Family office news: Charman v. Charman - The decision and its implications one year later

20 OCTOBER 2008

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ARTICLE

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Just over a year after the landmark ruling by a British court in the case Charman v. Charman, the dust is still settling. Its implications are still being considered throughout the private client world. The case is the first in recent times to effectively assess the entire asset base of a trust as being a husband's asset.

The facts

John and Beverley Charman were married for 27 years. The husband, a self-made man, created his own insurance business in 1986. He then set up two discretionary Jersey Trusts, both of which held significant shareholdings in his businesses. They presently hold interests in Axis Capital, a business based in Bermuda, of which John Charman is CEO and founder. When he decided to remain in Bermuda permanently in 2003, he appointed a Bermudian trustee for the trusts who then changed the governing law of the trust to that of Bermuda.

At the couple's divorce trial, the judge found that John Charman held approximately £56m of assets personally, his wife held £6m and the main family trust, nicknamed Dragon, held £68m, for a total of approximately £130m. One central question for the court was how the assets in Dragon should be treated. The trial judge treated the entirety of the assets in Dragon as a resource of the husband's from which he could choose to satisfy the court's order.

The Court of Appeal decision

In May 2007, the Court of Appeal upheld the trial judge's finding that Dragon was a resource of the husband's. It further held that the trial judge had, indirectly, asked himself the key question in these types of cases, namely: "If the husband asked the trustees to advance all the capital in Dragon to him, would they oblige?" (An affirmative answer to that question means that the trust is a resource of the beneficiary's.) The Court of Appeal further held that the trial judge had answered that question in the affirmative because the husband would have needed the assistance of the trustees to meet the judgment that the trial judge had made (requiring a payment of £40m to the wife).

Implications

- The decision of the Court of Appeal suggests that the divorce courts in England and Wales will be even more likely in the future to disregard a trust structure put in place, be it for tax planning, succession or any other reason.
- The burden of proof now seems to have shifted so that instead of the recipient spouse showing why the trust assets should be included, the settler/beneficiary spouse must now prove that it was never intended that the recipient spouse should benefit.
- Trustees should consider even more carefully what the proper law of the trust should be, the location of the trustees and the location of the trust assets. A robust trust jurisdiction – for example, one of the established offshore financial centers – may provide a useful defensive shield in the context of the enforcement of awards made on divorce in England and Wales.
- Advisers should be aware of the conflict between successful tax planning and disastrous divorce planning. Settlers and beneficiaries should be warned of possible divorce claims if either spouse is included in any class of beneficiaries or added to an existing trust.

Clients in the United States face a different legal climate, but the same advice applies: consult counsel experienced in dealing with trusts in the context of divorce.

We will continue to consider and advise clients on this developing area of law.

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