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GENERAL LIMITATIONS ON INDEMNITIES UNDER THE TRUSTS (GUERNSEY) LAW, 2007

Indemnities can provide a false sense of security where they are drafted to cover less or more than what is permitted by law. It is vitally important for retiring trustees to seek expert legal advice on the risks to their personal estate and how best to manage those risks through the use of indemnities.

The personal estates of trustees are at risk from liabilities to third parties dealing with the trusts they represent, even long after they ceased to act as trustee for the relevant trust. A practise has thus developed for retiring trustees to seek suitable protection from the incumbent trustees or the trust beneficiaries in the form of an indemnity agreement.

An indemnity grants a retired trustee recourse to the trust assets or beneficiary's estate to settle a liability that has arisen during his time as trustee, which liability would otherwise need to be settled out of the retired trustee's personal estate. However, it is not only retired trustees who do not have indemnities who end up having to pay debts out of their own pockets. There are many retired trustees holding indemnities that are either insufficient or unenforceable who ultimately experience the same outcome.

The Trusts (Guernsey) Law, 2007 (the "Law"), sets three general limitations on the protections an indemnity agreement may provide a trustee.

Firstly, an indemnity cannot grant a trustee recourse to the trust assets for liabilities that arose due to the fraud, wilful misconduct, or gross negligence the trustee committed in the performance of his duties. This applies to all trusts irrespective of when they were created. There is no protection for a trustee in these circumstances as such protection would go against the fundamental principles underpinning trusts.

Secondly, a beneficiary of a trust may grant a trustee recourse to trust assets for liabilities that arose due to the trustee being in breach of his duty under the Law or the trust deed. This will not be possible, however, in circumstances where the beneficiary is a minor, does not know all the material facts, or has been improperly induced by the trustee into granting such recourse.

This limitation is not peculiar to trusts but emanates from the laws of contract. A minor is incapable of concluding a binding legal agreement. A beneficiary cannot validly conclude an agreement where he does not have sufficient information to make an informed decision. If a retiring trustee unduly influences a beneficiary to agree to an indemnity agreement that he would otherwise not have agreed to then the resultant agreement will prove to be invalid.

Thirdly, a retiring trustee is not entitled to greater protection than that he would have had were he still a trustee of the trust, unless the Royal Court has granted leave for such to be granted or all the beneficiaries have consented to such protection being granted. This requires an understanding of the value of the assets held in the trust and the protections afforded to trustees under the relevant trust deed at the time the trustee retires. A trustee seeking greater protection would need to take the additional steps required to validly be afforded the extraordinary protection.

A trustee's final defence against claims to his personal estate is an indemnity. As indicated, a failure to comply with the applicable laws might mean that retired trustees are more exposed than they are aware, and it is critical that trustees give due consideration to the terms and extent of any indemnities they enter into, taking legal advice if necessary, to ensure that the risks associated with being a trustee are managed with confidence.

Babbé LLP has experience advising trustees on the risks and how best to manage the risks through the use of indemnities. If you would like any further information or if we can assist, please do not hesitate to contact us

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