

UPDATE

Correcting the Course: Court unwinds Cayman Islands trust on settlor's application

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The Grand Court of the Cayman Islands has exercised the statutory '*Hastings-Bass*' jurisdiction by unwinding a Cayman Islands law governed trust on the application of the settlor pursuant to section 64A of the Trusts Act. This is the first time that the Grand Court's jurisdiction to set aside a trust on the ground of a fiduciary mistake has been invoked on an application by the settlor of the trust. The decision confirms the court's wide and flexible, but not unlimited jurisdiction under section 64A.

Background

The settlor (**Settlor**) settled on a trust governed by Cayman Islands law, shares he had acquired as 'sweat equity' while working overseas for a company which ultimately became public. The Settlor, who had a non-UK domicile of origin, had resided in the UK during two separate periods prior to the establishment of the trust. He had taken and relied on advice from reputable advisers as to whether upon the establishment of the trust he would be deemed domiciled in the UK for the purpose of UK inheritance tax (**IHT**).

The S Trust (the **Trust**) was established in 2012 with a view to 'beating' what was believed to be a looming domicile deadline for the purposes of IHT liability. However, in 2021, during a review of the Settlor's affairs, it was discovered that an earlier period of UK residency had been overlooked. As a result, the Settlor was potentially liable to IHT when the Trust was settled and became liable to pay IHT immediately rather than upon his death.

The Settlor, who was also a beneficiary of the Trust, applied under section 64A of the Trusts Act (2021 Revision) to set aside the establishment of the Trust and all ancillary transactions associated therewith and for an order that all assets held on the terms of the Trust were held by the Trustee on bare trust for the Settlor. The Settlor applied on the basis that, had the true position been known, taking into account the implications of the Settlor's earlier period of UK residency, the trustee of the Trust (the **Trustee**) would not have agreed to establish the Trust and receive the trust assets onto trust. This position was supported by the Trustee's evidence.

Section 64A of the Trusts Act

By way of reminder, the so-called rule in *Hastings-Bass* is a traditional equitable jurisdiction of the court to set aside the exercise of fiduciary powers on the grounds of inadequate deliberation. This 'rule' was substantially narrowed by the UK Supreme Court (**UKSC**) in *Pitt v Holt*, where the UKSC held that for the exercise of power to be set aside the inadequate deliberation on the part of the trustee must amount to a breach of fiduciary duty. Relief was not available where the trustee had simply acted on professional advice that turned out to be wrong.

The Cayman Islands legislature enacted section 64A to preserve the flexibility of the traditional equitable jurisdiction of the court that existed prior to the UKSC decision in *Pitt v Holt*.¹ Section 64A of the Trusts Act

¹ *Hastings-Bass (deceased), Hastings and Others v Inland Revenue Commissioners* (2013 UKSC 26). See our previous update on section 64A of the Trusts Act: [Mourant: Law Firm | Correcting trustee mistakes: Hastings-Bass in the Cayman Islands](#).

permits the court to set aside decisions made in an exercise of fiduciary power on the grounds that, in the exercise of the power, the person who holds the power did not take into account one or more considerations that were relevant to the exercise of the power, or took into account irrelevant considerations, and without any requirement to establish that the fiduciary acted in breach of trust or in breach of fiduciary duty. The court's jurisdiction is expressly stated to be exercisable on the application of the holder of the fiduciary power, a beneficiary, the enforcer in the case of a STAR trust, the Attorney General in the case of a charitable trust, or, with the leave of the court, 'any other person'. There is no express basis for the jurisdiction to be exercised on the application of the settlor.

Decision

This was the first case before the Grand Court where the applicant was a settlor of the relevant trust. The Settlor, by virtue of being also a beneficiary of the Trust, clearly had standing to apply for relief under section 64A(5)(b) of the Trusts Act.

There was a flirtation by counsel for the Settlor with the concept that a settlor could also be construed as the holder of a fiduciary power within the section 64A definition of '*fiduciary power*', which is, '*any power that, when exercised, must be exercised for the benefit of or taking into account the interests of at least one person other than the person holding the power.*' The judge, having considered the traditional origins of the concept of a fiduciary power, which would no doubt require an identifiable donor and donee of the power, did not feel it necessary to explore in detail that concept of a settlor, qua settlor, as fiduciary. He was satisfied that the Trustee's decision to establish the Trust and accept the assets to be held on trust constitutes an exercise of fiduciary power within the meaning of section 64A. The Grand Court held that there was nothing in the language of section 64A which would limit its application to all transactions carried out by fiduciaries after the founding assets were received by the trustee.

The Grand Court was satisfied that had the Settlor's earlier period of UK residency been known, the Trustee would not have agreed to establish the Trust and receive the Trust assets. The Grand Court ordered that the Trust be set aside *ab initio* and all assets held on the terms of the Trust reverted to the Settlor. Certain specific asset transactions that were ancillary to the establishment of the Trust were also set aside.

In an earlier decision *Re Settlements made by Declarations of Trust dated 9 May 2023*,² the Grand Court suggested an additional implied requirement that relief under section 64A can only be obtained where the applicant has acted in good faith in relation to the impugned transaction and has not deliberately pursued a course of conduct designed to gain some undisclosed and impermissible onshore tax advantage or to procure any other improper benefit. This would require that the applicant cannot be pursuing a course of conduct to obtain an impermissible onshore tax advantage or other improper benefit. The application in this case was made on the basis that this additional requirement for granting relief had to be met. In exercising its discretion, the Grand Court held that the Settlor had acted in good faith in both establishing the Trust and pursuing the application to have it set aside on notice to the relevant UK tax authorities.

This decision demonstrates the flexibility of the court's jurisdiction conferred by section 64A of the Trusts Act. The Grand Court, once satisfied that the statutory prerequisites have been met, will interpret the jurisdiction to give it the full degree of flexibility that was intended when the provisions were introduced. This includes the willingness to unwind the very establishment of a trust. Even so, the court continues to acknowledge a good faith requirement on the part of those who seek to invoke the jurisdiction. Such a limitation, although never previously applied in practice, is no doubt reasonable and practical.

² (Unreported, 28 September 2023, Kawaley J).

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