

# Article

## Effective firewall legislation—Cook Islands

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### Abstract

Ordinary principles of international law require foreign judgments to be recognized and given effect in most offshore jurisdictions. A few jurisdictions have passed special legislation reserving certain areas of their law for application of domestic law only. The Cook Islands amended its law in 1989, reserving certain areas of law relating to Cook Islands international trusts for Cook Islands law only, prohibiting recognition and enforcement of foreign decisions in these areas. Those reservations have been considered by Cook Islands courts. Recent decisions of the United Kingdom Family Courts recognized by the Jersey High Court are examined and the conclusion is reached that a Cook Islands court would not have been able to reach the same decision if the trusts were Cook Islands international trusts.

The recognition and enforcement of foreign judgments in offshore jurisdictions is a complex area of law. In most cases, a careful analysis of the common law, constitutional, international and treaty law for that offshore jurisdiction is required, together with consideration of the nature of any judgment likely to be sought. In several recent cases the Jersey Royal Court ('Jersey Courts') has given effect to judgments of the English High Court (Family Division) relating to trusts settled in Jersey ('Jersey trusts'). These decisions should be seen as a warning to trustees

and lawyers who assume offshore jurisdictions do not recognize foreign judgments. The Jersey decisions are consistent with established principles of international law applying in the absence of a jurisdiction having special statutory protection against recognition of foreign judgments.

This article considers whether the results might have been any different if the relevant trusts had been established in a jurisdiction with statutory protection against recognition of foreign judgments. It briefly examines the ordinary law relating to enforcement of foreign judgments in the Cook Islands, reviews the protective provisions of the International Trusts Act 1984 (Cook Islands) ('ITA') and then applies this law to each of the Jersey decisions.

The Cook Islands is not a signatory to any treaty for mutual recognition of foreign judgments, nor foreign arbitration awards. Nor is it a 'scheduled territory' for the purposes of section 426 of the Insolvency Act (UK) 1986. However, English common law and constitutional law provide other avenues for recognition and enforcement of foreign judgments. The procedure for recognition and enforcement of foreign judgments for a sum of money (subject to jurisdiction and other exceptions of limited application) is fairly simple. In addition, under normal principles of comity, Cook Islands courts also have an inherent jurisdiction to recognize and give effect to foreign judgments.<sup>1</sup> Further, there are a number of what are loosely called 'Imperial Statutes' setting out mutual procedures for recognition and enforcement of

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1. See Dicey *et al.*, *Conflict of Laws*, 14th edn, 2007.

judgments between former members of the British Commonwealth which might apply depending on argument as to constitutional succession taking into account that the Cook Islands became independent of New Zealand, rather than the United Kingdom (UK). The Cook Islands also has provision in its own constitutional law for mutual recognition and enforcement of certain decisions of the New Zealand High Court.<sup>2</sup>

While this level of exposure to foreign judgments was minimal in comparison to other English law jurisdictions, the Cook Islands government determined that protection of the various unique provisions of Cook Islands trust law against contrary foreign decisions was fundamental to the long-term success of the jurisdiction. Therefore, in 1989 a decision was made to enact statutory provisions to override the existing body of law relating to recognition and enforcement of foreign judgments as it affected trusts. These provisions, contained in section 13D, 13H and 13I of the ITA 1984 relate only to specific reserved areas of Cook Islands law relating to trusts. The amendment follows many other jurisdictions which reserve areas of law under 'public policy' for their own courts. For example, Greece, India, Mexico, Spain and Thailand among others, deny recognition of foreign judgments if the cause of action does not exist in their own jurisdiction. Other countries, such as Indonesia, simply deny recognition of all foreign judgments.<sup>3</sup> We see the same principle adopted by the State of New York in its Libel Terrorism Protection Act (May 2008) which prevents enforcement of a foreign libel judgment in a New York court, unless the New York court first determines that the free speech and freedom of information protection guaranteed by the First Amendment and the New York Constitution apply equally in that foreign jurisdiction.

The provisions limiting recognition and enforcement and reserving areas of Cook Islands law are summarized as follows:<sup>4</sup>

Section 13D of the ITA provides that notwithstanding existing law, no foreign judgment may be recognized or enforced to the extent that it:

- a. is based upon the application of any law inconsistent with the provisions of the ITA, or
- b. relates to a matter or particular aspect that is governed by the law of the Cook Islands.

Sub clause (a) requires a comparison of the law applied in the foreign judgment, with the law contained in the ITA. If there is any difference, the foreign judgment cannot be given effect or recognized. The ITA codifies Cook Islands law in relation to fraudulent transfer as it relates to trusts, and that has been the main area for litigation to date. However, it also modifies other areas of trust law which rely for their ultimate effectiveness on section 13D. Examples are the repeal of the rule in *Saunders v Vautier* (1841) Cr & Ph 240, [1835–1842] All ER Rep 58,<sup>5</sup> the replacement of the perpetuities regime with a period of choice,<sup>6</sup> authorization of settlor participation,<sup>7</sup> the protection of spendthrift trusts<sup>8</sup> and a direction to courts to apply different law if necessary to validate a trust.<sup>9</sup>

Sub clause (b) restricts enforcement or recognition of a foreign judgment when it deals with matters of law reserved for Cook Islands law. These reserved areas are set out in section 13H(1), ITA and include issues as to:

- the capacity of any settler;
- any aspect of the validity of the trust, or a disposition to the trust;

2. Section 173, Cook Islands Act 1915.

3. There is an excellent discussion of these principles in J. Weems, 'Guidelines for Enforcing Judgments Abroad', 21 *IBL* 11, 509–512.

4. See Appendix 1 for full text of provisions.

5. ITA s 10.

6. ITA s 6.

7. ITA s 13C.

8. ITA s 13F.

9. ITA s 5.

- the administration of the trust, including questions as to powers, obligations, liabilities and rights of trustees and their appointment and removal; and
- the existence and extent of powers, including powers of variation and the validity of any exercise thereof.

These reserved areas are to be determined according to the laws of the Cook Islands, without reference to the laws of any other jurisdictions with which an international trust or disposition may be connected.

Section 13H(2) restricts the application of section 13D so that amongst other matters, section 13D:

- does not affect the recognition of foreign laws prescribing generally (without reference to the existence or terms of the trust) the formalities for the disposition of property;
- does not validate any disposition of property which is not owned by the settlor;
- does not validate a disposition of property to a trust which is void ab initio; or
- does not validate a testamentary disposition which is invalid according to the law of the testator's domicile.

Section 13I further extends the protection for trusts against foreign judgments. It provides that no trust (and no disposition to a trust) is void, voidable, liable to be set aside or defective, nor is the capacity of a settlor to be questioned, by reason that:

- a. the laws of any foreign jurisdiction prohibit or do not recognize the concept of a trust;
- b. the international trust or disposition avoids or defeats rights conferred by the law of a foreign jurisdiction upon any person; or
- c. the laws of the Cook Islands or the provisions of the ITA are inconsistent with any foreign law.

There are several points to note about these provisions:

1. The general body of law relating to recognition and enforcement of foreign judgments in the Cook Islands remains in force and takes effect subject only to these provisions;
2. The protection applies only to foreign judgments relating to trusts, and even then, does not apply to all such foreign judgments. For example, it is considered that if a foreign court gave a judgment based on correctly applied Cook Islands law, the restriction in section 13D(a) would not apply;
3. The protection is not limited to dispositions to a trust. It extends to many other areas of trust law; and
4. The protection does not protect a transfer to a trust from a person who has no title—such a person has nothing to protect.

The above provisions have been considered in obiter dictum in two cases before the Cook Islands courts.

In *A v E and B et al.* [2002] CIHC 29, [2002] CICA 29,<sup>10</sup> the plaintiff alleged several dispositions made to a trust were fraudulent transfers, and presented the High Court with judgments from the United States ('US') Bankruptcy Court to that effect. In interlocutory proceedings the plaintiff sought access to documents otherwise protected by professional privilege on this basis.

The High Court considered the rulings of the US Bankruptcy Court as to fraudulent transfer, and determined not to take them into account as the present application involved different issues and different standards of proof and was to be determined on the basis of a different governing law. Further, it went on to consider the application of section 13D, ITA and came to the conclusion that the wording of this provision was sufficiently wide to prevent the Court relying on the US decision as to the establishment of the trust being a fraudulent act.

10. High Court & Appeal Court, Cook Islands 7 September 2002, 10 October 2002, David Williams J.

The provisions were considered again in *Application for Directions by Trustee*.<sup>11</sup>

In this case a third party sought to set aside a disposition to a Cook Islands trust, and had obtained from a US court an injunction and a *Lis Pendens* notice/order over trust assets located within the US. The trustee wished to appear in the US court to defend these orders and applied to the High Court (of the Cook Islands) for a ruling as to whether it would lose the benefit of section 13D, ITA if in so doing it submitted to the jurisdiction of the US court. The High Court ruled that section 13D would continue to apply where the trustee did so submit, even if that resulted in a judgment against the trustee or any assets of the trustee.

Turning now to the Jersey cases, what would the result have been if these trusts had been established in the Cook Islands, instead of in Jersey? I have set out in summary the relevant Jersey Court cases and have commented on how a Cook Islands Court might have responded to judgments of the English family courts in each case.

***Minwalla v Minwalla and others***  
**[2004] EWHC 2823 (Fam),**  
**[2006] 7 ITELR 457<sup>12</sup>**

In divorce proceedings brought in the English High Court's family division (the 'English Court'), the English Court found a Jersey trust to be a sham, the husband to be the beneficial owner of the trust assets, and ordered the trustees to transfer the trust assets to the wife. The Jersey Court was asked to give effect to the decision of the English Court. The Jersey Court determined that the issue of sham was a question for Jersey law, not English law. However, it concluded that it would be fair to give effect to a part of the English judgment that ordered the transfer of assets to the wife.

If proceedings had been brought in the Cook Islands, both branches of sections 13D would prevent

recognition or enforcement of the decision held in the English Court. The ITA specifically permits participation by the settlor<sup>13</sup> so that there is a clear difference between Cook Island and English law as to sham arguments. Further, Section 13H(1)(b) reserves issues as to the validity of the trust for Cook Island law. A Cook Islands court would therefore not recognize or give effect to the UK decision.

***Re The A Trust. FM v ASL Trustee Company Ltd*** [2006] JRC020A,  
**[2006] 9 ITELR 127**

The trust held the freehold of property in London, in part of which the wife and the children lived. Again in the English Court, a number of orders were made, these included:

- the trust was varied so as to extinguish any interest that the husband might have in the trust; and
- the husband was ordered to transfer to the wife the benefit of a loan to the trustee.

The wife applied to the Jersey Court for an order to recognize and enforce the English Court orders in Jersey. Although the Jersey Court held that this was a trust administered in Jersey, with a Jersey trustee and governed by Jersey law, and that it was a matter of discretion whether to give effect to the foreign courts order or not, it recognized the basis of the English Court decision and decided that all the assets in the trust should be made available for the exclusive benefit of the wife and children.

In the Cook Islands, variation of the trust falls under the reserved area in section 13H(1)(d). The change in treatment of the loan falls under the reserved area in section 13H(1)(b). Both would prevent recognition or enforcement of the English Court decision.

11. Unreported High Court decision, Cook Islands 8 June 1998, Quilliam C.J.

12. Noted in *Trusts & Trustees*, Vol. 12, No. 1.

13. See n 7 above.

### **Re The H Trust. X Trust Company Ltd v RW and others [2006] JRC057, [2006] 9 ITELR 133**

The wife of the Settlor obtained various orders from an English Court against the husband Settlor and the trustee of a Jersey trust, including an order that she not be removed as a beneficiary. The trustee's sought directions from the Jersey Court as to its decision not to submit to the jurisdiction of an English court in divorce proceedings. The Jersey Court noted that if the trustee did not participate in the English court proceedings, the Jersey Court retained considerable discretion as to how to treat the foreign order, whereas if the trustee submitted, the foreign order was likely to be enforced without reconsideration of the merits.

Submission by a Cook Islands trustee to jurisdiction does not limit the operation of section 13D as previously illustrated in the unreported decision given by Quilliam CJ in *Application for Directions by Trustee*. Questions as to exercise of powers by a trustee are reserved for Cook Islands law.<sup>14</sup>

### **In the matter of the B trust [2006] JRC185**

Again, the Jersey Court considered an order of the English Court to the effect that a Jersey trust be varied this time under an amendment specifically enacted to deal with the problem. The Jersey Court was of the opinion that the amendment was not only unclear, but insufficient without 'very clear and express words' to affect the doctrine of comity, and once again gave effect to the English Court's order.

In the Cook Islands, variation of a trust falls under the reserved area in section 13H(1)(d), and would prevent recognition or enforcement of the English decision.

In each of the above cases, the plaintiff is free to file *de novo* proceedings in a Cook Islands court. The Cook Islands judiciary is appointed from senior New Zealand High and Appellate Court judges and the bulk of Cook Islands trust law follows

New Zealand (and English) trust law. The exceptions include the ability to exclude the rule in *Saunders v Vautier*, the repeal of perpetuity period, and the ability of a settlor to participate in trust activity without exposing the trust to the sham doctrine. There are also strict time limits imposed where claims are made against trust property by third parties, including claims based on constructive trust principles.

### **Summary**

In each of the above cases it is submitted that a more favourable result could have been achieved if a jurisdiction with effective statutory firewall provisions had been chosen as the situs of the trusts, instead of Jersey. This point is relevant whether the chosen law rejects forced inheritance, negates the rule in *Saunders v Vautier*, allows an extended perpetuity period, or protects trust assets from third party claims.

It is not suggested that simply choosing the Cook Islands as an offshore jurisdiction will provide complete protection for a trust. There are several methods of attacking trusts, some of which negate choice of jurisdiction. The lesson is that where there is potential for a party to challenge any part of a trust structure in home courts, the selection of an offshore jurisdiction with effective firewall provisions (and there are not that many) is one of the important ingredients of successful offshore structuring.

### **APPENDIX I**

#### **Foreign judgments not enforceable**

**13D.** Notwithstanding the provisions of any treaty or statute, or any rule of law, or equity, to the contrary, no proceedings for or in relation to the enforcement or recognition of a judgment obtained in a jurisdiction other than the Cook Islands against any interested party shall be in any way entertained, recognized or enforced by any

14. See s 13H(1)(c) and (d).

Court in the Cook Islands to the extent that the judgment:

- a. is based upon the application of any law inconsistent with the provisions of this Act or of the Trustee Companies Act 1981–1982; or
- b. relates to a matter or particular aspect that is governed by the law of the Cook Islands.

### **Matters determined by governing law**

**13H.(1)** All questions arising in regard to an international trust which is for the time being governed by the laws of the Cook Islands or in regard to any disposition of property upon the trusts thereof including, without prejudice to the generality of the foregoing, questions as to:

- subject to subsection 2(c), the capacity of any settlor;
- any aspect of the validity of the trust or disposition or the interpretation or effect thereof;
- the administration of the trust, whether the administration be conducted in the Cook Islands or elsewhere, including questions as to powers, obligations, liabilities and rights of trustees and their appointment and removal; or
- the existence and extent of powers, conferred or retained, including powers of variation or revocation of the trust and powers of appointment, and the validity of any exercise thereof,

are to be determined accordingly to the laws of the Cook Islands, without reference to the laws of any other jurisdictions with which an international trust or disposition may be connected.

(2) Subject to the provisions of this Act subsection (1) shall:

- a. not validate any disposition of property which is neither owned by the settlor nor the subject of a power in that behalf vested in the settlor, nor does

that subsection affect the recognition of foreign laws in determining whether the settlor is the owner of such property or the holder of such a power;

- b. take effect subject to any express contrary term of the trust or disposition;
- c. as regards the capacity of a corporation, not affect the recognition of the laws of its place of incorporation;
- d. not affect the recognition of foreign laws prescribing generally (without reference to the existence or terms of the trust) the formalities for the disposition of property;
- e. not validate any trust of real property or disposition or transfer of real property situate in a jurisdiction other than the Cook Islands which is void ab initio accordance to the laws of such jurisdiction;
- f. not validate any testamentary trust or testamentary disposition which is invalid according to the laws of the testator's domicile.

(3) A disposition of property located at a place beyond the Cook Islands to an international trust or a trust that shall subsequently become an international trust shall if made in accordance with the law of that place governing such disposition be deemed to be a valid disposition notwithstanding any law of the Cook Islands to the contrary.

### **Exclusion of foreign law**

**13I.** Without limiting the generality of section 13H, it is expressly declared that no international trust governed by the laws of the Cook Islands and no disposition of property to be held upon the trust thereof is void, voidable, liable to be set aside or defective in any fashion nor may relief be had under section 13B, nor is the capacity of any settlor to be questioned by reason that:

- a. the laws of any foreign jurisdiction prohibit or do not recognize the concept of a trust either in part or in whole; or

- b. the international trust or disposition avoids or defeats rights, claims or interests conferred by the law of a foreign jurisdiction upon any person or, contravenes any rules or foreign law or any foreign judicial administrative order or action intended to recognize, protect, enforce or give effect to any such rights, claims or interests; or
- c. the laws of the Cook Islands or the provisions of this Act or the principal Act are inconsistent with any foreign law.

### Note

I received a copy of the latest decision of the Jersey Royal Court (the Court) in *Mubarak v Mubarak* after completing this article. As I read it the most that can be said of this decision is that the Court will not

normally give effect to a decision of the UK Family Court directing variation of a trust if it requires an alteration to the trust (rather than a variation). Presumably it will however, recognize a decision to vary the trust. The decision is subject to an exception, being where the trustee has submitted to jurisdiction. The issue as to jurisdiction places an enormous practical burden on trustees. It also begs the question as to what the Jersey Royal Court will do if the UK court properly finds jurisdiction over the trustee irrespective of voluntary submission by the trustee. This issue has been resolved in the Cook Islands. Ultimately, the Court once again gave effect to the UK decision, although relying on the rule in *Saunders v Vautier* to do so. (This rule can be negated in the trust deed under Cook Islands law.) The latest ruling of the Jersey Royal Court does not provide, in my opinion, an acceptable basis for offshore planning.