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Exclusion of duty and the irreducible core content of trusteeship: A re-assessment

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EXCLUSION OF DUTY AND THE IRREDUCIBLE CORE CONTENT OF TRUSTEESHIP: A RE-ASSESSMENT

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Abstract

This article reviews Millett LJ's classic characterisation of the irreducible core content of trusteeship. Using duty modification / exclusion clauses that are commonly found in modern trust-corporate structures to circumvent a trustee's duty to actively engage in corporate management as an example, this article has two main objectives. First, this article re-examines the duty to act honestly and in good faith in the irreducible core; and secondly, it considers how our reanalysis can help conceptualise and construe the 'residual supervisory obligation' enunciated by the courts in the recent *Zhang v DBS* litigation.

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I INTRODUCTION

In the seminal judgment of Millett LJ in *Armitage v Nurse*, his Lordship identified the 'irreducible core' of the trust as follows:

> [T]here is an irreducible core of obligations owed by the trustees to the beneficiaries and enforceable by them which is fundamental to the concept of a trust. If the beneficiaries have no rights enforceable against the trustees there are no trusts. But I do not accept the further submission that these core obligations include the duties of skill and care, prudence and diligence. The duty of the trustees to perform the trusts honestly and in good faith for the benefit of the beneficiaries is the minimum necessary to give substance to the trusts, but in my opinion it is sufficient.[1]

In recent years, there has been a heated debate over which obligations are irreducible core obligations and which are not. In the traditional narrative, a trustee, as the paradigmatic fiduciary, is held to a very high standard of conduct and subject to a standard bundle of default rules governing both his fiduciary and non-fiduciary duties. A modern narrative based on the voluntary assumption of duties, however, suggests the freedom to reduce and modify a trustee's duties according to the will of the parties concerned.[2] Since the twentieth century, trust jurisdictions worldwide have facilitated increasing settlor autonomy through a variety of tools ranging from settlor's reserved powers to letters of wishes and exemption clauses. These developments have an inevitable impact on the 'irreducible core' content of trusteeship and the public policy limits on trusts. Given Millett LJ's 'irreducible core', which

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[1] [1998] Ch 241, 253-4.

[2] *Australian Securities and Investments Commission v Drake (No 2)* [2016] FCA 1552 [272]-[276].

is 'sufficient' to 'give substance to the trusts', entails only 'the duty of the trustees to perform the trusts honestly and in good faith for the benefit of the beneficiaries', the scope of mandatory default rules appears to be relatively restricted. Millett LJ's formulation thus provides support for the modern narrative and also a strong version of settlor autonomy which champions contractarian freedom of management and disposition of trust assets that give effect to the rights and duties voluntarily undertaken by the parties unless countervailing policy considerations prevail.[3]

However, Millett LJ's formulation of the 'irreducible core' of trusteeship has not gone unchallenged. The clash between the traditional and modern narratives continues to be a heated debate and has more recently played out in the context of the trust-corporate structure,[4] a structure commonly employed by settlors in wealth management practice to maximise their control through separating the function of trust administration from the function of corporate management. Many modern settlors wish to retain active control over the management and investment activities of their company even after they have transferred their shares in the company to a third-party trustee, regardless of whether the trustee is in fact competent to supervise the company's conduct. To keep the trustee 'out of the way', provisions to modify or exclude his duties are usually included in the trust deed stipulating that the trustee need not be actively engaged – or involved at all – in corporate management. The effectiveness of these provisions was recently affirmed by the Hong Kong Court of Final Appeal in *Zhang Hong Li and another v DBS Bank (Hong Kong) Ltd*.[5]

Using *Zhang v DBS* as the anchor context, this article has two objectives: first, to challenge the correctness of the Hong Kong Court of Final Appeal decision; and secondly, to offer a reanalysis of the scope of the irreducible core obligations of trustees. It argues that insofar as professional trustees are concerned, the law should hold them to a higher standard and invalidate provisions that purport to exempt a professional trustee's liability for gross negligence. Contrary to Millett LJ's characterisation in *Armitage v Nurse*, we argue that the imposition of a higher standard on professional trustees is entirely justified by existing equitable concepts and prevailing policy concerns, without the need to await legislative intervention. Apart from the introduction and the conclusion, this article is divided into three parts. Part II first outlines the trustee's duty in monitoring trust-owned companies and the modification of such duty through an anti-*Bartlett* clause, detailing in particular the facts of *Zhang v DBS* which involves an extensive anti-*Bartlett* clause. This will be followed by a careful examination in Part III of the possible conceptual bases of a 'residual, high-level supervisory duty' that was pronounced by the lower courts but ultimately rejected by the final court. Part IV reanalyses Millett LJ's characterisation of the irreducible core content of trusteeship and applies the irreducible core as reanalysed to *Zhang v DBS*.

[3] James Penner, 'Exemptions' in Peter Birks and Arianna Pretto (eds), *Breach of Trust* (Hart Publishing 2002) 241, 250.

[4] A 'trust-corporate' structure refers to a structure where the trust assets comprise shares in a company and the trustees are therefore the shareholders of the company. Our article focuses on structures where the trustees own controlling shareholding in the relevant company.

[5] [2019] HKCFA 45, (2019) 22 HKCFAR 392 ('*Zhang v DBS* (CFA)'); overturning the decision of the lower courts.

II EXCLUSION OF DUTY THROUGH ANTI-*BARTLETT* CLAUSES

A The *Bartlett* Duty and its Modification through an Anti-*Bartlett* Clause

The *Bartlett* duty, derived from the English case of *Bartlett v Barclays Bank Trust Co Ltd*,[6] arises where the trustee holds a controlling interest in a private company. In such a scenario, the company's shares, as opposed to the underlying assets held by the company, constitute the trust property.[7] The interposition of a corporate structure does not by itself relieve trustees from the active and independent administration of the trust. Under English law, the 'prudent man of business duty' requires the trustees of the hybrid structure to 'act in relation to the shares and to the controlling position which they conferred, in the same manner as a prudent man of business'.[8] In specific terms, a trustee is obliged to supervise the progress of corporate affairs, which in turn requires him to make inquiries and consult with the company's directors from time to time to ensure that he has an adequate flow of information to consider whether the company's affairs are being properly managed. In exceptional circumstances, trustees are expected to exercise the controlling interest held by the trust to intervene in corporate management. Merely receiving information on the affairs of the company *qua* shareholder does not suffice.[9] One way of fulfilling this expectation is to appoint one of the trustees (or his nominee) as director of the company, thereby ensuring that the interests of the trust are represented at the board of directors level.[10]

In recent years, a modern, younger clientele of the trust industry has emerged. This clientele is more reluctant to relinquish control over trust assets, as they often comprise shareholding in business empires that that clientele is still actively managing[11] or using as an investment vehicle.[12] Importantly, the *Bartlett* duty mentioned above may create undesirable disruption to the daily management of corporate affairs. Accordingly, to capture the market of this clientele, new 'trust' products with massive settlor reserved powers, attenuated trustee duties, and disenfranchised beneficiary rights have become the norm. These 'trust' products often include an 'anti-*Bartlett* clause' stipulating that the trustee is not required to supervise or intervene in corporate management, save in exceptional circumstances such as where there is dishonesty on the part of the company's directors or officers.[13] Such a clause not only reduces the trustee's ability to influence the company's

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[6] [1980] 1 WLR 430 ('*Bartlett*').

[7] *Gestrust SA v Sixteen Defendants* [2016] EWHC 3067 (Ch) [53].

[8] *Bartlett* (n 6) 442. See also similar judicial statements made pre-*Bartlett* in, eg, *Re Lucking's Will Trusts* [1968] 1 WLR 866, 874: 'trustees holding a controlling interest ought to ensure so far as they can they have such information as to the progress of the company's affairs as directors would have. If they sit back and allow the company to be run by the minority shareholder and receive no more information than shareholders are entitled to, they do so at their risk if things go wrong.' (Cross J).

[9] *Bartlett* (n 6) 532, 534, applied recently in *Re Weetman (dec'd)* [2015] EWHC 1166 (Ch), [2015] WTLR 1745 [55].

[10] *Bartlett* (n 6) 433.

[11] See, eg, *Kan Lai Kwan v Poon Lok To Otto* (2014) 17 HKCFAR 414 where Otto Poon set up an offshore (Jersey) discretionary family trust whose assets consisted mainly of shares in his engineering company and whose beneficiaries were his three children.

[12] See, eg, *Zhang v DBS* discussed below.

[13] See, eg, BVI Trustee Act (Cap 303), Schedule, paragraph 8. Note that an anti-*Bartlett* clause that seeks to negate the duty altogether – for example, by excluding the duty to intervene even where there is dishonest conduct at the corporate level – would amount to a trespass on the irreducible core obligations of a trustee, as

management (except in accordance with the trust deed), but also effectively ensures that its management is left to those with the requisite skills and expertise, ie the directors (of whom the settlor is often one). Needless to say, protecting trustees from liability in areas that they may not be expert in may also offer them additional incentives to take up the role of trusteeship.

The practice of inserting an anti-*Bartlett* clause into a trust deed has been accepted to varying degrees across jurisdictions. To be clear, the insertion of an anti-*Bartlett* clause into a trust deed is not generally motivated by a sinister intention to perpetuate a sham, evade tax or place assets beyond the reach of one's family members. But when embedded in a trust product sold by the modern wealth management industry, an anti-*Bartlett* clause can be more offensive in practice than it is in principle. The client-banker/trustee relationship, which is ultimately a business relationship, renders the trust concept more formal than substantive. The relational dynamics in practice thus threaten the irreducible core aspect of a trust that it must benefit the beneficiaries[14] and that any clashing settlor's wishes must yield.[15] In some cases, the tension between instituting sufficient distance between a settlor and the trust assets to ensure the creation of a valid trust while guaranteeing that the settlor is not abdicating full control over the assets results in the insertion of artificial layers and roles into the trust structure. These roles are played by parties related to the advisor or settlor, and their function is to ensure that the settlor achieves his objectives. The facts of *Zhang v DBS*, to which we now turn, are concerned with just such a structure.

B *Zhang v DBS*

The Hong Kong Court of Final Appeal decision in *Zhang v DBS* was the latest judicial examination of anti-*Bartlett* clauses.[16] The case was an 'epic saga of greed and great wealth gained and lost' that unfolded against the backdrop of the global financial storm in 2008.[17] The settlors, Zhang and Ji (a married couple) set up a Jersey-law governed family trust with the assistance of their banker, DBS Bank (Hong Kong) Limited ('DBS Bank'). The only trust asset was the sole share of a private investment company called Wise Lords Limited ('Wise Lords') incorporated and owned by Ji. The trustee was a subsidiary company of DBS Bank ('DBS Trustee'). DBS Trustee nominated DHJ Management, DBS Bank's corporate services subsidiary, as the sole director of Wise Lords to manage its daily operations. Under this structure, Ji was the settlor and one of its beneficiaries.[18] However, to retain her decision-making power over Wise Lords' investment activities, Ji was also appointed as its investment advisor and was further authorised by Wise Lords to give investment instructions on its behalf to DBS Bank directly.

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enunciated by Millett LJ in *Armitage v Nurse* above.

[14] John H Langbein, 'Mandatory Rules in the Law of Trusts' (2004) 98 NWULR 1105, 1120-1123.

[15] Lionel Smith, 'Give the People What They Want? The Onshoring of the Offshore' (2018) 103 Iowa Law Review 2155, 2157.

[16] n 5.

[17] [2018] HKCA 435 ('*Zhang v DBS* (CA)') [1] (Cheung JA).

[18] The other beneficiaries were Zhang and the couple's children.

Pursuant to the wishes of Zhang and Ji, the trust deed set out in clear language 'a detailed and complete code of conduct' for the trustee,[19] the relevant portions (the anti-*Bartlett* clauses) of which can be summarised as follows:

- DBS Trustee is under no duty to interfere with the management or conduct of the business of Wise Lords.
- DBS Trustee is to leave the management and conduct of the business of Wise Lords to the directors and other authorised personnel (including its investment advisor), and it is under no duty to supervise such personnel unless the trustee has actual acknowledge of dishonesty.
- DBS Trustee may assume that the conduct of Wise Lords' business is being carried out competently and is not obliged to take any steps to ascertain the correctness of that assumption.
- DBS Trustee is not liable for any loss to Wise Lords or the trust assets arising from any act or omission of the directors and other persons (including Ji as Wise Lords' investment advisor), even where the act is dishonest, fraudulent, negligent or otherwise.
- DBS Trustee is under no duty to obtain information in relation to Wise Lords' affairs and will not be liable for any loss arising from not obtaining information in relation to Wise Lords or not verifying the accuracy of any information that it received in respect of Wise Lords.

Although Ji's investment strategy was initially very successful, generating profits of more than US$17 million, her decisions concerning three transactions, namely (i) an increase in Wise Lords' credit facility to US$100 million; (ii) the purchase of $83 million Australian dollars; and (iii) the purchase of several decumulators, turned out to be disastrous when the Australian dollar depreciated during the 2008 financial crisis. Amongst their other claims, Zhang and Ji, in their capacity as the objects of the trust, sued DBS Trustee for dishonest and negligent breach of trust in relation to losses suffered by reason of Wise Lords' investments in these transactions. The case was litigated to the highest court in Hong Kong. Although all levels of the court accepted that the anti-*Bartlett* clauses in question were effective under Jersey law in circumscribing a trustee's duty to intervene in the affairs of companies in which the trustee holds shares, they differed on whether DBS Trustee should be held liable on the basis that, notwithstanding the operation of the anti-*Bartlett* clauses in question, it still owed a duty to supervise the conduct of Wise Lords' business.

Both the Hong Kong Court of First Instance and Court of Appeal upheld the couple's claim against DBS Trustee for breach of trust, albeit on slightly different grounds. Bharwaney J, the first instance judge, held that DBS Trustee was subject to a 'high-level supervisory duty' to act prudently and without gross negligence.[20] The Court of Appeal, in agreement with Professor Matthews' expert opinion on Jersey law,[21] premised DBS Trustee's liability on a

[19] *Zhang v DBS* (CA) (n 17) [6.3].

[20] *Zhang v DBS* (CFI) (unrep HCCL 2/2011, 13 April 2017) [83], [118] and [163].

[21] Note that the applicable law in *Zhang v DBS*, namely Jersey law, prescribes that liability for gross negligence can never be excluded (art 30(10) of the 1984 Trust (Jersey) Law). Professor Matthews agreed that the anti-*Bartlett* clauses were compliant with Jersey law, subject to the *residual obligation* that '[i]f circumstances were to arise where no reasonable trustee could lawfully refrain from exercising those powers, a failure to do so in such a case would amount to a breach of trust' (*Zhang v DBS* (CA) (n 17) [6.8]).

'residual obligation' to intervene in the corporate affairs of or seek information regarding the company 'where no reasonable trustee could lawfully refrain from exercising those powers'.[22] This residual obligation was described by the court as a *high-level supervisory duty*.[23] Although DBS Trustee had no obligation under the terms of the trust to interfere in Wise Lords' business or obtain information regarding Wise Lords, it still had the power to do so because it was a member of Wise Lords. On the facts, DBS Trustee had breached its high-level supervisory duty by granting (after-the-event) approvals to transactions about which it knew nothing and had not fully apprised itself of information regarding their substantial risk.[24] Such behaviour amounted to gross negligence, for which liability cannot be alleviated by any exemption clauses under Jersey law.

However, the decisions of the lower courts were overturned by the Court of Final Appeal. It is worthy of note that the parties had reached a settlement agreement shortly before the judgment was handed down. Nonetheless, the Court decided to render judgment in view of the important issues of law the case had raised, which had attracted considerable public interest both locally and internationally.[25] Ribeiro PJ, Fok PJ and Lord Neuberger NPJ delivered the Court's unanimous judgment (to which Cheung PJ and Tang NPJ agreed). They disagreed with the lower courts on two principal points. First, they held that the existence of a 'high-level supervisory duty' was inconsistent with the 'anti-*Bartlett*' clauses in the trust deed. Such a duty would require DBS Trustee to query and disapprove the three impugned transactions in question, which would in turn amount to interference with Wise Lords' business in a way contrary to the terms of the trust deed. As such, there was no legal basis for any residual obligation that might contradict or override the express anti-*Bartlett* clauses in the trust deed.[26] Second, the anti-*Bartlett* clauses in question relieved DBS Trustee's *Bartlett*-type duties only to the extent that it did not have any actual knowledge of dishonesty. Disagreeing with the Court of Appeal's view that the residual obligation requires trustees to exercise available powers in circumstances where no reasonable trustee could refrain from acting, the Court of Final Appeal held that the only obligation that can be said to be 'residual' is the obligation to act in cases involving actual knowledge of dishonesty not covered by the anti-*Bartlett* clauses.[27] On the facts, there was no actual knowledge of dishonesty that required DBS Trustee to interfere. Further, the speculative and risky nature of the transactions in question was irrelevant because the trust deed specifically allowed the taking of risks. Consequently, DBS Trustee's approvals of the transactions did not constitute gross negligence, and it was protected by the relevant exemption clauses exempting it from liability for any acts and omissions short of gross negligence. Both points are elaborated upon below.

The conclusion reached by the Court of Final Appeal appeals to one's instinctive sense of fairness and justice. Zhang and Ji should not be able to have their cake and eat it too: the anti-*Bartlett* clauses in the trust deed allowed the settlor-couple to direct an investment

[22] *Zhang v DBS* (CA) (n 17) [6.8]-[6.10].
[23] That description was inspired by the language used by DBS Trustee in its pleadings which state that it had assumed a 'high level supervisory role': *Zhang v DBS* (CA) [6.11] and [6.12]. That said, it is doubtful that DBS Trustee, by the wording of a 'high level supervisory role', meant that it had assumed a duty to intervene in circumstances where no unreasonable trustee could lawfully refrain from acting.
[24] *Zhang v DBS* (CA) (n 17) [6.67].
[25] *Zhang v DBS* (CFA) (n 5) [6].
[26] *Zhang v DBS* (CFA) (n 5) [45].
[27] *Zhang v DBS* (CFA) (n 5) [61]-[63].

profile of their choice rather than being restricted to the more conservative approach that DBS Trustee would likely have preferred, earning huge profits as a result. Only when their investment decisions went wrong did they seek to argue for a residual obligation underlying those clauses to minimise their losses.

Even though the outcome may be defensible on the facts, the *Zhang v DBS* litigation has brought to the fore the pertinent issue of imposing a 'residual, high-level supervisory obligation' on a trustee despite the presence of anti-*Bartlett* clauses. We argue that the Court of Final Appeal was wrong in rejecting this residual, high-level supervisory obligation. The difference in views between the Court of Final Appeal and the lower courts in essence, delineates the tension between upholding settlor autonomy on the one hand and ensuring trustee accountability and beneficiary protection on the other. The Court of Final Appeal decided in favour of the former, and the lower court in favour of the latter. In the lower courts' view, trustees should not be allowed to simply bury their head in the sand and turn a blind eye to clear and present risks, as they are the guardians of the trust assets. The difficulty in defending that view, however, lies in finding a legal or conceptual basis for the residual obligation. Even though the *Zhang v DBS* litigation addresses the position in Jersey law, and art 30(10) of the 1984 Trusts (Jersey) Act expressly prohibits the exoneration of trustees' liability for gross negligence, which position is different from English law wherein gross negligence and 'ordinary' negligence are treated simply as a singular negligence-based breach,[28] the same tension and challenge in finding a legal or conceptual basis for the residual obligation exist under English trust law and the laws of other major common law jurisdictions. Hence, our discussion below in Part III tackles the aforementioned conceptual complexity head-on under English law. We propose that the residual, high-level supervisory obligation formulated by the lower Hong Kong courts in the *Zhang v DBS* litigation (the 'residual obligation') can be conceived as a facet of our reanalysed account of the irreducible core of trustee's duties.

III CONCEPTUAL BASES OF THE 'RESIDUAL OBLIGATION' TO INTERVENE

Our attempt to justify the residual obligation on a reanalysed account of the irreducible core of trusteeship proceeds in two closely-related parts. We first consider in this part (Part III) the anterior question of whether the lower courts' proposed 'residual obligation' can even *exist* conceptually. Here, we explore three different conceptualisations of the 'residual obligation', two of which were propounded by the Hong Kong courts in the *DBS v Zhang* litigation but which are flawed in their respective ways. The third conceptualisation, put forward by us, is to treat the 'residual obligation' as an aspect of the irreducible core of trusteeship. However, the analysis cannot stop here. To accommodate the 'residual obligation' within the irreducible core of trusteeship, we go on, in the next part (Part IV) of our discussion, to explain and justify an expanded account of the irreducible core which encompasses the duty to act prudently and without gross negligence on the part of professional trustees. This exercise thus defines the content of the 'residual obligation'.

A 'Residual obligation' as a distinct, non-derogable duty that overrides anti-*Bartlett* clauses

[28] *Armitage v Nurse* (n 1) 253H-256D.

According to the lower courts in the *Zhang v DBS* litigation, the residual obligation remains in spite of the presence of effective anti-*Bartlett* clauses to exclude *Bartlett*-type duties (eg duties to interfere in the company's management, supervise its directors or obtain information). Their conceptualisation of the residual obligation is thus a distinct, non-derogable duty which overrides the effect of the anti-*Bartlett* clauses. In other words, the lower courts' approach effectively accepts that, in relation to the trustee's power of intervention, there are not one but *two* negligence-based duties: (1) a *Bartlett*-type duty and (2) a residual duty of intervention, ie the high-level supervisory duty.[29] Such a conceptualisation is, however, fundamentally flawed. If these two duties are the same negligence-based duty, then an anti-*Bartlett* clause cannot exclude the former but not the latter, as they differ in degree but not in kind.[30] Indeed, the basis of the lower courts' approach to the residual duty and its illogicality have already been highlighted by Davern in the following explanation:

> In a case, where a trustee holds all the issued shares in an investment company *without* the benefit of an anti-*Bartlett* clause, it does not make the slightest bit of sense to say that it has the ordinary *Bartlett*-type duty plus, over and above that, a high-level supervisory role such as would require it to spot, and take reasonable steps to prevent, things going seriously awry (ie so seriously that not noticing, or not doing something about the situation once noticed, would be grossly negligent): discharging the high-level supervisory function is included in the *Bartlett*-type duty (in the sense that if a trustee failed to spot or do something about the blindingly obvious, it would have breached its (*Bartlett*-type duty) as the greater includes the less.[31]

For this reason, the Court of Final Appeal was right in pointing out that the 'residual obligation' as conceived by the lower courts would be plainly inconsistent with the express anti-*Bartlett* clauses in the trust deed. Moreover, it is unclear, from the lower courts' judgments, the source of this distinct, non-derogable duty.

B Anti-*Bartlett* clauses preserve a 'residual obligation' to interfere where there is actual knowledge of dishonesty

A second conceptualisation of the 'residual obligation' is to be found in the Court of Final Appeal's judgment. The Court of Final Appeal reinterpreted the lower courts' decision as saying that there is a residual obligation to interfere in circumstances where there is actual knowledge of dishonesty. This reinterpretation stirs no controversy as it does no more than reiterate existing law and imposes no novel obligation on the trustee. The polite language of reinterpretation does not hide the fact that no residual obligation exists at all. At this point, it is helpful to revisit the Court of Appeal's reasoning and the Court of Final Appeal's objections to the same. The Court of Appeal had clarified that actual knowledge of dishonesty is but one example of how the residual obligation is engaged; it is not the *only* situation in

[29] Ray Davern, 'Trustee Residual Obligation: Is There a Basis for It?' (2019) 25 Trusts & Trustees 285, 288 and 289.
[30] Davern, ibid, 288.
[31] Davern, ibid, 288.

which a trustee should intervene.[32] Hence, trustees are under a duty to intervene in a company's affairs 'where no reasonable trustee could lawfully refrain from exercising those powers'.[33] In arriving at its conclusion, the Court of Appeal chiefly relied upon Professor Matthews' expert opinion. The Court of Final Appeal disagreed. Given that the anti-*Bartlett* clauses are effective to relieve the trustees from *any obligation* to interfere with the company's business or obtain information about the company, the Court of Final Appeal considered it self-contradictory if the clauses would simultaneously be rendered ineffective should circumstances arise 'where no reasonable trustee could lawfully refrain from exercising those powers [otherwise excluded]'.[34] Accordingly, the Court of Final Appeal proffered an alternative, 'non-contradictory' interpretation of Professor Matthews' expert opinion: 'no reasonable trustee could refrain from exercising otherwise excluded powers' can be interpreted only to mean interfering where trustees have actual knowledge of dishonesty, which is an exception already preserved by the anti-*Bartlett* clauses in question. The Court of Final Appeal buttressed its reading based on an example provided by Professor Matthews to illustrate his proposed residual obligation: the trustees would have been under a duty to intervene in corporate affairs if they had been informed by a credible source that the directors were stealing the company's assets.[35] The Court said that in such circumstances the trustees would have been in possession of actual knowledge of dishonesty, and their duty to intervene would have been justified simply on that basis, rather than on some notion of a non-excludable negligence-based obligation. In other words, according to the Court of Final Appeal, the residual obligation will only be engaged 'in cases involving actual knowledge of dishonesty not covered by the anti-*Bartlett* provisions',[36] and is not 'some implied, peremptory, free-standing 'high level supervisory duty' that came into being as an obligation that could not be excluded by the express terms of the Trust Deed'.[37]

It is submitted that the Court of Final Appeal's interpretation of 'unreasonableness' to mean 'actual dishonesty' is based on a strained, as opposed to non-contradictory, reading of Professor Matthews' expert opinion. First, extreme forms of anti-*Bartlett* clauses that seek to negate the duty to intervene even where there is dishonest conduct at the corporate level are already unenforceable at law. What is at issue is whether less extreme forms of anti-*Bartlett* clauses, such as that in *Zhang v DBS*, where the duty to intervene in cases of dishonesty is not excluded, should be subject to *additional* oversight by the courts in the form of a 'residual obligation' or otherwise. The Court of Final Appeal seems to believe that they should not be. But rather than expressly rejecting Professor Matthews' expert opinion, the Court watered down his residual obligation to the extent that it has no meaning other than restating the obvious position that anti-*Bartlett* clauses cannot exclude the duty to intervene in the case of dishonesty. Not only did the Court render Professor Matthews' residual obligation redundant; it in effect rejected it.

Second, it is difficult to imagine that Professor Matthews, an experienced professor, practitioner and judge, would have used the term 'unreasonableness' if he had really meant

[32] *Zhang v DBS* (CA) (n 17) [6.8] and [6.9].
[33] *Zhang v DBS* (CA) (n 17) [6.8].
[34] *Zhang v DBS* (CFA) (n 5) [60].
[35] See *Zhang v DBS* (CFA) (n 5) [61] and *Zhang v DBS* (CA) (n 17) [6.9].
[36] *Zhang v DBS* (CFA) (n 5) [61]-[62].
[37] *Zhang v DBS* (CFA) (n 5) [66].

actual knowledge of dishonesty.[38] The example he gave, namely where trustees have been informed by a credible source that a company's directors are stealing its assets,[39] was simply an (uncontroversial) illustration of what might amount to 'unreasonableness'. It certainly does not represent the *only* type of situation in which a trustee should intervene. Whilst the example itself may be confounding, it is not difficult to envisage alternative scenarios that do not involve clear-cut cases of trustees having actual knowledge of dishonesty. For example, could trustees stand by and do nothing if they heard from a source of unknown credibility that the directors were stealing the company's assets? What if they heard from a credible source that the directors were acting suspiciously, suggesting that they might be stealing the company's assets? What if they hear from a credible source that the directors' conduct raised alarm bells but received no specific details? These are likely to be scenarios in which no reasonable trustee could lawfully refrain from exercising its powers as a controlling shareholder. On balance, it is submitted that Professor Matthews likely intended the imposition of a residual obligation to intervene that encompasses, but also goes beyond, actual knowledge of dishonesty; in other words, that obligation encompasses circumstances in which no reasonable trustee could fail to intervene. The pertinent question is whether a trustee should be required to intervene in spite of anti-*Bartlett* clauses of the *Zhang v DBS* variety. The answer to that question lies in the normative basis for justifying the residual obligation.

C 'Residual obligation' as a facet of the irreducible core obligation of trustees

Here we put forward an alternative and more sensible reinterpretation of the lower courts' decision: that is, the 'residual obligation' is a facet of the irreducible core obligation of trusteeship (as reanalysed below). The 'irreducible core' of a trustee's duties provides a test of the 'minimum functionality' of a trust. Without this core basic duties, it cannot be said that the trustee, as the non-beneficial owner of the assets vested in him, can be held sufficiently accountable, and nor can the institution that the settlor has created function as a trust.[40]

At first glance, the proposed conceptualisation appears inconsistent with the view of the Court of Final Appeal in *Zhang v DBS*, which rejected the relevance of the notion of the irreducible core in the context of anti-*Bartlett* clauses as follows:

> It is important to note that the residual obligation referred to by Matthews is not to be equated with the 'irreducible core of obligations' which are 'fundamental to the concept of a trust' recognised by Millett LJ in *Armitage v Nurse*. As a matter of English law, those irreducible core obligations consist of '[t]he duty of the trustees to perform the trusts honestly and in good faith for the benefit of the beneficiaries' and do not include 'the duties of skill and care, prudence and diligence'. They do not posit some broad duty to exercise available powers in circumstances 'where no reasonable

[38] Note that Jersey law, the applicable law in *Zhang v DBS*, prescribes that liability for gross negligence can never be excluded (art 30(10) of the 1984 Trust (Jersey) Law), whereas English law permits exemption of liability for gross negligence. The language of 'unreasonableness' suggests that the residual obligation could apply to both Jersey and English law.

[39] See *Zhang v DBS* (CFA) (n 5) [61] and *Zhang v DBS* (CA) (n 17) [6.9].

[40] David Fox, 'Non-excludable trustee duties' (2011) 17 Trusts & Trustees 17, 17; David Hayton, 'The Irreducible Core Content of Trusteeship', in AJ Oakley (ed), *Trends in Contemporary Trust Law* (Clarendon 1997) 47.

> trustee could lawfully refrain from exercising those powers'. They do not operate to override express terms of a trust. They provide a touchstone for deciding whether the minimum requirements for constituting a trust have been met.[41]

The Court of Final Appeal's objection is not insurmountable and can be considered from two perspectives. The first pertains to the specific *Bartlett* duty in the *Zhang v DBS* litigation whereas the second relates to the content of the irreducible core more generally.

First, in the context of the *Bartlett* duty, the irreducible core obligation owed by trustees ought to take into account the factual matrix in which the *Bartlett* duty was breached (ie the trust-corporate structure). In a trust-corporate structure, although the trust asset is shares in the company, the value of those shares is inextricably linked to the value of the underlying corporate assets. Accordingly, the way in which the board of directors manages the company's affairs is of crucial importance. However, a trustee who is exempt from corporate management by reason of a generic anti-*Bartlett* clause is not directly involved in management. He is dependent on the board of directors to perform his functions competently. His only means of safeguarding the value of the trust assets is high-level monitoring and the exercise of discretion to intervene based on the information available to him. A trustee who is exempt from participating in corporate management and acquiring information as to the conduct of corporate affairs, and who may even blindly assume that the company is being managed competently, is in no real position to safeguard the interests of the trust. If his duty to intervene is engaged only in the circumstance of actual knowledge of dishonesty, it is hardly likely that he will, by reason of the robust exclusion of his involvement, come by such actual knowledge. The trustee's only source of information is the information he is entitled to by reason of being a shareholder in the company, such as company reports and records, which may not explicitly indicate dishonesty at the corporate level. In fact, it seems that a trustee with the benefit of anti-*Bartlett* clauses of the *Zhang v DBS* variety is excused from even reading annual reports and exercising his right to inspect company records. Realistically, a trustee might come to hear of or suspect corporate misconduct because of events that raise red flags but do not conclusively indicate dishonesty. Hence, in the context of the *Bartlett* duty owed by the trustee of a trust-owned company, there is a serious argument to be made that the irreducible core in which the *Bartlett* duty operates should mandate, at the very minimum, that it is insufficient for a trustee to intervene only in circumstances where he has actual knowledge of dishonesty.

Second, and more significantly, we suggest that not only should the irreducible core in the context of the *Bartlett* duty be redefined, indeed even Millett LJ's formulation of the irreducible core content of trusteeship in *Armitage v Nurse* itself can be challenged more generally beyond the *Bartlett* duty context. Indeed, this latter and wider project constitutes the primary aim of this article. In this connection, we argue for an expanded scope to include a duty to act prudently and without gross negligence on the part of a professional trustee. If we treat the residual obligation proposed by the lower courts in *Zhang v DBS* as a facet of the irreducible core duty of trustees,[42] this will offer a better conceptual basis for the residual obligation referred to by Professor Matthews without treating it as a separate, distinct duty

[41] *Zhang v DBS* (CFA) (n 5) [65].

[42] David Hayton, Paul Matthews and Charles Mitchell, *Underhill and Hayton Law of Trusts and Trustees* (19th edn, LexisNexis 2016) para 48.58.

that seemingly derives from no particular source. We will now turn to our reanalysis of the irreducible core.

IV A REANALYSIS OF THE IRREDUCIBLE CORE: AN EXPANDED SCOPE

A Reanalysing the irreducible core content of trusteeship

Millett LJ's formulation of the irreducible core content of trusteeship requires only that trustees perform the trusts honestly and in good faith for the benefit of the beneficiaries. Our reanalysis of the irreducible core of trusteeship comprises two key elements: first, a differentiation in the standard applicable to the lay trustee and the professional trustee; and secondly, the inclusion of the duty to act prudently, without gross negligence on the part of the professional trustee. In doing so, we define with clarity the content of the irreducible obligation: a professional trustee is under a duty to perform the trust honestly on an objective standard and in good faith which, in particular, requires him to not act gross negligently.

1. A higher standard on professional trustees

To argue for a higher standard of irreducible core to be imposed on a professional trustee is not a complex task. The differentiation of standards applicable to a lay trustee and a professional trustee is not unprecedented. Section 1 of the English Trustees Act 2000, for example, explicitly adopts a malleable standard of statutory duty of care that differentiates between a lay trustee and a professional trustee. In the context of trustee exemption clauses, English law has also adopted an objective test of dishonesty, as opposed to a subjective test, in respect of professional trustees.[43] Further, in *Armitage v Nurse*, Millett LJ acknowledged that it appears absurd for a professional trustee who charges a fee for his services to be exempt from liability for gross negligence, although he stipulated that he would prefer Parliament to take the lead in implementing any legal reform.[44] This is implicit recognition that a distinction may be drawn between a lay trustee and a professional trustee on the basis of public policy.

The more difficult task, which relates to the second element of our reanalysis of the irreducible core, is to *define* and *justify* the higher standard to be imposed on professional trustees at common law.

2. The duty to act honestly to be assessed by an objective standard

[43] *Walker v Stones* [2001] QB 902, 939 (the decision was confined to solicitor-trustees); *Fattal v Walbrook Trustees (Jersey) Ltd* [2010] EWHC 2767 (Ch) [81]. Cf *Spread Trustee Co Ltd v Hutcheson* [2011] UKPC 13, [2012] 2 AC 194 [107] where Lord Mance left open the correctness of *Walker v Stones*.

[44] *Armitage v Nurse* (n 1) 256. It may also be said that the beneficiaries of a trust managed by a professional trustee are entitled to expect a higher standard of protection (and correspondingly, stricter duties on the trustees) because the professional trustee's annual administration fees are paid out from the trust fund which is beneficially owned by the beneficiaries. Some support may be drawn from Lord Walker's dicta in *Pitt v Holt* [2013] UKSC 26, [2013] 2 WLR 1200, 1231.

Our first step in arguing for an expanded scope of the irreducible core of trusteeship is a modest and relatively uncontroversial one. Where professional trustees are concerned, the law should apply an objective standard of honesty. This proposition has already been accepted in the context of trustee exemption clauses. As alluded to above, in *Walker v Stones*, the English Court of Appeal applied an objective test of dishonesty to determine whether the solicitor-trustees had acted dishonestly for the purpose of the exemption clause in question: that is, it is necessary to take into account whether the solicitor-trustee's actually held 'honest belief' is 'so unreasonable that by, any objective standard, no reasonable solicitor-trustee could have thought what he did or agreed to do was for the benefit of the beneficiaries'.[45] Although Sir Christopher Clarke limited his proposition to solicitor-trustees, he stressed that the test of dishonesty should vary with the role and calling of the trustee in question.[46] Like solicitors, professional trustees profess to have particular expertise that is relied upon by settlors and beneficiaries. There is therefore no reason that they should not be held to a higher standard than lay trustees. In the subsequent English High Court case of *Fattal v Walbrook Trustees (Jersey) Ltd*, Lewison J, agreeing with the decision in *Walker v Stones*, also incorporated a similar objective standard of dishonesty in his definition of dishonesty for a professional trustee.[47]

According to the lower courts in *DBS v Zhang*, the 'irreducible core' in the context of the *Bartlett* duty of trustees of trust-owned companies will be breached if there is a failure to act in circumstances in which no reasonable trustee would have failed to act. Such reckless indifference can, though not always, constitute objective dishonesty in law. Acting in conscious disregard of a relevant risk is a tell-tale sign of dishonesty. Drawing inspiration from Sir Christopher Clarke's decision in *Walker v Stones*, we argue that it is an instance of dishonesty if the professional trustee's failure to act in the circumstances was so unreasonable that no reasonable professional trustee could have thought that his inaction was for the benefit of the beneficiaries.

Further support for our argument can be derived from the law of dishonest assistance. As in *Walker v Stones*, there is much to be learnt from the test for dishonesty enunciated in the context of dishonest assistance. In that case, the English Court of Appeal cited[48] Lord Nicholls' comments in *Royal Brunei Airways Sdn Bhd v Tan*, part of which is worthwhile reproducing in full here:

> Honesty is not an optional scale, with higher or lower values according to the moral standards of each individual… Unless there is a very good and compelling reason, an honest person does not participate in a transaction if he knows it involves a misapplication of trust assets to the detriment of the beneficiaries. *Nor does an honest person in such a case deliberately close his eyes and ears, or*

[45] n 43. Cf *Spread Trustee v Hutcheson* (n 43) [107] where Lord Mance left open the correctness of *Walker v Stones*.
[46] ibid 939.
[47] [2010] EWHC 2767 (Ch) [81]: a professional trustee is dishonest is if he commits a deliberate breach of trust (i) knowing that the deliberate breach is contrary to the interests of the beneficiaries; (ii) is recklessly indifferent to whether the deliberate breach is contrary to their interests; or (iii) whose belief is so unreasonable that, by any objective standard, no reasonable professional trustee could have thought that what he did or agreed to do was for the benefit of the beneficiaries.
[48] *Walker v Stones* (n 43) 939-940.

deliberately not ask questions, lest he learn something he would rather not know, and then proceed regardless.[49]

In the context of dishonest assistance, Lord Nicholls accepted that actual knowledge of dishonesty is not the only instance of dishonesty. Turning a blind eye to the red flags raised by a transaction and failing to make inquiries in such circumstances also amount to dishonesty in law. Relevant to our discussion here, concerning investment risks, Lord Nicholls said that '[i]mprudence may be carried recklessly to lengths which call into question the honesty of the person making the decision'.[50] Indeed, the conceptual parallel between the dishonest assistance and trust-corporate contexts makes the lesson on the test of dishonesty from the former particularly relevant to the latter.[51] In the context of dishonest assistance, a third-party assistant's dishonesty is being judged objectively, in light of his subjective knowledge (in particular, his subjective knowledge of the circumstances of the transaction conducted by the primary wrongdoer, ie the errant fiduciary). Similarly, in the context of a trust-corporate structure, a trustee's dishonesty is determined by his degree of knowledge of dishonest conduct at the corporate level. In one sense, a trustee who suspects dishonesty at the corporate level but fails to act in a situation in which no reasonable trustee would have failed to intervene can be said to be 'dishonestly assisting' the underlying dishonest conduct. This is so even if the trustee subjectively believes that his suspicion warrants no further inquiry to be made.

3. The duty to act in good faith includes the duty not to act gross negligently

Even if we readily accept that an objective standard of honesty should be applied, it must be acknowledged that Professor Matthews' framing of the 'residual obligation' is not definitively confined to dishonesty, and strays into the territory of gross negligence. In any event, albeit conceptually different in kind, the line between reckless imprudence that calls into question one's honesty (dishonesty) and serious deviation from ordinary standards of care that does not amount to recklessness is often difficult to draw in practice.[52] After all, a claim of dishonesty is frequently built on suggestive circumstantial evidence. A further question is whether there is any basis for redrawing the line of the irreducible core of trusteeship at gross negligence where professional trustees are concerned – that is to say that provisions in the trust deed can neither remove the professional trustee's duties to perform the trusts honestly and prudently, without gross negligence; nor exempt a professional trustee for liability arising from both dishonesty and gross negligence. This is clearly a more difficult proposition to make, as it is contrary to a line of cases allowing exemption clauses to exclude liability for gross negligence, including *Armitage v Nurse*, *Fattal v Walbrook Trustees (Jersey) Ltd* and *Spread Trustee v Hutcheson*. Moreover, it would be difficult in practice to distinguish between mere

[49] [1995] 2 AC 378, 389 (emphasis added).
[50] ibid 389-390.
[51] In *Walker v Stones* (n 43) 941, Sir Christopher Slade did not think there was a need to distinguish between the test for dishonesty in dishonest assistance and the test for dishonesty in the context of the validity of a trustee exemption clause.
[52] L Aitken, 'Limiting the trustee's liability – is 'gross negligence' relevant?' (2011) 127 LQR 503, 505.

negligence and gross negligence, as the two forms of wrongdoing merely differ in degree rather than in kind.[53] It follows that defining gross negligence would not be a simple task.[54]

However, the foregoing proposition is by no means impossible. The correctness of *Armitage v Nurse* was called into serious question by the dissenting judgments of Baroness Hale and Lord Kerr in *Spread Trustee v Hutcheson*.[55] Baroness Hale cautioned that *Armitage v Nurse* had yet to be reviewed by the Supreme Court.[56] Examining pre-*Armitage v Nur*se cases, she stated that Millett LJ's reasoning is 'open to serious question'.[57] Indeed, there was a majority opinion in *Spread Trustee v Hutcheson* that Millett LJ had misinterpreted the Scottish authorities he examined in *Armitage v Nurse* as turning on the construction of the exemption clauses in those cases, when in fact these cases reflected a Scottish public policy against the exemption of liability for dishonesty and gross negligence.[58] Baroness Hale further commented that the view that gross negligence should attract liability was neither 'eccentric' nor 'unusual', and may well be a good thing 'perhaps particularly in the light of the development of professional trustees and the modern approach to exemption clauses in consumer contracts'.[59] Lord Kerr added that denying trustees an opportunity to escape liability for gross negligence would be internally consistent with the concept of trusteeship:

> [I]f … 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 me to be entirely in keeping with that essential aim.[60]

Indeed, holding trustees liable for gross negligence would be in line with a proper, conceptual understanding of a trustee's duty of good faith. According to Mitchell, although judges often use the labels 'honesty' and 'good faith' synonymously,[61] the two are distinct duties. As Mitchell explains, the duty of good faith, whilst varying in content depending on the context, generally requires a power holder to 'make a sincere and serious commitment to the purposes for which his powers have been given and this may require her to pay proper regard to the interests of those whose position will be affected by the serious exercise of these powers, even if she is not required to prioritise their interests over her own interests and those of other people'.[62] Mitchell refers to the duty of good faith as the duty of

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[53] *Armitage v Nurse* (n 1) 254.
[54] cf *Great Scottish & Western Railway Company Ltd v British Railways Board* (unrep, CA 10 February 2000).
[55] *Spread Trustee v Hutcheson* (n 43). The Privy Council held by a slim majority of 3:2 that insofar as the law of Guernsey mirrored that of England, liability for gross negligence could be exempted by an appropriately drafted exemption clause.
[56] *Spread Trustee v Hutcheson* (n 43) [129].
[57] *Spread Trustee v Hutcheson* (n 43) [137].
[58] *Spread Trustee v Hutcheson* (n 43) [38] (Lord Clarke); [137] (Baroness Hale); [169]-[174] (Lord Kerr); and [133] (Sir Robin Auld, agreeing with Lord Clarke).
[59] *Spread Trustee v Hutcheson* (n 43) [137].
[60] *Spread Trustee v Hutcheson* (n 43) [180].
[61] For example, Mitchell observes that Millett LJ's statement of the irreducible core duty of 'good faith and honesty' in *Armitage v Nurse* has been read conjunctively and synonymously by courts. See Charles Mitchell, 'Good faith, self-denial and mandatory trustee duties' (2018) 32 TLI 92, 102.
[62] Mitchell, ibid 96.

'seriousness'[63] and clarifies that it is measured on an objective standard.[64] For this reason, it is possible for a trustee to have acted honestly (on a subjective standard) but breached the standard of good faith. Mitchell further argues that the duty to exercise discretionary powers rationally and transparently (ie the duty to exercise powers in good faith) should be mandatory in nature.[65] In a similar vein, and more generally, we argue that a trustee's duty of good faith requires him to act in a fair-minded, serious and rational manner in his administration of the trust.[66] Acting gross negligently or turning a blind eye to third parties' gross negligence that might affect the beneficiaries' interests is hardly acting in good faith. For the reasons stated by Lord Kerr in *Spread Trustee v Hutcheson*,[67] a trustee's duty of good faith should be a mandatory, non-excludable one.

Accordingly, the expansion of the irreducible core of trusteeship to include the duty not to act gross negligently does not require legislative intervention.[68] It only requires a clarified and principled understanding of the content of the duty of good faith, which is already part of the *Armitage v Nurse* formulation of the irreducible core.

Finally, it is also noteworthy that the laws of several other jurisdictions (including established wealth management centres) such as Jersey,[69] Scotland,[70] Canada,[71] Hong Kong[72] and, most recently, New Zealand[73] have already accepted, whether by way of case law or statute, that trustee exemption clauses cannot exclude liability for gross negligence.

B Impact of our reanalysed irreducible core of trusteeship on the construction of anti-*Bartlett* clauses

Having set out our reanalysis of the irreducible core of trusteeship and how that defines the 'residual obligation', it is necessary to address the question of how our proposed understanding of the irreducible core of trusteeship impacts the way in which courts should construe anti-*Bartlett* clauses. In particular, we must re-examine the effectiveness of the anti-*Bartlett* clauses in the *Zhang v DBS* litigation through this refined lens.

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[63] Mitchell, ibid 102.
[64] Mitchell, ibid 96.
[65] Mitchell, ibid 102.
[66] For a similar argument in the context of a fiduciary's duty of good faith, see, Lionel Smith, 'Aspects of Loyalty', available at SSRN: https://ssrn.com/abstract=3009894 who argues that extreme recklessness is not only a breach of the fiduciary's duty of care, but also a breach of his fiduciary's duty of good faith which should be treated as part of the irreducible core of the fiduciary relationship. Thus, a fiduciary, who is dishonest or consciously disregards the interests of the beneficiary, is in breach of his fiduciary duty of good faith.
[67] See text to n 60 above.
[68] One may also say that s 61 of the English Trustees Act 1925, which confers power on the courts to relieve a trustee from personal liability for breach of trust in circumstances where he has acted 'honestly and reasonably' and 'ought fairly to be excused', represents a rule of public policy on when a trustee may be exempted from liability. Cf English Trustees Act 2000, Schedule 1, para 7.
[69] Trusts (Amendment) (Guernsey) Law 1990, s 34(7).
[70] *Seton v Dawson & Ors* [1841] 4 D 310.
[71] *Re Poche* [1984] 6 DLR (4th) 40.
[72] Trustee Ordinance (Cap 23 of the Laws of Hong Kong), s 41W.
[73] Trusts Act 2019, s 40.

To begin with, it is obvious that the Hong Kong Court of Final Appeal prioritised respect for settlor autonomy in construing anti-*Bartlett* clauses:

> Anti-*Bartlett* provisions are generally incorporated in the Trust Deed in cases like the present because the parties wish to enable the settlor or the settlor's nominee freely to exercise control and management of the underlying company, especially regarding matters such as its investment decisions, and to relieve the trustees of any management or supervisory duties in that regard (save where extreme situations such as those involving actual knowledge of dishonesty might arise). To postulate that the parties' chosen scheme may be overridden by some implied, non-derogable external duty arising in circumstances 'where no reasonable trustee could refrain from exercising otherwise excluded powers' would be to introduce an amorphous and ill-defined basis for undermining a legitimate arrangement consciously adopted by the parties, exposing the trustees to unanticipated risks of liability and sowing confusion as to the extent of their duties.[74]

The value of our reanalysis of the irreducible core of trusteeship lies in highlighting the moral dimension of the trust relationship that the courts should maintain, in light of the relevant factual matrix, in their construction of anti-*Bartlett* clauses. Sir Philip Sales (writing extra-judicially) also supports this approach. In a recent chapter,[75] Sales argues for an objective interpretive approach to trustee exemption clauses that takes into account not only the context and specific factual matrix of each case, but also 'reflects the moral values which the courts regard as informing the trust institution' by reason of the beneficiaries' position of vulnerability vis-à-vis the trustee and take into account the identity of the trustee and specific circumstances in which the trustee assumes his role.[76] Given that anti-*Bartlett* clauses may give the settlor an excessive amount of control such that the trust in question may become a form of revocable agency and the trustee is under diminished or even no accountability at all to the beneficiaries, even though Sales has not gone so far as refining the irreducible core of trusteeship, it is clear that he will not favour an interpretation which effect is to transform a trustee's duties into 'simple contractual duties owed to a stranger to the trust'.[77]

In practice, different levels of conflicts may arise between the primary terms and objectives of the trust relationship and the anti-*Bartlett* clauses.[78] At the most intense level, the anti-*Bartlett* clause may directly trespass on the irreducible core with the effect of negating the existence of the trust relationship. This may happen if the anti-*Bartlett* clause

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[74] *Zhang v DBS* (CFA) (n 5) [64].

[75] P Sales, 'Exemption Clauses in Trusts' in P Davies and J Goudkamp (eds), *Defences in Equity* (Hart Publishing, 2018) 128-129 and 132-135.

[76] ibid 133-134.

[77] ibid 134, drawing support from *Citibank NA v MBIA Assurance SA* [2007] EWCA Civ 11, [2007] 1 All ER (Comm) 475, [82] (Arden LJ). Where we differ from Sales is that we advocate casting the moral dimension of the trust relationship as a rule of law to operate formally as a control on maximal settlor autonomy, which is relevant to and informs the courts' construction of anti-*Bartlett* clauses, other duty modification clauses or exemption clauses. Sales (ibid 134) prefers to treat both the moral dimension of the trust relationship and settlor autonomy as competing interests that can be practically balanced and reconciled through the interpretation process. Our approach should be preferred as it sets a more properly defined standard and would consequently promote clearer judicial reasoning and in turn better safeguard the moral dimension of the trust relationship.

[78] This part of our discussion has benefited from Sales' analysis of contractual interpretation in Sales (n 75) 129.

allows a trustee to refrain from acting even when he is in possession of actual knowledge of dishonesty. In such a case, the court should invalidate the anti-*Bartlett* clause. At a less intense level, the terms of the anti-*Bartlett* clause may be open to different interpretations, in which case the court should adopt a restrictive reading of the relevant terms so as to ensure that the existence of the trust relationship, its objectives and its moral dimension are maintained. Any ambiguity must be resolved against the person seeking to rely on the clause or the person who has inserted the clause into the trust deed.[79]

Returning to the *Zhang v DBS* case itself, if our reanalysis of the irreducible core of trusteeship is accepted, would the anti-*Bartlett* clauses in the case still be valid and effective? The anti-*Bartlett* clauses in *Zhang v DBS* excluded the trustee's duty to monitor and interfere with corporate management unless he has actual knowledge of dishonesty. Even though the Court of Final Appeal respected settlor autonomy, the strong moral dimension of the trust relationship should suggest that the anti-*Bartlett* clauses in *Zhang v DBS*, even though they were valid and enforceable for not infringing the irreducible core of the trustee's obligation as enunciated in *Armitage v Nurse*, would infringe the irreducible core as reanalysed in this article. This is because, first, a failure to act on the part of the professional bank-trustee in circumstances in which no reasonable professional trustee could have thought that his inaction was for the benefit of the beneficiaries would be regarded as a failure to duty to act honestly based on an objective standard, which infringes the irreducible core, as reanalysed.

Second, one may argue that a case of dishonesty, even on an objective standard, would be difficult to establish in respect of a trustee's inaction given that the relevant anti-*Bartlett* clauses sanctioned his extreme inaction save in the case of actual knowledge of dishonesty. Nonetheless, it is still arguable that the professional trustee could be said to have acted gross negligently in failing to act in circumstances where he has the power to intervene. Indeed, that was also the view of the Court of Appeal in *Zhang v DBS* which emphasised that although DBS Trustee had no obligation to interfere in the business of Wise Lords, it still had a power to do so as a member of the company[80] and the failure to do so amounted to gross negligence. As argued above, the failure to act in good faith entails the duty not to act gross negligently in our reanalysis of the irreducible core content of trusteeship.

V CONCLUSION

According to Millett LJ in *Armitage v Nurse*, however widely drafted an exemption clause, it cannot exclude a trustee's liability for fraud or dishonesty because a trustee has a duty to perform the trusts honestly and in good faith for the benefit of the beneficiaries. This characterisation of the irreducible core content of trusteeship highlights a policy tension between ensuring trustee accountability and beneficiary protection on the one hand and respecting settlor autonomy on the other. This tension is also played out in duty modification/exclusion clauses in trust-corporate structures. Traditionally, a trustee who

[79] This becomes less straightforward if the person seeking to rely on the clause is not the person who has inserted the clause into the terms of the trust, a situation that may arise often in the *Bartlett* duty context. The clause may be inserted by the settlor to keep the trustee out of the corporate affairs but which is relied upon by the trustee in litigation involving the settlor (suing in the capacity of beneficiaries).

[80] *Zhang v DBS* (CA) (n 17) [6.8], quoting para 87 of Professor Matthews' report.

holds a controlling interest in a company as trust property is still under a *Bartlett* duty at common law to monitor the conduct of the company's directors and to intervene if necessary to ensure that the trustee, by virtue of his legal ownership of the shares, continues to take an active role in corporate management so as to protect the underlying interest of beneficiaries. However, in modern trusts, the settlor often wishes to retain maximal control over 'his' business even after the trust is set up and thus inserts an anti-*Bartlett* clause into the trust deed to relieve the trustee from the *Bartlett* duty unless he has actual knowledge of dishonesty on the part of the company director's corporate management.

Our article suggests that the irreducible core should be reanalysed. Insofar as professional trustees are concerned, the duty to act honestly and in good faith should entail a duty to perform the trust honestly on an objective standard and in good faith which, in particular, requires him to not act gross negligently. This refined irreducible core represents the moral dimension of the trust relationship that the courts should maintain and take into account, alongside the specific factual matrix of each case, in their construction of anti-*Bartlett* or other duty modification clauses. With the rapid proliferation of the innovative trust products created by the modern trust and wealth management industry to maximise settlor control, our reanalysis ensures that contractarian freedom of management and disposition of trust assets will not be allowed to go unchecked. This, in turn, can better preserve the integrity and sustainability of the trust institution.