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Duties of Trustees

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In the last article, we considered the fundamental relationship between trustees, agents, and their counterparties. This article focuses on the duties of trustees and the extent to which those duties can be excluded or modified by contractual provisions. Our next article will focus on the duties owed by agents in bond and syndicated lending transactions.

Irreducible Core of Duties

The duties incumbent on 'conventional' trustees, such as individuals who administer family trusts, arise from a combination of statute, equity, and contract. To an extent, the same is true of corporate trustees. However, in the corporate trust context, any tensions between equitable and fiduciary obligations on the one hand, and express contractual provisions on the other, have invariably been resolved in favour of the latter. That is to say that by far the most important source of duties (as well as powers) for corporate trustees will be the trust deed and associated transaction documentation.

A compelling example of the courts' approach in this respect is ***Citibank N.A. and MBIA Assurance S.A. v QVT Financial LP*** ([2007] EWCA Civ 11). The case concerned the securitisation and subsequent restructuring of Eurotunnel Tier 3 junior debt and the ability of a security trustee to act on the direction of the contractually stipulated 'note controlling party', MBIA, which was also a guarantor of the debt. The trust deed specifically provided that the security trustee 'need not have regard to the interests of the noteholders' when acting on MBIA's instructions. As part of a restructuring, MBIA directed the security trustee to exercise a cash option. An unsecured noteholder (QVT) opposed this direction on the basis that it was a breach of the negative pledge clause forming part of the security for the notes. The security trustee therefore sought directions from the court.

In the Court of Appeal, QVT argued that the security trustee could not, to the exclusion of all else, follow the direction of MBIA and at the same time be consistent with the duties owed to the noteholders as a result of the trustee relationship. Allowing MBIA to give binding directions meant that the trustee's obligations were reduced to such a degree as to negate the existence of a trust. In this respect, reference was made to the well-established principle that a trustee's duties must consist, at a minimum, of an 'irreducible core' (***Armitage v Nurse*** ([1998] Ch 241)). In ***Armitage***, the principal duty of the trustee was found to be to 'perform the trusts honestly and in good faith for the benefit of the beneficiaries' – a fundamental obligation which could not be excluded within a trust instrument. The Court of Appeal in ***Citibank/QVT*** found that there were matters that required the security trustee's discretion (where the security trustee must consider the interests of its beneficiaries), notwithstanding that MBIA could still give binding directions on other matters. It was also found that the trustee was still required to act in good faith at all times. The role of the security trustee was not therefore displaced entirely and remained sufficiently meaningful to pass the ***Armitage*** test. Bearing in mind the degree of delegation to MBIA as 'note controlling party' in that case, the reliance placed upon the contractual wording by the Court of Appeal is striking. It may well be helpful in such instances to be able to point to standard market provisions in the trust deed that cover reliance on instructions and confirm that the duties are solely mechanical and administrative in nature.

Typical Duties of Corporate Trustees

It is important when assessing a trustee's duties, particularly in light of any allegations of breach, to establish the nature of the duties in question, since this will scope the nature of a claim and will inform potential remedies and whether the common-law principles of causation, remoteness of damage, and measure of damage should apply (***Bristol and West Building Society v Mothew*** ([1998] Ch 1)).

The extent of a trustee's duties beyond the 'irreducible core' will primarily be determined by the wording of the trust deed. That said, and despite the strong steer from the courts, certain general statutory and fiduciary duties are significant since they are the source of more specific duties. Such duties therefore must be qualified or excluded by express wording in the trust deed.

Duty of Care

Duty of skill and care

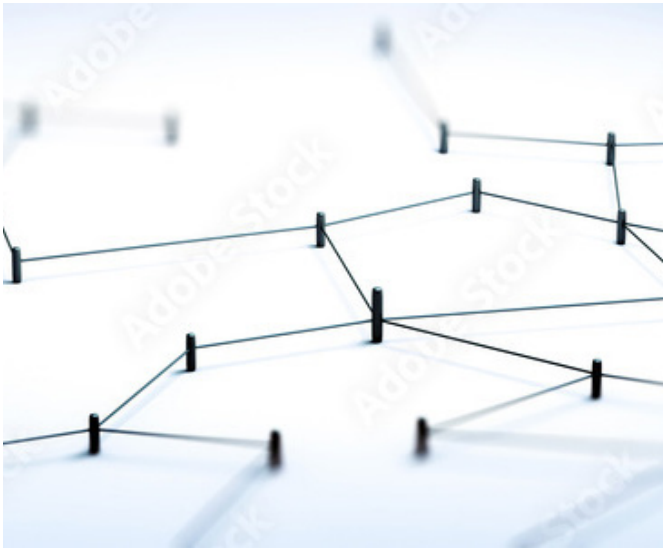
The principal duty of a trustee is to exercise its function with due skill and care. This duty of skill and care is derived from: (1) Section 1 of the Trustee Act 2000 and Section 750(1) Companies Act 2006, as applicable; and (2) the common-law 'General Duty' that applies to professional corporate trustees as stated in ***Bartlett v Barclays Bank Trust Co. Limited*** ([1980] 1 All ER 139).[1]

The Trustee Act applies to certain trustee functions, only some of which will be relevant to a note or security trustee, such as when the trustee exercises powers of investment or powers for the appointment of agents, nominees, and custodians. In such instances, the Trustee Act requires a trustee to exercise such care and skill as is reasonable in the circumstances, having regard in particular to any special knowledge or experience that they have or hold themselves out as having (which means a higher threshold if acting as a professional trustee specialising in a particular sector). The statutory duty is usually excluded by the terms of the trust deed, something that the Trustee Act expressly contemplates.

[1] In ***Bartlett***, Brightman J held that 'a professional corporate trustee is liable for breach of trust if loss is caused to the trust fund because it neglects to exercise the special care and skill which it professes to have'.

The General Duty requires trustees, when managing trust affairs, to take at a minimum all precautions which 'an ordinary prudent man of business' would take. There is undoubtedly an enhanced higher standard over and above these standards for professional trustees that is consistent with the 'special care and skill which [the professional trustee] professes to have'.[2] ***Bartlett*** decided that this included being held to standards, abilities, and expertise advertised by a professional trustee in advertising literature. In ***Bartlett***, the particular breach (arising from a trustee's shareholding in a property company) took the form of excessive reliance placed by the trustee on the limited information provided at annual general meetings and annual financial information. The court found that the duty required the trustee to go further to require the board of the relevant property company to actively inform and consult the trustee. To mitigate this outcome, it is advisable to limit the trustee's duties to those which are expressly set out in the transaction documents, but noting that even these contractual provisions will not in all contexts serve to give effect to this limitation.

Direct exclusion of liability for breaching the General Duty is not permitted under Section 750(1) Companies Act 2006 (applicable to bond trust deeds), although provisions which limit such duties are likely to be upheld.



Practical Considerations: It should be ensured that a comprehensive description of the purpose of the trust and sufficient powers, exculpations of liability, and limitations on duties and liabilities are present in the trust documentation. However, trustees should remain mindful of the General Duty, which has a potentially wide application to many of its functions.

The manner in which a professional corporate trustee promotes and markets itself (for example, by way of statements relating to specific expertise in certain financial products) may well be relevant to the standards a court will hold it to.[3] In line with this, it may well be relevant to consider the wider corporate structure and be mindful of the expertise of other divisions that would be available to the trustee.

Duty to monitor and investigate

As a bridge between the issuer and noteholders, the trustee will often be party to information before it is disseminated, if at all, to noteholders. A key consideration in this context is the extent to which a trustee is under a duty to actively monitor or investigate the issuer's financial position and the issuer's compliance with its covenants.

The courts considered the duty to monitor in ***Torre Asset Funding Limited & another v The Royal Bank of Scotland plc*** ([2013] EWHC 2670). While that case was predominantly about RBS's role as an agent, RBS also acted as a security trustee in the transaction. The court had to consider the extent of RBS's duty to disclose the financial difficulties of the borrowers, and the court found that the extent of the investigative duty was to be interpreted in the context of its limited and mechanical role. We expect that the court would take a similar approach when construing the extent of a trustee's investigative duties when events of default are not clear cut.

2 Some cases have stated that the general duty may apply at its highest level to trustee departments of major clearing banks (***Galmerrow Securities Limited v National Westminster Bank*** ([2002] WTLR 125)).

3 Specifically, in Bartlett, although the advertising material of the corporate trustee was not available in evidence, had it been in evidence, the material would have been considered relevant to the standard to be attributed to a corporate trustee.

Typically, trust deeds contain provisions which confirm that the trustee is, for example:

> not bound to take any steps to ascertain whether any event, condition, or act, the occurrence of which would cause a right or remedy to become exercisable by the Trustee or by any other Transaction Party under any of the Transaction Documents, has occurred or to monitor or supervise the observance and performance by any Transaction Party of their respective obligations hereunder, and until it shall have actual knowledge to the contrary, the Trustee shall be entitled to assume that no such event, condition, or act has occurred and that the Issuer and each of the other Transaction Parties are observing and performing all their obligations hereunder.

This clause seeks to ensure that the trustee is not required to take active steps to monitor the issuer's compliance or performance. However, once the trustee is deemed to have actual knowledge[4] of the occurrence of a particular event or circumstance, it will need to consider what degree of care and diligence is required of it (having regard to the provisions of the trust deed). The nature of the event in question and the type of transaction involved will inform the trustee's assessment of the degree of care required.[5]

If there is uncertainty of factual circumstances or the nature of a particular event, trustees may request a certificate from the directors of the issuer certifying that the issuer has complied with all of its obligations (which may include further certifications of compliance with specific issuer covenants) and that no event of default has occurred. This right to request an issuer certificate is a standard power included in most trust deeds. From the issuer's perspective, upon receipt of such a request, it must consider which (or which combination) of its agents has the requisite knowledge and expertise to provide the confirmations the issuer will require for it to conclude that a compliance certificate can or cannot be given. In this endeavour, the issuer should also consider what degree of reliance it can place on these back-to-back confirmations, and in what form they should be given. In engaging with agents, time will be of the essence since the issuer typically has a short window (usually seven days) from the date the trustee's request is made to provide the certifications.

Practical Considerations: In the context of managing the flow of information and who may be deemed to have actual knowledge of it, it is important to look at the corporate group structure of the trustee and agency organisation. This is to avoid a situation where an individual is an officer of both the agency division and trustee division of the same legal entity on the same or related transactions who may, as a consequence, obtain actual knowledge of some fact in one capacity which is then inadvertently attributed to the other.

Disclosure

Information in the possession of trustees will have varying degrees of sensitivity. Some of it may be confidential (belonging to the issuer and potentially third parties), and other information might be price sensitive, with regulatory restrictions on dissemination. With this in mind, we consider 'disclosure' from two perspectives: (1) a trust beneficiary's desire to be informed and whether this translates into a trustee's duty of disclosure; and (2) the trustee's ability to disclose information.

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4 Actual knowledge has been held to refer to personal, rather than attributed, knowledge (***Infiniteland Ltd. v Artisan Contracting Limited*** ([2005] EWCA Civ 758)). In the case of a corporate trustee, this would include the knowledge of its officers but not its advisors.

5 Contrary to the view of one commentator, in the ordinary course of a performing transaction, it is not the normal practice of trustees to review the annual accounts and other documents sent to creditors, nor to monitor the financial press.

Duty to disclose

Noteholders regularly request information which has been provided by the issuer to the trustee. The question of whether the trustee is obliged to provide that information will be determined by applicable confidentiality and regulatory restrictions, the duties arising out of the trustee relationship in general, and the terms of the trust deed in particular.

The leading case on a trustee's duty of disclosure in response to a demand by a beneficiary is ***Schmidt v Rosewood Trus***t ([2003] UKPC 26). The case, originating in the Isle of Man, concerned a personal trust and the access by an individual, who had a discretionary interest under the settlement, to accounts and assets of two trusts set up by his father.

The Privy Council set out the following general principles regarding access to information: (1) beneficiaries have a right to *seek* trust documents; (2) that right is subject to the court's inherent jurisdiction to supervise trustees rather than existing as a proprietary right to the documents; and (3) the response to a request is a matter for the trustee's discretion. In most categories, beneficiaries will not have an absolute right to the disclosure of information regarding (for example) trust assets or property, but for some categories, such as trust accounts, there will need to be good reasons for a decision to withhold a document from a beneficiary.

"For some document requests, there will need to be good reasons for a decision to withhold a document from a beneficiary"

In capital markets transactions, the trust deed will usually contain language which expressly removes from the trustee any obligation to disclose to noteholders information flowing from the issuer, for example:

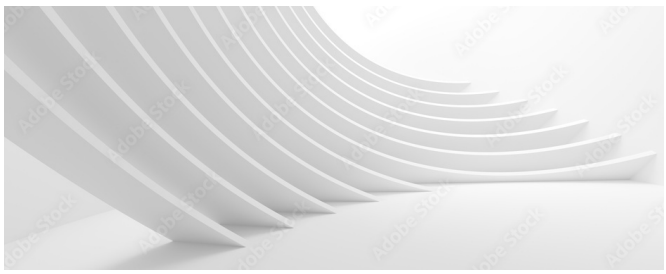
> The Trustee shall not (unless and to the extent ordered so to do by a court of competent jurisdiction) be required to disclose to any noteholder any information (including, without limitation, information of a confidential, financial, or price-sensitive nature) made available to the Trustee by the Issuer or any other person in connection with the Trust Deed, and no noteholder shall be entitled to take any action to obtain from the Trustee any such information.

Some commentators have questioned whether this type of clause can effectively fetter a beneficiary's right to documents held by trustees because this duty is part and parcel of the irreducible core of the obligations of a trustee under ***Armitage v Nurse***. In our view, given the commercial nature of the trust and the primacy frequently given by the courts to the terms of the trust deed in commercial contexts, it is likely that such clauses will be upheld.

Ability to disclose

As mentioned above, trustees may find themselves in possession of information with varying degrees of sensitivity. Consider, for example, an event of default. It is important that this information is disclosed to noteholders, and typically a contractual obligation to disclose in such instances will be imposed upon the issuer. In practice, the trustee will usually publish its own notice to noteholders following the issuer notice because the noteholders are trust beneficiaries. However, trustees should keep in mind that there are often other beneficiaries, such as contractual counterparties, who may also need to receive such notices. In addition, there are frequently provisions requiring the issuer to provide copies of notices to noteholders before publication, and there can be conditions on listed bond transactions which provide that notices are only deemed given a certain number of days after they have been published/sent through the clearing systems. If the giving of a particular notice has consequences, such as commencing the running of time periods, awareness of these provisions is vital.

In certain circumstances, for example a distressed corporate issuer on the brink of insolvency, it may be that appropriate disclosure by the issuer in a timely fashion is not taking place; and in such instances the trustee may wish to unilaterally disclose information to its beneficiaries,



but it should always bear in mind issues relating to confidentiality and regulatory restrictions.

Practical Considerations: With any given disclosure, trustees should first consider which parties have contractual obligations to disclose, and then, to the extent the trustee determines that disclosure by it is required, it should think carefully about the identity of the correct recipients, the manner of disclosure or publication, the consequences of such disclosure, and to whom any enquiries stemming from such disclosure should be directed in the first instance.

Duty to give reasons

In general, trustees are not obliged to give reasons for making a decision or exercising a discretion. This follows from ***Re Londonderry's Settlement*** ([1965] Ch 918), in which it was held that, where there was an absolute discretion in favour of trustees, so long as the trustees exercised their powers bona fide and with no improper motive, the reasons for the trustee acting in a particular way are immaterial. It follows that trustees are not bound to disclose or allow inspection of documents that would lead to the disclosure of the reasons for a trustee exercising a discretion in a particular way. There have been attempts, in the context of private trusts, to draw distinctions between information rights arising from the exercise of dispositive powers by a trustee (whereby one trustee may receive a greater benefit compared to another) and administrative powers concerning information about the trust (such as its assets), with trustees in the latter case still potentially being required to disclose reasons for decisions (***Lewis v Tamplin*** ([2018] EWHC 777)). However, this relatively recent line of case law has not found favour amongst the commentary and probably has a more limited application to the commercial sphere.

In ***Satinland Finance S.a.r.l. and another v BNP Trust Corporation UK Limited and another*** ([2010] EWHC 3062 (Ch)), the court considered the approach of ***Re Londonderry's Settlement*** in the context of a note issue. In that case, the noteholders argued that they were entitled to ask the court to direct the trustees to present a winding-up petition to the issuer of notes (the Irish Nationwide Building Society – INBS) on the basis of allegedly repudiatory statements made on behalf of INBS. The trustees declined to take that step (or accept the alleged repudiation) and argued that there was no basis for the court to intervene to direct the trustees to do so. The court agreed with the trustees and found that the ***Re Londonderry's Settlement*** principles applied to the commercial notes context. It was found that there was no basis for the court to intervene against the trustees and their exercise of discretion. When exercising discretion, trustees will need to consider the extent to which they should document their reasons for exercising it. Documenting the reasons behind the decision may assist the trustee in later establishing that it met any applicable obligation that it was under, and good governance from the perspective of the trustee as a trust company is also important. However, if noteholders or other beneficiaries looked to challenge the exercise of discretion through litigation, the documentary record could be subject to disclosure under the applicable civil procedural rules, and careful thought over questions of privilege will need to be given. In contentious circumstances in particular, it is advisable to seek legal advice (whether internal or external) before taking any particular steps in order to avoid or mitigate hazardous outcomes. Whether there are sensitivities or issues with disclosing the reasons for a particular exercise of discretion will be highly fact-dependent to any given case. We will consider the exercise of trustee powers and discretions in further detail in a future article.

Duty to advise

There have been numerous attempts, particularly on the part of noteholders, to argue that a trustee owes

noteholders a duty to advise on the best course of action in a particular set of circumstances. One of the clearest examples of this was in ***Elektrim S.A. v Vivendi Holdings*** ([2008] EWCA Civ 1178). Elektrim SA guaranteed an issue of bonds by its wholly owned subsidiary Elektrim Finance BV. A trustee was appointed under the bonds pursuant to an English law trust deed. Separately, Elektrim and Vivendi were involved in an ongoing dispute over the ownership of shares in Polska Telefonia Cyfrowa (PTC). Deutsche Telekom challenged the transfer of Elektrim's interest in PTC to a joint venture controlled by Vivendi. Following an arbitration award, the PTC shares were transferred to Deutsche Telekom, to the detriment of Vivendi. A subsidiary of Vivendi, VH1, was then established to purchase the bonds issued by Elektrim Finance BV. At the time of VH1's purchase, the bonds were already in default. The scene was therefore set for the next round of litigation between Elektrim and Vivendi.

Insolvency proceedings in Poland against Elektrim were withdrawn by the trustee (on the instructions of 30% of the bondholders) as a consequence of payment to the bond trustee of part of the funds that had been received from Deutsche Telekom in the PTC disposal. Following directions from the court concerning those funds, a distribution was made to bondholders. VH1 then commenced proceedings in Florida against Elektrim and the trustee alleging breach of fiduciary duty and negligence against the trustee. An anti-suit injunction was successfully obtained from the English High Court. In addressing an appeal against the anti-suit injunction, the Court of Appeal examined the nature of a 'no-action clause' and the duties allegedly owed by the trustee to VH1 as noteholder.

VH1 alleged that the trustee breached its fiduciary duty in: (1) accepting 'tainted funds' (the payment arising from the PTC disposal) without consulting the noteholders; (2) failing to disclose and draw the noteholders' attention to the risks of accepting the tainted funds and not conducting legal due diligence into the legality of the transaction; and (3) withdrawing the bankruptcy proceedings and thereby losing the right to pursue other avenues of recovery. These actions (or failures to act) were also said to be a breach of the requirements of care and diligence set out in the trust deed.

The Court of Appeal made short shrift of these arguments, going so far as to express the view that it was 'surprising' that those allegations had been made at all. The acceptance of the funds and the withdrawal of the petition were undertaken on the instruction of the bondholder committee and that, under the terms of the trust deed, '[i]f [the trustee] receives such instructions[,] it has to act (subject to getting satisfactory indemnities)'. This left little room for an advisory role. In addition, the noteholders were found to be expert investors, capable of looking after their own interests. The noteholders were aware of both the relevant arbitral award and the circumstances of the funds and had their own legal advisers. It was not the role of the trustee to second-guess or displace the legal advice given to the noteholders, and there was no special duty on the trustee to take steps to confirm that the transaction was the appropriate course of action.

'Watchdog' duty

Noteholder trustees also have a duty to act as a 'watchdog' for unrepresented creditor interests in legal proceedings. This duty includes assisting the court by raising any relevant legal argument affecting the position of unrepresented beneficiaries or parties in proceedings commenced by the trustee. Two cases that discuss the watchdog duty are ***State Street Bank & Trust Company v Sompo Japan Insurance Inc and Others*** ([2010] EWHC 1461 (Ch)) and ***Citicorp Trustee Company Limited v Barclays Bank plc and Others*** ([2013] EWHC 2608 (Ch)).

In ***State Street***, a dispute arose in connection with floating rate notes that were issued in six tranches with varying priorities. As the notes had been issued in dematerialised form to Clearstream and Euroclear, the trustee had been unable to ascertain the identity of all the noteholders. In the absence of any noteholders willing to

participate in the proceedings, the judge called upon the trustee to advance any arguments that were reasonably available to the unrepresented noteholders. Notwithstanding the trustee's contention that it ought to be able 'to maintain complete neutrality', the court held that the trustee's specific duty to act as a watchdog for unrepresented creditor interests flowed from its more general duties.

Citicorp concerned a highly complex structured finance transaction. As in ***State Street***, the junior noteholders did not initially participate. Rather than rely purely on the trustee's watchdog duty, the judge in that case ordered that a representative of the junior noteholders be added to the proceedings in order to ensure that the junior noteholders were represented in and bound by any judgment.

Practical Considerations: Trustees seeking directions from the court may need to consider the interests of all beneficiaries for whom it acts as a trustee and be prepared to represent the interests of absent beneficiaries in proceedings. This could cause considerable difficulties to trustees acting in highly complex structured finance transactions involving several classes of noteholders – particularly if not all creditors can be identified. To guard against such issues and others such as the presumption of an advisory role, the trustees' package of powers, limitations of liability, and exculpatory provisions are key. It should be ensured that provisions are included that describe the instruction mechanics clearly, and remove discretion, and that intercreditor arrangements are equally clear and unambiguous. In addition, provisions covering items such as the ability to seek and rely absolutely on instructions, appoint professional advisors (and rely on them), and cease to act if there is any financial or legal exposure should also be included.

Fiduciary Duties

The fiduciary nature of a trustee's duties does not flow from the mere fact of the office of trustee. Rather, a trustee may be regarded as a fiduciary only as a result of the specific duties that it is subject to. This means that a trustee is not necessarily acting as a fiduciary in the discharge of all its functions (***Saltri III Limited v MD Mezzanine SA SICAR and others*** ([2012] EWHC 3025 (Comm)). Nevertheless, a trustee's fiduciary duties are typically considered to include: (1) duties of undivided loyalty; (2) the duty to not put itself in a position of conflict with its private interest or its duties to other beneficiaries; and (3) the duty to not make an unauthorized profit without authority.

> "The courts have shown themselves willing to narrowly interpret the irreducible core when express commercial terms restrict a trustee's duties."

The extent of these duties is usually significantly curtailed by the terms of the trust deed. As noted above, trust deeds cannot detract from the irreducible core obligations described in ***Armitage v Nurse***, without which it is said that the office of trustee cannot exist. Nevertheless, the courts have shown themselves willing to narrowly interpret the irreducible core when express commercial terms restrict a trustee's duties (see for example the ***Saltri III*** decision considered in our last article, where the duty to avoid conflicts was significantly reduced by the terms of the intercreditor agreement).

Conflicts of interest

There may be scenarios of conflicts between noteholder classes which a trustee may be required to manage. This type of conflict was considered in our first article, 'Who Calls the Shots with Trustees and Agents?'

The duty to avoid conflicts merits particular attention for two reasons. First, there is often potential for overlapping interests in related transactions involving the same issuer (particularly in separate issues of different priorities, for example secured or unsecured or subordinated or unsubordinated issuances). Second, corporate trustees may often sit within a banking group where other group companies take other roles on the transaction.

The classic statement of the duty to avoid conflicts can be found in ***Aberdeen Rail Company v Blaikie Brothers*** ([1854] 1 Macq 461, HL):'… no one, having such duties to discharge, shall be allowed to enter into engagements in which he has or can have a personal interest, conflicting, or which possibly may conflict, with the interests of those whom he is bound to protect'. This prohibition encompasses a duty to avoid situations which will potentially give rise to a conflict.

The trust deed will usually include exculpatory language expressly sanctioning the trustee to enter into financial transactions or arrangements with the issuer and to act as trustee in relation to other securities issued by the issuer. In order to protect such clauses from future challenge, reference is usually made to them in the offering circular. However, while the language may protect against liability from the point of view of breaching a duty to avoid conflicts, the fact of an actual conflict may still influence the question of whether the trustee breached the General Duty (***Re Dorman, Long and Co Limited*** ([1933] All ER Rep 460)) or its standard of care. It is also unlikely that the contractual protections will be effective if the trustee can be shown to have acted in bad faith.

"The fact of an actual conflict may still influence the question of whether the trustee breached the General Duty or its standard of care."

Practical Considerations: Particular care is needed when a trustee deals with a related company within its financial group which has an interest in the transaction. One of the few areas of judicial criticism of the security trustee in ***Saltri III*** was in its sharing of information with the related group affiliate senior lender entity but not the mezzanine lenders. A trustee must therefore keep in mind the potential for conflicts when disseminating information, including when information is shared informally between colleagues of the same financial group. Appropriate information barriers should be implemented to ensure robust governance of conflict of interest and also to manage information flows and liability/exposure.

The typical trust deed language should be effective in allowing different subsidiaries within the same financial group to occupy various roles on the same transaction. If a conflict is not excluded by the protective clauses within the trust deed, other options may be available to a trustee to manage a situation of conflict. These may include seeking bondholder consent, the implementation of ethical walls, the potential delegation of powers and duties, and the appointment of an additional trustee for one or more specific purposes.

Secret profit

Subject to certain exceptions, a fiduciary must not make a profit out of its position without the informed consent of the beneficiary. As a result, the fact that the trustee will be remunerated by the issuer out of transaction funds is expressly set out in the trust deed. The trust deed will also contain exculpatory language to state that the trustee is not bound to account for profits from other business with the issuer.

Issues can sometimes arise when a trustee's remuneration does not follow standard terms. We will consider a trustee's remuneration in future articles, but for these purposes we note the general requirement for a trustee's remuneration to be authorised, including in situations where the structure of that remuneration is complicated.

Wider commercial use of information obtained in the course of acting as trustee must be treated with caution. In

United Pan-Europe Communications NV v Deutsche Bank AG ([2000] BCLC 461), United Pan-Europe Communications (UPC) claimed that Deutsche Bank had utilized confidential information (provided to it in the course of its participation in syndicated loans and as underwriter to UPC) in order to pursue its own commercial opportunities by acquiring shares in a third party against UPC as a rival bidder. Although this was not strictly a trustee case, the considerations on the scope of the fiduciary duty will be similar, and although the case concerned an application for an interim injunction (with the much lower evidential standard of whether there was a serious issue to be tried), the Court of Appeal found that there was a seriously arguable case for breach of a fiduciary duty.

The Contractual Limitation of Trustee Duties

The trust deed will include a range of clauses intended to insulate the trustee from liability. These will include clauses that directly exclude liability for certain trustee duties or, by contrast, limit what is required by the duty itself.

For example, trust deeds will include wording which excludes the application of Section 1 of the Trustee Act 2000. Clauses are often framed around Section 750 of the Companies Act 2006 and follow the wording closely:

> Subject to Section 750 of the Companies Act 2006, nothing in the Trust Deed shall in any case in which the Trustee has failed to show the degree of care and diligence required of it as trustee having regard to the provisions of the Trust Deed conferring on it any trusts, powers, authorities, or discretions exempt the Trustee from or indemnify it against any liability for negligence, default, breach of duty, or breach of trust for which it may be responsible in relation to its duties under this Trust Deed.

"It appears that the provision envisages that clauses can limit the ambit of any duty but not exclude the consequences of breaching that (contractually limited) duty."

Section 750 of the Companies Act itself provides that clauses are 'void in so far as it would have the effect of exempting a trustee of the deed from, or indemnifying him against, liability for breach of trust where he fails to show the degree of care and diligence required of him as trustee, ***having regard to the provisions of the trust deed conferring on him any powers, authorities or discretions***'. The scope of the latter wording is not entirely clear, but it appears that the provision envisages that clauses can limit the ambit of any duty but not exclude the consequences of breaching that (contractually limited) duty. On this reading, provisions allowing the trustee to rely on experts, advice, or certificates in the course of its activities serve to define the trustee's duties and should therefore be permissible under Section 750.

Other statutory provisions that may be relevant to trustee liability include:

- Unfair Contract Terms Act 1977 (UCTA): The provisions of the UCTA requiring exclusion clauses for negligence to satisfy the requirement of reasonableness have limited application to the trust context. This is because in the UCTA, negligence is defined as a duty arising either from the terms of a contract or from a common-law duty to take reasonable care. Neither of those concepts fit easily into the trustee–noteholder relationship, which is based in trust rather than contract (***Baker v JE Clark & Co (Transport) UK Ltd.*** ([2006] EWCA Civ 464)). This conclusion is also reinforced by Schedule 1(b) UCTA, which states that the Act does not apply to 'any contract so far as it relates to the creation or transfer of securities or of any right or interest in securities'.

- Section 61 Trustee Act 1925: This section provides a mechanism for the court to relieve a trustee of personal liability for breach of trust when the trustee acted honestly and reasonably and 'ought fairly to be

excused' for breach of trust. This avenue may be open to a trustee over and above the protective clauses in the trust deed – but will be less likely to be available in the case of professional/specialist trustees.

Exclusion clauses will not be effective to restrict liability for fraud or dishonesty. Such liability is part of the irreducible core of obligations that must be preserved to allow for the existence of a trust. Reliance in bad faith upon an exclusion clause may vitiate that reliance and the operation of the clause (***Wilkins v Hogg*** ([1861] 31 LJ Ch 41)). However, as a matter of common law and subject to the statutory provisions considered above, liability is capable of being excluded for gross negligence and even a deliberate breach of trust if the breach is committed in good faith and on the basis of an honest belief that the trustee is acting in the interests of the beneficiaries (***Armitage v Nurse***).

When considering breach in the context of fiduciary duties, it is important to bear in mind that 'the expression "fiduciary duty" is properly confined to those duties which are peculiar to fiduciaries … it is obvious that not every breach of duty by a fiduciary is a breach of a fiduciary duty' (***Bristol and West Building Society v Mothew***). In the context of breaches more generally, care must be taken to understand clearly what is being alleged, since there are material consequences for the trustee depending on whether the allegation is for breach of trust, breach of fiduciary duty, or breach of the trustee's duty of care, and whether the remedies for such breach are in contact, tort, statute, or equity. We will consider such topics in a later article in this series.

Enforcement

Capital market transactions may have a unitary trust structure where the security and the intermediation between the issuer and noteholders are given to the same trustee entity or the roles split into those of a 'note trustee' and 'security trustee'. It is not always an arbitrary distinction – the security trustee may have a different set of beneficiaries or parties empowered to instruct it; however, the analysis remains the same – i.e., subject to exclusion and limitation clauses, security trustees will be subject to similar obligations as those considered above. These include Section 1 of the Trustee Act 2000 (if not excluded), the General Duty, and potential fiduciary duties.

The increasing demands placed on trustees in an enforcement context have resulted in enhanced scrutiny over the duties that they owe and the contractual limits on those duties. Before default or enforcement, in most cases the trustee will have a limited role. When security is being enforced or released, including in the context of restructurings, the trustee may be called upon to exercise discretion.

The trustee may be subject to additional specific duties that are unique to enforcing security:

- The equitable duty to take reasonable care to obtain the best price reasonably obtainable for the security at the time of sale or disposal.
- To exercise the power of sale bona fide and for its proper purpose.

As was seen in ***Saltri III***, these duties may be owed by the trustee to lenders as terms of the intercreditor agreement (or equivalent). The extent of these duties will be a matter of construction of the terms of the intercreditor agreement or trust deed, and these duties may be limited.

Practical Considerations: The trustee should ensure that the terms of the relevant transaction documents make clear that the trustee is not liable or responsible for the suitability, adequacy, sufficiency, validity, or enforceability of the security.

Conclusion

Trustees can continue to take comfort from the contractual protections which limit their roles and duties. Despite sustained challenges to those contractual protections, they remain both extensive and effective. Nevertheless, as we have seen, a trustee is not simply a creature of contract and, even in commercial environments, may need to consider its duties and obligations beyond the contractual terms. This will mainly arise where the law limits the extent to which those noncontractual duties can be excluded or limited. Some of those duties, such as the General Duty of skill and care, can be wide-ranging.

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