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## **THE USE OF PROTECTORS IN ASSET PROTECTION TRUSTS**

Most modern offshore asset protection trusts have a protector. This article provides a brief discussion on the use of protectors in Cook Islands International Trusts.

It is impossible to provide a universally accepted definition of what a protector is. The office of protector is not a traditional part of trust law and most countries do not have legislation that defines or recognizes the position. Generally a protector is considered to be a watchdog, overseeing the trustees and ensuring the settlor's intentions are carried out.

The nature of the powers, duties and functions of a protector usually depend on the terms of the trust instrument as there is very little case law that offers useful guidance. More recently some countries have enacted legislation that recognizes and to some extent defines the role of protector.

The Cook Islands was one of the first countries to provide a statutory definition for a Protector. Section 2 of the International Trusts Act 1984 (the "Act") provides that a protector is a person who has the power to appoint or remove trustees or who has the ability to control certain trustee decisions (including a power to veto trustee decisions).

Further, to provide flexibility for settlors who desire the role of protector be modified for a special purpose such as amending the trust instrument in response to changes in estate tax laws, a protector is also a person who is appointed to the office of protector established by a trust instrument.

There are a number of different types of powers typically given to protectors. The most common power is the power to remove and appoint trustees. Another common protector power is the power to approve or veto certain trustee decisions such as trustee decisions to make certain types of investment, to make amendments to the trust instrument or even to make distributions. Protectors may also be given other affirmative powers such as powers to amend the trust instrument or powers of appointment.

A protector's powers can be either affirmative such as a power to compel a trustee to carry out a certain action or negative such as a power to veto an action of the trustee. Negative protector powers are more commonly used by US trust attorneys in asset protection trusts for a variety of reasons. One important reason is to prevent a court ordering a protector to remove the foreign trustees if there is litigation against a trust.

As a protector can have extensive powers and play an important role in the administration of the trust it is important to consider whether the protector's powers are personal or fiduciary in nature. This distinction is very important because it determines what obligations the protector has to the beneficiaries.

If a protector's powers are personal then the protector can use them as they like, including for their own benefit, without consideration for the beneficiaries. In contrast, if a protector's powers are fiduciary then they have a duty of loyalty to the beneficiaries and must take into account the beneficiaries interests when exercising their powers.

The issue of whether a protector's powers are personal or fiduciary is a matter for interpretation by the courts. Most courts that have considered this issue have not surprisingly preferred the view that protector powers are fiduciary. However, it is still generally recognized that the nature of the protector's powers will depend on the settlor's intentions when they settled the trust. If there is no clear intention it is likely a protector's powers will be fiduciary because the powers relate to a trust relationship.

The Cook Islands has taken a different approach that encourages certainty. Section 20(4) of the Act provides that a protector is not liable as a trustee or fiduciary to any person unless the trust instrument provides that they are. This section has not been tested by a Cook Islands court to date.

Cook Islands law also allows a settlor, trustee or beneficiary to be appointed as a protector of an International Trust. Many settlors appoint themselves as the first protector and desire to exercise the protector powers without risk of personal liability to the other beneficiaries. Section 20(4) of the Act enables them to do this.

Of course, it is not always desirable that the protector should be free to do as they please. A settlor of a trust should consider whether they want the person who eventually replaces them as protector to have the same privileges. It may be desirable for successor protectors to be subject to fiduciary obligations so the beneficiaries can challenge their decisions in court if there are any alleged instances of misconduct. Under Cook Islands law it is possible to have the first protector whose powers are personal replaced by a protector whose powers must be exercised as a fiduciary.

The above illustrates that not only is it important to understand the nature of the protector's powers but that it is also important to ensure a suitable successor protector has been chosen. Failing to appoint a suitable successor protector can result in difficulties after the current protector dies.

It may even be worthwhile considering the appointment of a corporate protector as successor protector. The main advantage of a corporate protector is the experience they have in acting as a fiduciary. The main disadvantage in appointing a corporate protector is that they will usually take a more conservative approach to administration so there may be less flexibility.

Another option is to appoint more than one successor protector. Under Cook Islands law where more than one protector is appointed the powers conferred on them are exercisable by a majority unless the trust instrument provides otherwise. The potential disadvantage of having more than one protector is that there may be extra administration costs.

In other circumstances, it may also be worthwhile considering establishing a committee of protectors. A committee of protectors is created by the trust instrument and its rules of operation will depend on the terms of trust instrument. A committee of protectors can include any number of individuals and corporations much like a board of directors. It is not commonly used because in most situations such a high level of administrative oversight is unnecessary. However, for particularly large trust estates with high levels of activity or for trusts where an extra level of security and oversight is desired it is an option to consider.

In summary, a protector's main role is to ensure the trustee carries out its duties properly. However, a protector's role is not limited and a protector can perform a number of different roles. Cook Islands law provides a certain level of certainty in the role of protector but still allows a great deal of flexibility. It is important for the settlor of a trust to give careful consideration to the extent of the powers granted to a protector, decide whether the protector should be able to exercise those powers for their own benefit and, most importantly, ensure that the persons appointed as protector or successor protector are the right people for the job.