

# Basic Principles on Trust in Maltese Law

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This article is intended to set out the key principles regulating and establishment of a trust governed by Maltese Law (Malta Trust). This piece was neither conceived nor has it been written with the view to be a treatise on the Maltese law on trusts. It is motivated by the frequent and numerous occasions in which the present writer, who has been involved with advising and the setting up of a considerable number of trusts for more than two decades in Malta and overseas, has met with inaccurate, misguided and, at times, seriously flawed understanding or statement of the very basic rules that apply to trusts under Maltese law by the civilian population and the legal profession in the broadest meaning of the term.

## 1. BACKGROUND AND CULTURAL CONTEXT TO THE MALTA TRUST

The concept of trust is essentially an English law concept which was for the first time imported into our legal system in 1988/89 through the concept of an offshore trust as part of the offshore legal regime introduced in the late nineteen eighties when Malta was launched as an offshore centre. That law is still in existence and applies to trusts registered under its terms and whose shelf-life has not yet expired.<sup>2</sup> This article will not focus on that law but rather on the 2005 Trust and the Trustees Act<sup>3</sup> (Trust Act).

There is no doubt that the Malta Trust is a relative of the English trust. The real question is whether the Maltese is an offspring of the other or whether it is a separate branch of a wider family. They are best to be considered as distant cousins and should be treated as such. I say this in an attempt to curb a seemingly prevalent and unbridled enthusiasm to adopt and import English common law principles, statutory

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<sup>2</sup> The shelf-life is the tenth anniversary from the date of their registration and then the trustees and the settlor or protector or beneficiaries have a maximum two year period within which to decide whether to re-domicile the trust under a foreign law or apply the 2005 law on trusts or close down the whole structure.

<sup>3</sup> Chapter 331 of the Laws of Malta

rules and practice and apply them almost mechanically to the Malta Trust simply because our law may be silent or untried or our jurisprudence still embryonic. This will lead to confusion and a deeper misunderstanding locally of the concept. Such signs are already found in the recent decision of our courts in '**Bettina Vossberg pro et noe v Equinox International Ltd et**';<sup>4</sup> but more on this judgment later.

The present writer's experience is mainly with trusts in a commercial context. However, trusts may, of course, also be established for cultural, religious, charitable and purely private reasons. I cannot possibly comment with any degree of certainty on the latter categories as my experience is limited in those scenarios. But in the private-sector commercial world, i.e. the world of corporations and successful men and women in business, it is safe to say that the trust is looked upon as follows. It is seen as an entity per se, i.e. another form of a juridical person, over which the Settlor would like to continue to exercise a varying but material degree of control after settling assets or had assets settled into it. It may be surprising to some but this characteristic is prevalent in Europe, the UK and the US.

Depending on why and how it is established, the Malta Trust may or may not have tax advantages, even though in most cases tax benefits is the main driving force behind its creation. In any event, it is seen as a convenient recipient with which to ring fence some or all assets for a variety of reasons - none of which are illegal but all have one or more common objectives, namely to separate assets and/or to conceal them and/or to distance them, from someone (including themselves) or some entity.

This is a reality of commercial life regardless of whether one finds affinity with it or not. This is not just a local but an international phenomenon and almost certainly intrinsic in the civilised Western democracies.

For Maltese nationals who have some notion of the concept of trust, this phenomenon and outlook is predominant and widespread. I would suggest that nine out of ten Maltese nationals who, for instance, might be advised to set up a trust to inject a professional/ impartial management of an otherwise highly charged, tense, envy riddled environment of a family-owned but highly successful business or, for example, to regulate the management, development and eventual distribution of a rich estate among the prospective heirs, will almost certainly decline the advice if they realise, as they should, that once they settle their assets into the Malta Trust, they have ceded ownership and, theoretically, have lost control at law.

Cessation or forfeiture of legal control and ownership are sine qua non elements for a trust to succeed. It's as simple as this - no transfer of ownership between Settlor and Trustee - no Malta Trust.

Ironically, the fulfilment of this criterion, essential for the validity of the trust, is in reality the very element which is or will be largely responsible for the Malta

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<sup>4</sup> Court of Appeal, 9 November 2012

Trust from ever becoming a popular legal instrument among the Maltese whose DNA is dominated by the urge to control.

## **2. ESTABLISHMENT AND SETTLEMENT OF THE MALTA TRUST**

The Trust Act provides for the creation of a trust in writing and orally but most significantly – ‘in any manner’.<sup>5</sup> This position should be altered by the Legislator and avoided meanwhile in practice as much as possible.

A trust should be created preferably at all times by instrument in writing even if or when it is created *ex lege*. At times the Trust Act and other laws in Malta may provide for the creation of a relationship of trust and hence the trust becomes a statutory one. The Act<sup>6</sup> also contemplates the creation of a trust by means of a judicial decision. The question whether this extends to an arbitral award is moot. But if it does not, it begs the question, why not? And, if it does, then why would it have to depend on the definition of ‘judicial decision’? This aspect of trust creation deserves to be refined by the legislator.

In the opinion of the present writer none of these methods are the preferred manner in which a trust should be created. For the nonprofessional, the uninformed and the inexperienced individual, these scenarios are singly or collectively, fertile ground for error, confusion, and misunderstanding and certainly for abuse. The terrain then becomes the breeding ground for ‘naive’ and ‘passive’ so-called aggrieved participants aided possibly by third party ambulance chasing lawyers and advisors to cultivate and manufacture ‘claims’ against settlors, trustees, protectors and beneficiaries. The disservice to the institute of the trust is immeasurable and uncontainable. The following two episodes illustrate the concerns expressed above.

In an application filed before the Court of Voluntary Jurisdiction in 2009, a claim was brought by some disgruntled minority shareholders against a company in liquidation and against the liquidator arguing that the assets of a company in liquidation are held on trust by the liquidator and that the liquidator is the trustee. It was argued that this ‘trust relationship’ was created by ‘law’. Their agenda was to have the liquidator replaced and the assets placed in the hands of a person acceptable to them. The strategy was ‘political and commercial’ rather than one enshrined in trust law; except of course, unless it was a manifestation of ignorance of the law. In any event, they effectively tried to short cut the rules and processes laid down by company law. The basis of their claim was as flawed as it was audacious. The Court quite rightly rejected their claim *in toto*.

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<sup>5</sup> Chapter 331 of the Laws of Malta, Trust and Trustees Act, Article 7

<sup>6</sup> *Ibid*.

In another application filed before the Court of Voluntary Jurisdiction in February 2009, a settlor/beneficiary and a protector filed an application against the trustee claiming that an asset had been settled in trust notwithstanding that at the point in time when the settlement is alleged to have been made, the Trust Act had not entered into force, the trust in question had not been created and concrete evidence had been submitted to indicate that no such settlement had in fact been made.

The Court consumed more than six months of hearings and to date has failed to deliver judgment on a matter where quite plainly and, prima facie, the court has no jurisdiction.

In the light of these known experiences before Maltese courts, it is strongly advised that the creation of a trust should be made by the drawing up of a trust deed or a deed enrolled in the records of a notary public where the trustee and the settlor are related or have known each other for more than a decade<sup>7</sup>. The deed should be signed by the Settlor, the Trustee, the Protector, if any, and preferably by two witnesses. Fancy modes of creation such as by oral declaration or by unilateral declaration should be avoided like the plague particularly in 21st Century society where, as a rule, one's word is regrettably no longer one's bond.

The trust deed should be as specific as possible. The key provisions in a trust deed are those that regulate:

- (a) the appointment and removal of trustees;
- (b) the appointment and removal of protector/s;
- (c) the powers and obligations of trustees and of protectors;
- (d) the scope and object of the trust;
- (e) the investment policy of the trust property, if applicable;
- (f) an arbitration clause for disputes arising among the participants.

The latter is a much preferred form of settlement of disputes especially among foreigners setting up trusts as they can be involved in selecting an internationally tried and tested arbitration centre and in the appointment of arbitrators who are well versed and have a proven record in both arbitration and trust law matters. It is by far a preferred mode of dispute resolution than the luck of the draw at a court registry case docket system.

It is advisable to formulate trust deeds on templates drafted by trustees and lawyers with considerable experience in trust law. Experimenting and tinkering is dangerous, although circumstance specific drafting is encouraged and often vital.

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<sup>7</sup> A decade is too long a requirement. Half that time is more than sufficient.

### **3. THE PARTICIPANTS OF A TRUST**

#### **3.1 The Settlor**

The Settlor may be an individual or a juridical person and indeed may be another trust. The person creating a trust must have legal capacity to settle property otherwise the relationship does not arise and no trust is created. Trust creation may not necessarily occur contemporaneously with settlement of property in trust and may indeed be a separate act. However, some property, no matter how nominal, is required to be settled into trust. This should occur in a reasonably short time following the conclusion of the trust deed so as not to run the risk of having no trust at all.

Trusts are created for the administration of property by a trustee for the benefit of beneficiaries. As a rule, the Settlor is also the beneficiary and many times he or she is the sole beneficiary.

#### **3.2 The Trustee**

In the Malta Trust, the trustee is typically a company and is licenced by the Malta Financial Services Authority to provide those services. In the case of a so-called private trustee, this will be an individual who is either related to or who has known the Settlor for at least a decade.

Once property is settled into the trust, it ceases to be owned by its owner and it becomes the property of the trust - not of the trustee.<sup>8</sup> The trustee, however, has the duty and the power to manage it or to preserve it (sometimes these are quite contradictory tasks or objectives, hence the need for very specifically worded trust deeds) for the benefit of the beneficiary.

At times, there may be more than one trustee. In the case of a Malta Trust, one of the trustees must be at least a licenced trustee. The MFSA places the burden of the office squarely on the shoulders of the licenced trustee regardless of the number of other trustees or their experience. In such cases, rules regulating proceedings of the Board of Trustees must be clear and preferably written in the trust deed as though they were the provisions of proceedings concerning directors' meetings contained in the Articles of Association of a limited liability company.

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<sup>8</sup> This is a controversial statement but the jury is still out on this aspect. See section below on the legal personality of the Malta Trust.

### **3.3 The Protector**

This post is usually occupied by a person of trust or close friend or relative to the Settlor. The Protector is in essence the Trustee's supervisor and guardian to both the Settlor and, possibly but not necessarily, also for the beneficiaries. The Protector is typically not given a veto over the powers exercised by the Trustee but it's as close as one gets to it because the Protector's written advice and counsel is usually stipulated as a key requirement prior to the exercise of any material decision taken by the Trustee. This mechanism is one of the most effective forms of control retained by the Settlor. It's almost management by remote control especially when coupled with a document known as 'Letter of Wishes' issued by the Settlor. It may be more than a single document and issued throughout the duration of the Trust. It contains precisely what its name indicates namely a list of wishes and considerations of the Settlor on how the trust property should be invested or employed. It is not binding on the Trustee or the Protector but it would be very courageous of them to ignore the contents of these letters, unless in those instances where the wishes are irregular, contrary to public policy or in breach of the law.

### **3.4 Beneficiaries**

There is no trust without a beneficiary or beneficiaries. It is necessary to nominate them and it is necessary that they are identifiable. They do not have to be individuals but if they are, they do not have to be born or to exist at the moment of the trust settlement. However, in the event that a trust has no beneficiaries the trust will fail.

Beneficiaries have an interest in a trust. This interest is typically regulated by the terms of a trust deed such as whether it is permissible to charge it or not. The interest is deemed movable property under Maltese law and it may of course be inherited.

The Settlor is typically a beneficiary and often the first and only one. His or her heirs follow upon the demise thereof. The Settlor also usually drafts the conditions in the trust deed attached to the appointment and removal of beneficiaries including the manner in which, how, what and when beneficiaries may enjoy their interest.

If the trust deed allows it, a beneficiary may sell, transfer or deal the interest in the Malta Trust. The interest in a Malta Trust may be disclaimed by a beneficiary. If disclaimed in whole then the disclaimer is irrevocable whereas when it is made in part the disclaimer may be revoked if the terms of the disclaimer allow it. This distinction made by the law is not easily reconcilable.

#### **4. THE LEGAL PERSONALITY OF THE TRUST**

In trust law, this is a controversial topic. It is entirely a non-common law issue. Under Maltese law, entities ranging from village band clubs to audit firms to limited liability companies traditionally enjoy a legal personality separate and distinct from their members. Is this the case with the Malta Trust? The present writer endorses the view that it is.

##### **4.1 The Civil Code - Second Schedule<sup>9</sup>**

The most recent substantive contribution made to our law on legal personality is the enactment of the Second Schedule. It was designed to regulate organisations including their sub-divisions, as defined therein, and private foundations. But, the Second Schedule also represents a legislative effort to define the concept of legal personality. To a degree it is a bold attempt to define the proverbial elephant confident, falsely or otherwise, in the notion that to do so is progressive development of law. Thus, it also catches the concept of an entity such as the Malta Trust and together with the Trust Act, it is indeed a legal source which affirms the legal personality of a Malta Trust for the following reasons.

The first reason is that as a matter of principle, there is no rule at Maltese law which prohibits the Malta Trust from enjoying its own separate legal personality. The following statement is offered by the Second Schedule –

A universality of things which are appropriated to achieve a lawful purpose having a form recognised by law, and which is capable of being a legal person in terms of law.

One would think this a suitable definition of the concept of Malta Trust. But, it is actually a definition of an ‘organisation’ in the Second Schedule.<sup>10</sup> Such is the affinity between the two concepts at law.

The Malta Trust is not an organisation as contemplated by the Second Schedule but the provisions contained therein enunciate rules of law that may well apply to the Malta Trust. To some extent the Second Schedule is an effort to codify general principles of law concerning the legal personality of juridical entities, but the rules it has enunciated also capture the Malta Trust.

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<sup>9</sup> Chapter 16 of the Laws of Malta, hereafter referred to as the Second Schedule

<sup>10</sup> See Section 1(1) of the Second Schedule

Upon analysis, the law provides that an organisation which - (i) is established for a lawful purpose by means of a written instrument such as a deed; (ii) is conferred a patrimony that naturally includes assets as well as liabilities; (iii) holds its patrimony separate and distinct from any other patrimony or person; and, (iv) is administered by a governing body vested with the requisite powers, shall have legal personality at law. Legal personality subsists when the entity is recognised at law or is established in accordance with 'a special law'.

All of these rules are set out in clause 1.2 of the Second Schedule in very clear terms and may well be applied to the concept of the Malta Trust. Clause 1.6 also rightly contemplates such entities to be public or private which is exactly the typical form taken by a Malta Trust.

For some archaic reason, the Second Schedule has elected to make the registration of organisations (as defined by it) at the Public registry a mandatory pre-requisite for legal personality. This is a pedantic and unnecessary measure particularly in the light of the position established by leading judgments on the topic. It certainly does not stop the local football club from having a legal personality nor the Malta Trust from being legally capable of acquiring its own. Many Malta Trusts are not registered with any authority in Malta but some are/may well be so registered. Surely, those that are registered in a notarial deed at the Public Registry cannot be said to have legal personality whereas those which are not so registered, do not. There is no such thing in life as being half pregnant.

The second reason is made up of a number of elements which characterise an entity capable of having its own legal personality. These are found across a whole range of clauses in Title I to the Second Schedule. The most relevant, in no particular hierarchical order, are:

- (i) **Purpose:** The entity is required to have a lawful purpose and when it is private it must be for the benefit of persons which are identified or capable of being ascertained.
- (ii) **Name:** The entity is required to have a name on the day it is established and under which it will operate.
- (iii) **Malta Address:** The entity is required to have an address in Malta as its principal place of activity where it may be notified and where it keeps its records.
- (iv) **Governing Body:** The entity is required to be administered by a management board composed of, inter alia, by 'trustees' - in the language of clause 4.4 of the Second Schedule.
- (v) **Representation:** The entity shall be represented legally and judicially in the manner provided by its constituting documents or by law as may be the case. The authority to delegate administrative powers is also set out.

The elements listed above are naturally not the only rules set out in the Second Schedule applicable to organisations and foundations. They are, however, very much the DNA of the concept of legal personality and when tested against the concept of the Malta Trust - they measure fully. Interestingly, there are at least two instances in the Second Schedule which contribute to this conclusion.

The first is found within a discussion of conversion of entities from one legal form to another. Article 21.4 provides that when a legal person (which according to article 3 of the same Schedule is conferred with legal personality) is converted into a trust, the trustee succeeds to the rights and obligations of the said legal person.

The real issue becomes - is legal personality lost upon conversion into a Malta Trust? Is it incorrect to argue that legal personality survives post conversion, particularly where contractual rights and obligations succeed and subsist?

The second is article 26 which clearly stipulates that foundations are not trusts. The inference being that the Second Schedule clearly sees the Malta Trust, the Foundation and the Organisation as three separate entities under our law enjoying, however, common characteristics including, it is submitted, separate legal personality.

#### **4.2 The Trust Act<sup>11</sup>**

Independent juridical personality should be seen as an attribute of the Malta Trust. Without it our trusts would be that much poorer and weaker as a legal instrument, particularly within our non-common law traditions and culture.

The Trust Act contains significant provisions which in the opinion of the present writer establish, forcefully, the legal personality of the Malta Trust. The relevant section is Article 3 of the law. Article 3(1) determines the existence of a trust relationship when the trustee holds property that once belonged to someone else, '...as owner or has vested in him property'. The choice of words is telling. The trustee is not the owner of the property. He has an obligation to deal with it as though it were, but not as though it is, his own. This is not a distinction without a difference. The property is not his in any capacity whatsoever.

Article 3(2) lays down the rule that trust property is a separate 'estate' or 'patrimony' from that of the trustee and from that held for other trusts.

Article 3(3) stipulates the key attribute of the concept of legal personality at law - the right '...to sue and to be sued in respect of the trust as well as to act in all matters concerning the trust'. Furthermore, sub-article (5) provides that when property is required by law or otherwise, to be registered, such as in the case of

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<sup>11</sup> Trusts and Trustees Act 2005, Chapter 331 of the Laws of Malta

immovable property, the registration must clearly indicate that it belongs to a Malta Trust and not simply to the trustee.

The legal proceedings filed or the registration of property must be Malta Trust specific. The attribution of legal personality thus lies with the specificity requirement and not with the element of generality.

Article 3(4) ring fences trust property from all else that concerns the trustee. It ensures that no claim is made by the trustee's third party creditors against it or that it gets mixed up somehow in his/her/its bankruptcy or dissolution proceedings. It also makes it clear that it does not form part of matrimonial regimes and similar legal scenarios that may apply to a trustee during his marriage or indeed following his demise.

In a single provision of the law, the Trust Act has done more for the cause of the separate legal personality of the Trust than any other legal source.

## **5. Bettina Vossberg pro et noe v Equinox International Ltd et<sup>12</sup>**

This 2102 judgment by the Court of Appeal merits some consideration because its singularity on the topic makes it relevant. It's unlikely that this would have been the case had there been several judgments on the law of trusts. It is not unreasonable to say that the Vossberg matter is less of a case on trust law and more a contribution on the Maltese 'actio pauliana' and creditor's claims for maintenance.

### **5.1 Facts in brief**

Plaintiff, a wife alleging that her husband owes her child support and that he has insufficient funds in Malta with which to do so, or at least to secure the claim, sues for the annulment of a settlement in trust of a paraphernal residential property in Malta. This is done naturally to have an asset to seize in order to secure the alleged matrimonial claim. The Trustee and the husband are both sued. Alleged fraud is the basis of the action.

The defence denies wrongdoing and submits evidence that (a) there is no outstanding amount due and (b) in any event, the other assets in Malta of the husband to make good for any claim are more than adequate, hence the action is vexatious.

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<sup>12</sup> Court of Appeal, ( November 2012

At the time of writing, the matter is still sub-judice, pending an application for re-trial. The operative part of the twenty seven page appellate judgment runs from the latter part of page 19 to page 27. It deals with two important points that concern purely trust law, the other issues concern the *actio pauliana*.

First, it distinguishes between the establishment of a trust and settlement in trust. The former relates to the creation of a trust, which basically means signing a trust deed and settling a nominal amount (as happens in most cases) and the latter refers to an occurrence that may take place once or several times throughout the lifetime of a trust. The Settlor transfers by private writing or public deed (depending on the nature of the property and the legal requirement for formal validity) an item into the Malta Trust.

Second, the court felt the need to make this distinction in order to address the issue as to whether the settlement of the residential property was onerous or gratuitous as that has a direct impact on third party responsibility in terms of the *actio pauliana* under Maltese law.

The court's language on the distinction is regrettably unclear and unhappy.<sup>13</sup> But, as a general rule, in most cases settlements in trust are gratuitous and no price is paid by the Malta Trust otherwise it is not a settlement in but an acquisition by the Malta Trust and that changes the legal scenario.<sup>14</sup>

The Court of Appeal quite rightly rejected the trustee's view that the settlement of the residential property in the trust was onerous. The court held that it was indeed gratuitous and not just because no price had been paid for it but because such is the nature of settlements in trust.

The Court held that the settlement was improper and that the property had to revert to the Settlor. It came to this conclusion, however, on the basis that the husband had failed to show the court that he had other sufficient assets in Malta to secure the claim. Indeed, the court went as far as to say that he did not make use of the institute of benefit of discussion which may well have been helpful in the circumstances. This basis is founded on a matter of fact which is challenged by the

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<sup>13</sup> See page 21 et seq. The court speaks of the onerous nature of the contractual relationship between the Settlor and the Trustee in the creation of a trust and compares it to the gratuitous or otherwise nature of a settlement in trust. The two, however, are not related. There is an underlying inference that the court wanted to make this point but it fails to do so crisply, hence the muddled drafting of the judgment. The text dilutes the focus on the main issue namely:

(a) the settlement in trust of the settlor's residential home for no consideration is in the ordinary course of trust business;

(b) in the Vossberg case the relevant question is, was this done fraudulently?

The gratuitous settlement of the property is not per se evidence of fraudulent behaviour. Indeed fraud may be present even where the settlement in trust is made onerously.

<sup>14</sup> A trust may purchase property from a settlor but that would be an acquisition just as it were buying from any third party. It is useful to bear in mind that there may be more than one settlor to a trust. There is a difference between a settlement in trust and an acquisition by a trust and the circumstances in which this occurs is neither immaterial nor irrelevant. The context deserves due consideration.

husband in the retrial stage, but that is neither here nor there for the purposes of this piece.

It would be incorrect and extreme to label this case as a landmark judgment on trust law in Malta. The only claim it might have to glory would be that it's probably the first to be delivered by the Court of Appeal<sup>15</sup> and that it is recent. The Vossberg case properly belongs among the dicta on the actio pauliana and not in the emerging annals on trust law.

## **6. Some Key Principles**

The following is not an exhaustive or an immutable list of principles that apply to a Malta Trust but it does represent some of the key basic principles on trusts under Maltese law.

- (i) Malta Trusts are mainly created by written instrument but may also be created by law or by a judicial decision.
- (ii) Settlements of property in trust means that a transfer of ownership has occurred. It has the effects of a sale or of a donation but it is neither. Essentially, it is a sui generis legal concept.
- (iii) Property must be settled into the trust.
- (iv) Beneficiaries must be either identified or identifiable. They need to exist at the time of distribution.
- (v) Trustees must be appointed and a Malta Trust cannot survive without trustees.
- (vi) A Protector may be appointed but there is no mandatory rule to make such an appointment.
- (vii) Interest in a Malta Trust is movable property and may be charged, transferred and inherited.
- (viii) Legal personality is an attribute of the Malta Trust.

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<sup>15</sup> This is subject to correction, given the Maltese practice not to publish judgments in a regular, transparent, referenced and easily accessible manner.