The Rule in Hastings- Bass:

Help for Trustees who Make Mistakes

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Introduction

There is a Confucian proverb that runs something like this :

"A man who has committed a mistake and doesn't correct it, is committing another mistake."

With the advent of the Rule in Hastings-Bass, a trustee who makes a mistake can, in certain circumstances, effectively undo the past, wiping the slate clean so that he can start anew and get things right the second go-round.

The Decision in Hastings-Bass

The Rule (or Principle, as it is usually referred to) is taken from the decision in Re Hastings Bass in the English Court of Appeal in 1975.

In that case, the trustees of a settlement exercised, or purported to exercise, the statutory power of advancement to transfer funds to another trust. Their aim in doing so was to avoid the payment of estate duty. At the time of the transfer, the trustees did not know that there would be any

infringement of the perpetuity rule as, in fact, there turned out to be in relation to at least a part of the sub-trust to which the transfer had been made.

On the facts of the case, it was clear that the trustees had indeed thought that what they were doing was the right thing. They had acted in good faith. They had honestly thought that what they were doing was for the benefit of the beneficiary. Moreover, they did not think for a moment that it was not within their power to act as they had. More specifically, they were not aware that there might be any violation of the rule against perpetuities.

At any rate, it fell to be decided whether the trustees had validly exercised the power of advancement.

In rendering his decision in the Hastings-Bass case, Lord Justice Brown articulated what has since come to be known as the Rule (or Principle) in Hastings- Bass. He did so in these terms :

"Where a trustee is given a discretion as to some matter under which he acts in good faith, the court should not interfere with his action, notwithstanding that it does not have the full effect which he intended unless 1) what he has achieved is unauthorized by the power conferred on him or Where he has acted outside of the power conferred on him or 2) it is clear that he would not have acted as he did a) had he not taken into account considerations which he should

not have taken into account or b) had he not failed to take into account considerations which he ought to have taken into account."

In Hastings-Bass, the court was satisfied that the trustees must have given consideration to the estate duty-saving aspect of the sub-settlement and, further, that they must have duly considered whether the sub-trust would be for the benefit of the beneficiary. Moreover, since the failure of the sub-trust did not decrease the element of direct benefit to the beneficiary, the trustees had, in fact, addressed their minds to the relevant considerations.

In the result, the relevant part of the advancement was held to be valid, and exempt from estate duty as well.

Ironically, therefore, the original Hastings-Bass case was a case in which the trustees – and ultimately the beneficiaries – benefited from the Court of Appeal's decision that the rule did not apply on the facts of the case.

The test -"might have" or "would have"

The Rule in Hastings-Bass was comprehensively re-stated in 2005 in Sieff v Fox[1] in which Lord Justice Lloyd made the rather fine distinction between :

[1] [2005] 3 All ER 693

(a) situations where trustees are free to decide whether or not to exercise the discretion as opposed to;

(b) situations where the trustees are obliged to exercise their discretion.

It was suggested in Sieff that in the case of (a), namely, where a trustee is free to decide whether or not to exercise his discretion, a more stringent test applied, namely, that for relief under the rule in Hastings-Bass to apply, it must be shown the trustee would have acted differently had he not taken into account irrelevant considerations.

In the case of (b), however, that is to say, where a trustee is not free to decide whether to exercise his discretion, a more relaxed test is applied: the question then is whether he might have acted differently had he not failed to take into account relevant considerations, or taken into account irrelevant considerations. In cases of this particular kind, those who seek relief under the Rule in Hastings-Bass will therefore have an easier road to travel.

The Rule Applied

Since the original Hastings-Bass decision, the rule has been used to set aside, and thus effectively reverse, the exercise of powers in a variety of circumstances but most especially where the exercise of the relevant power has resulted in unintended tax consequences. In fact, the frequency

with which the Hastings-Bass Rule is now being invoked in the UK represents a worrisome trend for Her Majesty's Revenue and Customs which, as a result, has indicated that it will likely intervene more frequently in future cases in which the Hasting-Bass rule is invoked by those who seek to nullify or reverse trustee decisions that have created a significant tax exposure.

A recent case along those lines is Burrell v. Burrell[2] in which the trustees of a settlement sought to set aside a part of a deed of appointment. In entering into the deed, the Trustees had relied on the advice of a solicitor that it would be beneficial to do so from a tax perspective. They failed to appreciate, however, that the appointment would, in fact, have a diametrically opposite effect. Indeed, it would produce absolutely horrendous inheritance tax consequences for the trust under UK law.

Applying the Rule in Hastings-Bass, however, it was held by the court that a relevant consideration for trustees must surely be the fiscal consequences of their actions. In the case under consideration, it was clear that the trustees had failed to appreciate the tax consequences of the deed of appointment. Had they appreciated that the appointment would have operated the way it did, they would surely have acted differently. More specifically, they would not have made the appointment at all.

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[2] Burrell v Burrell [2005] EWHC 245

In the result, on the basis of the Hastings-Bass rule, the deed of appointment was declared invalid. And in the result, the tax disaster was avoided.

Two other recent cases involving the application of the Hastings-Bass merit special mention if only because they demonstrate the adaptability of the rule to a variety of trustee mistakes:

- One is a case where trustees incurred a large capital gains tax liability because they had overlooked the advice of senior counsel that a strict timetable needed to be observed in relation to the execution of a deed of appointment[3] ; and

- The second is a case where the trustee had mistakenly appointed 60 per cent of the trust fund to the settlor's son when, in fact, the settlor had instructed that he appoint only 40 per cent.[4]

The rule in Hastings-Bass has therefore demonstrated a vitality and versatility in its relatively short life to date.

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[3] Abacus Trust Co v National Society of Prevention of Cruelty to Children [2001] WTLR 953.

[4] Abacus Trust Co v Barr [2003] Ch 409

Although most of the case-law is coming out of England, it bears noting that the Rule has gained acceptance in offshore jurisdictions as well, most notably Jersey and the Cayman Islands[5].

Criticism and Justification

Needless to say, however, the increasing resort of trustees to the rule has introduced a great deal of uncertainty as to the finality of trustee decision-making. Indeed, what may appear to be a final decision by trustees on a particular matter today may be unwound tomorrow, on the trustee's own initiative, almost as if it had never occurred at all, if a serious mistake is discovered to have been made.

Predictably, professional trustees have not been slow in welcoming this new addition to its defensive arsenal. The prospect of being able to go back to square one, as it were, and wipe the slate clean and start afresh as if the original decision had never been, can be a source of great deal of reassurance and comfort for trustees who operate in an increasingly litigious, high-exposure, environment .

Not surprisingly, however, there has been a counter-thrust to this emerging jurisprudence. Indeed, the Hastings-Bass rule has instigated not only a great deal of academic debate but an increasing amount of judicial

[5] Barclays Private Bank & Trust (Cayman) v. Chamberlain (2005, unreported); A v. Rothschild Trust Cayman Ltd (2006) WTLR 1129

skepticism – even condemnation – as well. It has been alternately described as both revolutionary and reprehensible.

No less a person than Sir Robert Walker, as he then was, in a hard-hitting speech entitled **The Limits of the Rule in Hastings-Bass**, has even gone so far as to say this :

"The unrestrained extension of the Hastings-Bass principle could lead to trustees being treated as a new class of incapacitated persons, like children or feeble minded adults. No one could ever be sure that they had taken proper advice (even…if they had teams of expert advisers) or that they meant what they said. Huge uncertainty would arise, especially as each doubtful decision would tend to have a knock-on effect making analysis of later decisions much more difficult…."

The Rule and Exoneration Clauses

Whatever the justification for the rule may be and however uncertain its ultimate limits may turn out to be, it should perhaps not be forgotten that professional trustees are already insulated to a great degree by the generous exculpatory clauses that have long been the industry norm in jurisdictions such as ours. As is well known, these clauses typically exempt trustees from every liability for just about every sin under the sun except fraud and wilful misconduct. Moreover, it bears noting that the validity of such clauses has been specifically upheld in the Bahamas in such leading cases as Roywest v. Savannah.

One may therefore ask, of what practical use is the rule in Hastings-Bass where trustees are already well insulated by exoneration clauses of the standard kind to which I have referred.

The short answer is the trustees can use the Hastings-Bass rule preemptively (as opposed to reactively which is necessarily the case with exoneration clauses), that is to say, the trustees can apply to the court to undo a mistake before aggrieved beneficiaries invoke the rule themselves. They can also apply preemptively where they reasonably apprehend that claims will be made against them by beneficiaries for some mistake that has been discovered to have been made. In such cases, the trustees need not wait to rely on an exoneration clause in their defence. Instead, they can seize the initiative and dash off to court with a view to straightening things out before any action is instituted against them.

It also bears noting that since an exoneration clause will often exempt a trustee from liability for simple (or even gross) negligence, the rule in Hastings-Bass may even operate to assist beneficiaries in undoing the negligent acts of the Trustee in circumstances where the trustees may be disinclined to take the initiative because they know that they are already sheltered from personal liability.

The Rule and Rectification

One question that has come up is how Hastings-Bass relates to the remedy of rectification. It should be said at once rectification is much more limited in scope. In rectification, the "intention" of the parties is of paramount importance. Rectification can only be obtained where the instrument in question does not express the real intention of all the parties. In Hastings-Bass, there is no such requirement for mutuality of intention.

Moreover, Rectification is primarily concerned with correcting documents that fail to reflect the true intention of the parties. The application of the rule in Hastings-Bass, on the other hand, does not depend on whether the mistake in question has been embodied in any document or not.

Even more fundamentally, the Hastings- Bass rule may be applicable in cases where a trustee has acted without considering certain crucial questions at all whereas rectification usually only arises in cases where the relevant matters have indeed been fully considered but the relevant document erroneously expresses, or incorrectly carries into effect, what was duly considered and decided.

In addition, it has been suggested in at least one case[6] that there may indeed be a lighter burden of proof for those who seek relief based on the

[6] Mettoy Pensions Trustees v Evans[1990] 1WLR 1587

Hastings-Bass rule than would be the case for those who seek rectification of an instrument.

Cost Implications to Trustees

Lest I give you the false impression that the rule allows trustees to escape scot-free from all liability for mistakes, trustees may still be required in certain circumstances to personally bear the costs of a successful application to set aside their own decisions, rather than having those costs met from the trust fund.

In one case[7], having made an application to the court to determine the validity of a deed, the trustees, acting in their own self-interest, adopted an approach to the application that was considered by the court to be contrary to the interests of the successful beneficiary. In the result, the trustees were not allowed their costs out of the fund.

Trustees should therefore be mindful of this possible costs-exposure lest they be seduced into thinking that all is rosy and good when it comes to Hastings-Bass.

Uncertainty on the Limits of the Rule

[7] Breadner v Granville-Grossman [2000] 4 All ER 705

Moreover, it should not be thought that the Rule applies to any and very kind of mistake that a trustee makes. Although the limits of the rule have yet to be definitively established, it is clear that it does not, for example, apply to situations where the trustee has failed to act at all.

If a Trustee, having a power, fails to exercise it at all, thereby creating a tax exposure or some other financial loss for the trust or its beneficiaries, Hastings-Bass will not be available to cure the trustee's mistake in failing to exercise the power at all.

The case of Breadner and others v Granville-Grossman[8] illustrates this well. There the trustees purported to exercise a power of appointment outside of the period within which it was exercisable, thereby rendering the appointment void, as fully as if the trustee had never made it at all. The learned judge in the case declined to validate the appointment, saying instead:

"the court may undo something which the trustees have done but will stop short of doing something which the trustees might have done but did not do".[9]

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[8] See cite above

[9] Breadner see above

It should also be noted that the Hastings-Bass principle does not apply to the power to appoint new trustees[10]. In such a case, the trustees can only on the exoneration clause contained in the trust deed, if there is one.

The Future?

Despite the criticisms of the rule, there can be no question that the Hastings-Bass principle represents a powerful new addition to the menu of remedies available to trustees and beneficiaries alike for the reversal of the consequences of human error.

While there does not yet appear to have been a case in the Bahamian courts in which the rule has been specifically applied, there is little doubt that the rule would indeed be applied in much the same way as it is now being applied in England and in jurisdictions such as the Cayman Islands.

The rule will no doubt continue to evolve but within the framework of limitations and exceptions that will over time have the cumulative effect of narrowing its scope and applicability. Hastings-Bass is likely to suffer such a fate as judges attempt to strike an appropriate balance between the need for certainty and finality in the making of decisions by trustees, on the one hand, and the need to retain judicial flexibility to correct

[10] Sieff v Fox[2005] EWHC 1312 (Ch) UnderHill & Hayton

mistakes which would do grave injustice to beneficiaries if permitted to stand.

Exactly where that balance will be struck is anybody's guess but I suspect that the rule will, in the short term, continue to expand, perhaps even aggressively so, only to meet up with increasing resistance that will likely translate into some legislative curbing of the rule or, more probably, a more conservative judicial reaction that will cause the rule to contract over time.

Trustees would therefore be well advised not to allow the availability of the rule in Hastings-Bass to induce a relaxation of the kind of thorough, careful, well-informed analysis that should underpin the decision-making process.

After that, that is what trustees, especially professional trustees, are being paid for.