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CASE COMMENTARY

EXEMPTING A TRUSTEE FOR GROSS NEGLIGENCE

Spread Trustee Company Ltd v Hutcheson Privy Council [2011] UKPC 13

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Can an exemption clause exclude a trustee's liability for gross negligence? That was the question which the Privy Council was required to consider in this appeal from the Guernsey Courts. Guernsey has developed substantial activities in finance and trusts, and now has legislation (the Trusts (Guernsey) Law 2007) creating a legal framework for this business. The legislative framework was first introduced in 1989, and amended in 1990. The effect of an exemption clause had never been considered in litigation in Guernsey prior to the introduction of legislation. The Trusts (Guernsey) Law 1989 section 34(7) provided:

“Nothing in the terms of a trust shall relieve a trustee of liability for a breach of trust arising from his own fraud or wilful misconduct.”

That provision was amended by the Trusts (Amendment) (Guernsey) Law 1990 by adding “or gross negligence”. The 2007 Law contains a provision which is in substantially similar terms to the 1989 Law as amended. In *Spread Trustee Co Ltd v Hutcheson*¹ the acts and omissions on the part of the trustees took place over a number of years. The relevant trust instruments contained an exclusion clause and the Privy Council had to decide whether or not it was effective to exclude liability for gross negligence in respect of the matters arising before the coming into force of the 1989 and 1990 Laws. The Board was unanimous in finding that the legislation did not operate retrospectively. However, the Board was divided over whether under the customary law of Guernsey it was not possible to exempt trustees from liability for gross negligence. The Privy Council concluded by a majority that the customary law of Guernsey would have followed English Law, and that the Guernsey

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¹ [2011] All ER 51.

CASE COMMENTARY

courts, if the question had arisen before 1989, would or should have come to the same conclusion as the Court of Appeal in *Armitage v Nurse*,² which correctly states English law. There was therefore nothing in Guernsey law, prior to legislative change, which prevented the exclusion of liability for gross negligence.

THE ISSUES

The claimants were beneficiaries under two settlements set up in November 1977 who alleged they were entitled to compensation of £53.5 million, including interest, for losses arising from failures on the part of the defendant, a professional trustee company, and the previous trustees. The beneficiaries claimed that the defendant was grossly negligent in its investment policy and in failing to investigate breaches by the previous trustees. Each settlement contained an exclusion clause, exonerating the trustees from liability for losses to the trust fund except in the case of wilful and individual fraud and wrongdoing on the part of the trustee sought to be made liable. The defendant claimed this protected it from any liability for breach of trust resulting from its gross negligence. The question to be determined as a preliminary issue was whether Guernsey law prohibited the exclusion of liability for gross negligence for breaches of trust arising before February 19th 1991 (being the date the 1990 Amendment Law came into force) and if it did, whether the prohibition applied to breaches arising prior to April 22nd 1989 (being the date the 1989 Law came into force).

ROYAL COURT OF GUERNSEY

The case first came before the Lieutenant Bailiff Sir de Vic Carey. In his view, it had never been possible for a trustee to exclude liability for gross negligence under Guernsey Law. He believed that the provisions dealing with exclusion clauses in the 1989 Law, as amended in 1990, were declaratory of Guernsey law. The policy letter³ introducing the 1989 Law proposed legislation broadly on the lines of earlier legislation passed in Jersey, and the legislation actually introduced was similarly worded. That demonstrated that the enactment of Guernsey Trust Laws arose from a desire to keep in step with Jersey. The original Jersey law of 1984 did not refer to exclusion of liability for gross negligence, but was amended to cover this aspect of liability in 1989. The Jersey Court of Appeal in *Midland Bank Trust Co (Jersey) Ltd v Federated Pension Servs*⁴ had considered obiter that the aim of the legislature

² [1997] 2 All ER 705.

³ *Billet d'État* No.IX of 1988, Art VI.

⁴ 1995 JLR 352 (the *Midland Bank Trust* case).

in amending the 1984 Law was to clarify, rather than to change, the provisions, and that therefore the 1989 Jersey Amendment Law had effect in relation to breaches taking place between the two Laws. The Lieutenant Bailiff considered that, even though the Jersey decision had only persuasive force, the statement in s 18(1) of the 1989 Guernsey Law, which provides that a trustee “shall, in the exercise of his functions, observe the utmost good faith and act *en bon père de famille*” was declaratory of the existing law, and the same was true of s 34(7) dealing with exclusion clauses. The amendment made in 1990 was only a minor change of emphasis. Acting with gross negligence in the discharge of one’s duties as a trustee could not be compatible with acting *en bon père de famille*. He said: “I further cannot see how any clause in a trust deed completed before 1989 which purported to discharge a trustee from liability to the trust for failures to act *en bon père de famille* could have been upheld by the court.”⁵

COURT OF APPEAL (GUERNSEY)

The Trustee appealed to the Guernsey Court of Appeal,⁶ and once again the preliminary issues were answered in favour of the claimant, but for different reasons. The Guernsey Court of Appeal said that the proper approach to construction of the two Laws was firstly to investigate the customary law of Guernsey before the enactment of the 1989 Law. The law of trusts in Guernsey comprised a mixture of English and customary principles and even though the rules had generally advanced further in England than in other jurisdictions, they would not be applied where they were inconsistent with Guernsey law. The court considered both *Midland Bank Trust* and *Armitage v Nurse*, pointing out that both cases had been decided after the 1989 Law had been introduced. In *Midland Bank Trust* the Jersey Court of Appeal had reviewed a series of mainly nineteenth and early twentieth century Scottish cases and concluded that they could all be regarded as decisions on the construction of the relevant exclusion clause, a conclusion with which Millet LJ in *Armitage v Nurse* agreed. The Guernsey Court of Appeal did not agree, and thought the cases laid down a clear rule of law that no exoneration clause could exclude liability for fraud or gross negligence. The Court pointed out that The Scottish Law Commission had come to same view, saying:

“In our view... the Scottish law on immunity clauses remains as stated in the 19th century cases. Gross negligence or gross breach of duty is

⁵ 2009-10 GLR 197 at 215 [52] (the paragraphing referred to in the Privy Council report is different from that in the official Guernsey Law Report).

⁶ 2009-10 GLR 403.

CASE COMMENTARY

regarded as tantamount to dole or fraud and cannot be excused : *culpa lata dolo aequiparatur*.”⁷

The Court noted that prior to *Armitage v Nurse*, which held that it was permissible to exclude liability for gross negligence, English law was uncertain. The English Law Commission thought in 1992 that gross negligence might not be excluded, saying:

“Beyond this, trustees and fiduciaries cannot exempt themselves from liability for fraud, bad faith and wilful default ... It is also not altogether clear whether the prohibition on the exclusion of liability for ‘wilful default’ also prohibits exclusion of liability for gross negligence although we incline to the view that it does.”⁸

The Court concluded that the conclusion reached in *Armitage v Nurse* was inconsistent with Guernsey customary law. Millett LJ had rejected the suggestion that a duty to act without gross negligence was one of the core obligations of trustees, but his decision should not be applied. He had been mistaken in his view of the Scottish cases; his rejection of gross negligence as a civilian concept alien to the common law carried no weight in Guernsey, with its mixed English and Norman law ancestry;⁹ and the clear position in Scottish law would, in Guernsey, have been adopted in preference to the uncertainty in English law. The report¹⁰ put before the States (the legislature) highlighted the fact that the roots of Guernsey law lay in Norman customary law, and the Lieutenant Bailiff had rightly attached significance to the obligation of a trustee to act *en bon père de famille* which is a phrase derived from French law with no place in English law, even if it can be equated with the standard of care required of trustees in England, viz to act a prudent man of business. The Guernsey Court of Appeal could find nothing to suggest that the 1989 Law was intended to take a different view with regard to exclusion clauses than the Court had taken with regard to customary law. The fact that the Law had not referred to gross negligence was only a mistake which was corrected by the 1990 Amendment. The change could not have been seen as significant because the report¹¹ preceding the 1990 Law talked only of making

⁷ *Discussion Paper on Breach of Trust*, September 2003 (Discussion Paper No. 123), para 3.16 at 19.

⁸ *Fiduciary Duties & Regulatory Rules: A Consultation Paper* (Law Com No 124), para 3.3.41, at 105.

⁹ 2009-10 GLR 403 at [32]-[33] citing Millett LJ [1998] Ch. at 250 at 253-254. The Court also observed that gross negligence was in fact recognised in English law for some purposes including manslaughter and bailment.

¹⁰ Report dated 12th February 1988 of the States Advisory & Finance Committee.

¹¹ Report dated 16th March 1990 of the States Advisory & Finance Committee.

“minor technical amendments.” Thus the effect of the 1989 and 1990 Laws was to confirm the position that in Guernsey law, a trustee exoneration clause could not exclude liability for gross negligence. The question of retrospectivity did not therefore arise in respect of either Law, but if it had had to decide the matter, the Court would have held that neither Law had retrospective effect.

PRIVY COUNCIL

The trustee appealed to the Privy Council, the majority of whom (Lord Clarke, Lord Mance and Sir Robin Auld)¹² held that clauses excluding liability for gross negligence were effective in Guernsey law until prohibited by the 1990 Law. The 1989 Law was clear: “a trust could not lawfully include a term excluding the trustee’s liability for breach of his obligation to act *en bon père de famille* arising from his own fraud or wilful misconduct.”¹³ It was implicit in this express prohibition that the Law permitted a trustee to exclude liability for other causes, in particular negligence and gross negligence. The Court of Appeal had been wrong to hold that the omission of gross negligence in the original form of s 37(4) was a mistake. Firstly there was no evidence to support that conclusion. Secondly, the majority of the Board was of the view that the 1990 amendment was intended to follow the relevant change to the Jersey Law of 1984 because it employed almost identical terms.¹⁴ Moreover, since the Jersey Law in its original form contained no provision at all which expressly set out the extent to which a Jersey trust could exonerate a trustee, the inclusion of limits on exoneration clauses in the Guernsey Law of 1989 must have been the result of a considered decision about what to allow and what to prohibit. The failure to prohibit exclusion of liability for gross negligence was not a mistake. The beneficiaries therefore lost their arguments based on statutory interpretation.

The question remained of what the position was in Guernsey customary law prior to the 1989 Law, and this is the question of most interest to English lawyers. The majority in the Privy Council held that the Court of Appeal was wrong in concluding that before 1989 the Guernsey courts would have followed Scottish Law in preference to English law.¹⁵ The Board accepted that there was a rule of Scottish law or policy to the effect that no trustee

¹² Lord Clarke delivered the opinion of the Board; Lord Mance and Sir Robin Auld gave concurring opinions.

¹³ [2011] UKPC 13 at [21].

¹⁴ *Ibid* at [25]-[34] (Lord Clarke); at [118] (Sir Robin Auld).

¹⁵ Sir Robin Auld at [127] thought that the question was not what a court *would* have decided, but what it *should* have decided, but his conclusion was the same.

CASE COMMENTARY

could be exonerated in respect of fraud or gross negligence.¹⁶ It also entirely accepted that Guernsey looked to other jurisdictions for assistance in developing particular areas of law. In the case of trusts, however, the position in English law was the usual starting-point. While this would not be imported wholesale and would yield to Guernsey customary or statute law, there was no specific Guernsey customary law with regard to exclusion clauses and there was no evidence that Guernsey had at any stage looked at the law of Scotland.

So, what would the Guernsey courts have discovered if they looked to English law? “It seems to the Board to be much more likely than not that a Guernsey lawyer or judge or the Board itself, considering the position under English law before 1989, would have looked at the cases cited by Millett LJ and would have reached the same conclusions as he did.”¹⁷ The Board did not think it important that Millett LJ differed on the interpretation of Scottish law. His view that negligence and gross negligence differed only in degree was not negated by examples in which English law recognised gross negligence because there was still a difference between both types of negligence and fraud.¹⁸ Finally, even if for some purposes in systems drawing on Roman or classical principles gross negligence could be equated with fraud, that was not relevant to the interpretation of English law. There was no rational basis for drawing a distinction between liability for negligence and gross negligence,¹⁹ and any such distinction would have had to be made by statute, as was done in Guernsey by the 1990 Law. The Board agreed with the Court of Appeal that the 1990 Law did not apply to breaches of trust before it came into force, and the same was true of the 2007 Law.

Lord Mance, in a concurring opinion with which Sir Robin Auld agreed, raised the possibility that, for the purposes of applying exemption clauses, fraud might be interpreted as including cases where fraud was interpreted objectively, as it was in *Walker v Stones*.²⁰

DISSENTING OPINIONS

Neither of the dissenting opinions agreed with the majority that the Guernsey courts, prior to 1989 would have reached the same conclusion about

¹⁶ Lady Hale and Lord Kerr (dissenting) agreed on this point: [2011] UKPC 13 at [133]. Lord Mance, in a concurring opinion, was doubtful, leaning to the view that the Scottish cases were based upon the construction of the exemption clauses concerned rather than applying “an absolutely inflexible rule, effectively one of public policy” precluding exemption of liability for gross negligence: at [108].

¹⁷ [2011] UKPC 13 at [57].

¹⁸ A view emphatically endorsed by Sir Robin Auld in his concurring opinion: [2011] UKPC 13 at [117].

¹⁹ [2011] UKPC 13 at [62] (Lord Clarke) and at [124] (Sir Robin Auld).

²⁰ [2001] QB 902.

exemption clauses as that reached subsequently in 1997 by Millett LJ in *Armitage v Nurse*. This is unsurprising given the contrary conclusion reached in the Guernsey courts in this case, and the various doubts which have been expressed about *Armitage v Nurse*.²¹

Lady Hale pointed out that the Board had upheld a decision of the English Court of Appeal which had never been considered by the Supreme Court, and the Board should have been slow to depart from the views of the two lower courts of Guernsey, when to do so might pre-empt consideration of the issue in the English courts.²² Before *Armitage v Nurse* there had been considerable uncertainty about the law,²³ and the view of the Law Commission that it was not possible to exclude liability for gross negligence was based upon thorough research.²⁴ Predictions by the Law Commission could be wrong, and so it proved with *Armitage v Nurse*.²⁵ But the decision had been subject to immediate criticism, and in 1999 the Trust Law Committee²⁶ thought the force of the decision was diminished by the court's apparent view that it had to decide between outlawing or accepting *all* negligence clauses rather than considering whether to *only* outlaw exemption for gross negligence despite a long line of authority distinguishing the two.²⁷ Lady Hale also noted the view of the Law Commission, in its examination in 2002 of the current law and practice of trustee exemption clauses in England and Wales:

“It must be admitted that the authority of *Armitage v Nurse* ... is not entirely free from doubt. The view taken of the nineteenth century Scottish cases does not accord with the understanding of these decisions north of the border... While there is no reason why the English and Scottish law should be identical in this respect, the reliance placed by Millett LJ on the Scottish cases was clearly an important part of his reasoning, and should that reliance be shown to have been misplaced, the authority of the decision may thereby be called in question.”²⁸

²¹ See Lady Hale's explanation below of some of these doubts.

²² [2011] UKPC 13 at [129].

²³ *Ibid* at [130].

²⁴ *Ibid* at [132].

²⁵ *Ibid* at [135].

²⁶ The Trust Law Committee's Consultation Paper on Trustee Exemption Clauses, para 2.8.

²⁷ [2011] UKPC 13 at [135].

²⁸ *Trustee Exemption Clauses: A Consultation Paper* (Law Com No 171), para 2.54, at 19.

CASE COMMENTARY

Lady Hale said that nothing could be concluded from the fact that the Law Commission in its later Report on Trustee Exemption Clauses²⁹ did not recommend legislation. That did not mean that a higher court might not subsequently take a different view of the law. Since opinion about *Armitage v Nurse* was divided, it was open to the Guernsey courts to find that, given their jurisdictional heritage, and the differently expressed duty of trustees, liability for gross negligence could not be excluded. The Privy Council should not interfere with their decision to reach that conclusion.

Lord Kerr agreed that English law before 1989 was uncertain, although there was an ample basis for advice that it was *probably* permissible to exempt a trustee from liability for gross negligence.³⁰ However, he pointed out that no investigation of the public policy arguments was undertaken in *Armitage v Nurse* although Millett LJ had expressed concern about the propriety of professional trustees excluding liability for everything except actual fraud. The Scottish cases demonstrated that culpa lata (gross negligence) by a trustee could not be exempted in a trust deed, and there was a sufficient basis for the Guernsey Court of Appeal to conclude that this line of authority would have been applied than the less defensible English law. This was not, though, the principal basis for the Guernsey courts' decision, which was that the fundamental obligation of a trustee to act *en bon père de famille* gave rise to fiduciary obligations different from those in English law.³¹ He said:

“Ultimately, it appears to me that the notion of exempting from liability a trustee's gross negligence is not only inimical to the fiduciary duty that he owes to the beneficiary under Guernsey law, it is wholly destructive of the essential feature of the relationship between the two.”³²

The Scottish cases the Guernsey court followed were based on similar reasoning.

COMMENTARY

Trusts are a creation of English law, and it is natural to assume that in cases of uncertainty in other jurisdictions, English law can provide a useful, even if not conclusive, guide. There is also value in achieving some harmony between different jurisdictions in areas like trusts and finance where

²⁹ Cm 6874 (2006).

³⁰ [2011] UKPC 13 at [163].

³¹ A view which was rejected by the majority at [11] and [61].

³² Ibid at [177].

international transactions are commonplace.³³ However, the value of English law as a guide to the resolution of uncertainty is surely diminished where English law itself is uncertain and controversial, as it is in relation to trustee exclusion clauses, and certainly was prior to the decision in *Armitage v Nurse*. That was recognised in the minority opinions, but appears to have had little effect upon the majority. Reconstructing the past is never easy, and it is even harder to decide how a question which was never asked in the past might have been answered then. It is, of course, not open to a judge to leave the question unanswered when it is essential to the outcome of the litigation. The detailed consideration by the majority of the conclusion in *Armitage v Nurse*, and its endorsement of it, may be seen as an indication of how the decision will be treated if the question of trustee exclusion clauses reaches the Supreme Court. However, the dissenting opinions leave continued uncertainty, and the respect traditionally shown for decisions of the Privy Council by no means guarantees that the same view will necessarily be taken in domestic English courts.³⁴ Moreover, despite the endorsement of *Armitage v Nurse*, some ammunition is given to its critics. For instance, Millett LJ was convinced that the Scottish cases could be treated as based upon the interpretation of the exclusion clauses used in the cases concerned. All but one of the judges in the Privy Council in this case take a different view and accept that the Scottish cases establish a rule of law that trustees cannot be exempted from liability for gross negligence.

There can be sound reasons of policy why the law varies from jurisdiction to jurisdiction. The decision of the majority of the Privy Council aligns Guernsey law with English law only in respect of acts or omissions by trustees prior to the coming into force of the Trusts (Amendment) (Guernsey) Law 1990. Since that date, the law in the two jurisdictions is different, for one or both of two reasons. The first is that there may be a more significant difference between the concepts of *en bon père de famille* used in Guernsey and that of the prudent man of business as tests for the standard of a trustee's conduct than the Privy Council appears to have believed.³⁵ A man of business

³³ M Kirby "Of Advocates, Drunks and Other Players: Plain tales from Australia" [2011] Denning LJ 47-64; *Breakspear v Ackland* [2008] EWHC 220 at [32].

³⁴ See *Sinclair Investments (UK) Ltd v Versailles Trade Finance Ltd* [2011] EWCA Civ 347 (doubting *AG for Hong Kong v Reid* [1994] 1 AC 324).

³⁵ Lord Clarke indicated that he thought there was no identifiable discernable difference between the nature and extent of a trustee's duty to act with reasonable care in all the circumstances and a duty to act *en bon père de famille*: [2011] UKPC 13 at [20] and [39] as explained by Sir Robin Auld at [123]. Sir Robin Auld dismissed all the beneficiaries' arguments to the contrary: [2011] UKPC 13 at [121]-[124]. Lady Hale agreed that the duty to act *en bon père de famille* was "clearly equivalent to the duty ... to act as a prudent man of business" at [139]. Only Lord Kerr considered that there was a distinct difference: at [176].

CASE COMMENTARY

is more likely to be prepared to take risks than a *bon père de famille* (which is why the duty of care defined by reference to the prudent man of business has to be qualified by adding that he acts “for the benefit of other people for whom he felt morally bound to provide”).³⁶ Moreover, the concept of the *bon père de famille* is an obvious import from Norman or French law, and in French law is one where a departure from the required standard of conduct can be either *simple* or *lourde* (ordinary or gross). There is therefore a more rational basis for distinguishing between ordinary and gross negligence than the Privy Council acknowledges. The second reason for the distinction is that the offshore trust business is of great importance to Guernsey’s status as an international financial centre, and that status is likely to be enhanced by rules on exclusion clauses which are more favourable to beneficiaries. As Sir de Vic Carey said at first instance, “settlers and beneficiaries of trusts... needed to have the reassurance that Guernsey was a suitable place to bring their wealth for looking after.”³⁷

Just as other jurisdictions can learn from decisions of the English courts, so our courts can learn from decisions in other jurisdictions. The dismissal by most of the judges in the Privy Council of the concept of the *bon père de famille* as an explanation for a different attitude to exclusion clauses in Guernsey before the 1990 Law is based on treating the concept as no more than a different way of explaining the idea of the prudent man of business. This seems to underplay the significance of a concept which may, in fact, be a better way of explaining the range of obligations which fall upon a person with fiduciary responsibilities to place the interests of others above his own interests than the obligations commonly shown in the frequently cut-throat world of business. There could also be value in addressing the utility of the concept of gross negligence in relation to exclusion clauses. It is surely legitimate to ask whether there is a difference in terms of culpability and responsibility between say, a total failure by a newly appointed professional trustee to review the actions of the previous trustees, and a review which, through careless oversight, fails to identify one isolated instance of a breach. Under the principles adopted in *Armitage v Nurse* the trustees would not only escape liability in both instances, despite the seriousness of the breach, they would be entitled to claim their fees as if they had acted with due diligence. Millett LJ himself seemed to recognise this, pointing out that the exemption clause in that case:

“...exempts the trustee from liability for loss or damage to the trust property no matter how indolent, imprudent, lacking in diligence,

³⁶ *Re Whiteley* (1886) 33 Ch D 347 at 355.

³⁷ 2009-10 GLR 197 at 211 [38]-[39].

negligent or wilful he may have been, so long as he has not acted dishonestly.”³⁸

In response to the claim that exclusion clauses allow a professional fee charger to act irresponsibly, it is often countered that exclusion clauses are risk-shifting devices which simply transfer the onus of taking out insurance against the risk. However, that argument may have little merit in the case of trustee exemption clauses. Lord Clarke points out in this case that professional trustees may be unwilling to take on the administration of trusts without the protection of exclusion clauses of very wide effect given the cost and difficulty of obtaining insurance³⁹ (the argument used to persuade the Law Commission not to recommend legislative change to the result produced by *Armitage v Nurse*). But, by thereby transferring the risk to the beneficiaries, the risk is upon parties who have very little ability to control it, and whose ability to obtain insurance (or to spread the risk if insurance is not available) is even more constrained than professional trustees. Fairness is therefore a relevant consideration in deciding where the line should be drawn in relation to trustee exemption clauses. Guernsey and Jersey have chosen to draw that line between ordinary negligence and gross negligence. There appears to be no evidence that doing this by legislation in 1990 and 1989 respectively has destroyed or even damaged their professional trust business, and as Lord Kerr observed in his closing observations:

“The fact that this [dissenting conclusion] would have resulted in discordance between the law in England and Wales and that in Guernsey could have been faced with equanimity, I believe. If the placing of reliance on a responsible person to manage property so as to promote the interests of the beneficiaries of a trust is central to the concept of trusteeship, denying trustees the opportunity to avoid liability for their gross negligence seems to be entirely in keeping with that essential aim.”⁴⁰

³⁸ [1997] 2 All E.R. 705 at 711d.

³⁹ [2011] UKPC 13 at [74].

⁴⁰ Ibid at [180].