Is it time for the flee clause to come in from the cold?

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When establishing a trust structure, clients often ask the following questions:

- What kind of trust is best to meet my goals?
- Which jurisdiction would benefit the proposed wealth structuring best?
- Which offshore jurisdiction is less likely to face scrutiny from my "home" onshore jurisdiction?
- What happens if political or tax changes make offshore wealth structuring less advantageous than onshore wealth structuring?
- What happens if the offshore trustee gets mixed up in a fraud or has its hands bound by sanctions?
- What if the offshore custodian becomes unresponsive because of an earthquake, hurricane or mass civil insurrection?

In most cases, a competent private wealth expert is well equipped to explain the risk profile of each option as well as the relevant advantages and drawbacks. However, there remain circumstances in which a presently advantageous mode of wealth structuring can be put in place with automatic safeguards to change its home jurisdiction if certain "trigger events" (normally defined to include geopolitical unrest and / or natural disasters) occur which make that jurisdiction less advantageous.

Enter the "flee clause".

What is a flee clause?

A flee clause is a provision in a trust deed which activates once an express condition or test is met, which has an express outcome. The usual effect of a flee clause is that once a prescribed event takes place, the trust's current trustee retires in favour of a new trustee, in a different jurisdiction, with provision for an automatic change to the governing law of the trust, in order to mitigate the negative impact the clause is drafted to avoid.

Flee clauses are nothing new. In fact, *Pepper v Tuckey* from 1844 demonstrates the provision's longevity. However, despite a resurgence to onshore wealth structuring in response to potential political changes in the United Kingdom, flee clauses have fallen out of fashion in both the onshore and offshore markets.

Risks

Historic flee clauses often found in older offshore trusts were drafted using broad wording, for example: the trusts would migrate upon the declaration of a state of emergency in the trust's home jurisdiction. However, there are circumstances where a state of emergency could be triggered which doesn't endanger the proper administration of the trust.

Many trust practitioners warn against the effect of flee clauses using the cautionary tale of the Governor of Bermuda's assassination in the 1970s. The Government of Bermuda declared a state of emergency and triggered flee clauses for certain Bermudian trusts.

A more recent example of a world event which resulted in the inadvertent triggering of flee clauses is the coronavirus pandemic. To minimise the transmission of the virus among the population, most international governments declared some form of state of emergency to enact legislation restricting movement. As a result, trusts which still contained broadly worded flee clauses may have experienced an inadvertent transfer of trusteeship even though the triggering stimulus was not what was intended – an event which could endanger the fabric of the trust.

Vesting

Any well drafted flee clause will normally contain a provision that binds the outgoing trustee to vest the trust fund of the relevant trust in the "Emergency Trustee". The need for this provision is obvious, however, practical issues can arise relating to the flee clause's purpose.

For example, imagine a situation where the trustee and the trust assets are in and held in a location that has suffered from a natural disaster such as a category five hurricane. The jurisdiction has been heavily damaged, and infrastructure (such as internet and electricity) will be impacted for weeks. How can a trustee in these circumstances effectively action a transfer of the trust fund to the Emergency Trustee? It may be possible, but it could also be a protracted process.

A protracted transfer process does not fit with the flee clause's purpose - to get out of a temporarily less advantageous jurisdiction and into the safe harbour of the "emergency jurisdiction".

One possible solution is to use a nominee or a series of nominees. If trust assets are held via a nominee entity for the benefit of the trustee of the relevant trust, on a trigger event occurring, the outgoing trustee would simply direct the nominee to hold the assets for the new "emergency trustee". However, to ensure that this arrangement would be effective, the nominee needs to be an entity in a stable offshore jurisdiction that won't be directly impacted by the trigger event causing the change of trusteeship and governing law.

Conclusion

We have seen a slight renaissance in relation to the deployment of flee clauses in trust deeds over the last two years. Clients are perhaps nervous with the geopolitical uncertainty that has impacted the world following sociopolitical changes. Clients are eager to understand the options that are available to them to ensure that the assets that they settle onto trust are kept safe and out of harm's way. Although flee clauses offer a solution, it's important to note there may still be practical limitations to their use.

Do you have a particular query about flee clauses or would you like to find out more? Contact a member of Ogier's top-tier Trust Advisory Group.

Key Contacts

Jordan Constable

Senior Associate

Cayman Islands

E: jordan.constable@ogier.com

T: +1 345 815 1808

Gregory Haddow

Associate

Cayman Islands

British Virgin Islands

E: gregory.haddow@ogier.com

T: +1 345 815 1824