors, which T had provided to the trustee, could not be ignored by the trustee. Significant US tax liabilities would arise on T's relocation to the US and the trustee was obliged to take this into consideration in the exercise of its discretion. If it did not, there was a real risk that the trustee could be found liable to a claim for breach of trust for its failure to take into account all relevant considerations in the exercise of its discretion. Importantly, though T had not yet relocated to the US, the Court was not considering a circumstance of 'prospective obsolescence' because from the point of view of the trustee's responsibilities, 'the change of circumstances had already occurred'.⁹

The Chief Justice was therefore satisfied that the execution of the trust in accordance with its terms has become obsolete, and that it could be reformed consistently with the general intent of the trust *cy-près*. Importantly, in his decision the Chief Justice stated that there was no discretion of the Court to simply

⁷ At para 24.

⁸ At paras 34 and 35.

⁹ At para 45.

refuse to exercise its power, and if it had been found that the trust could not be reformed, *'the trustee must dispose of the trust property as if the relevant part of the trust, had failed'*.¹⁰

Conclusion

The Chief Justice's reasons for his decision provide helpful guidance to trustees and enforcers of STAR trusts as to the circumstances in which an application may be brought to reform the terms of a STAR trust *cy-près*, consistent with the general intent of the trust.

STAR trusts are designed to be enduring and flexible and the decision should provide comfort to settlors, beneficiaries and enforcers of STAR trusts that they are capable of adapting to unforeseen changes in circumstances and that the Cayman Islands Courts are likely to take a pragmatic and sensible approach when considering applications to reform them.

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¹⁰ At para 51.

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