Arbitration of foundation and trust disputes in Liechtenstein and the United Kingdom—a comparative analysis

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Abstract

Arbitration has become the most important means of dispute resolution in an international commercial context. Its most commonly recognized advantages are confidentiality and cost-efficiency, as well as the average pace of the proceedings. Furthermore, one of the main assets of arbitration is that the parties are able to appoint arbitrators based on their professional background, and thus secure a certain quality standard of awards in their matter.

The same advantages can be exploited in foundation- and trust-related arbitrations as well, which is why this piece tries to shed light on this rather unknown field of application of commercial arbitration.

Arbitration of foundation and trust disputes in Liechtenstein

In 2010 and 2011 Liechtenstein modernized its arbitration legislation and can today be considered a 'UNCITRAL-Model Law-Nation', meaning that it has almost completely adopted the United Nations Commission on International Trade Law's model law on international commercial arbitration. At the same time Liechtenstein joined the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards. Accordingly, an arbitral award rendered by an arbitral tribunal seated in Liechtenstein can be enforced in 156 states world-wide.

While Liechtenstein is quite a young arbitration jurisdiction, it has a long-standing tradition as international financial centre, especially in the realm of estate planning and asset protection. Ultra high-net worth individuals and High-net worth individuals from around the globe value Liechtenstein's highly sophisticated legislation in particular in terms of foundations and trusts.

The combination of the recently modernized arbitration law and the well-established foundation and trust legislation created unknown synergies, which—in the past years—have resulted in an increasing number of arbitrations in the principality.

The latter rise is predominantly reflected in the arbitration of foundation disputes. Before outlining the possibilities arbitration can offer in this context it makes sense to briefly compare the concept of a Liechtenstein foundation with a trust.

A Liechtenstein foundation is a special purpose fund which has been set-up by the founder (settlor) in order to pursue a special purpose, such as functioning as a holding structure or to serve as instrument for estate planning. In contrast to a trust a foundation is an entity which has its own legal personality and thus becomes the sole owner of the assets transferred by the founder.[1] Therefore, the Liechtenstein Supreme Court held in a line of decisions that the foundation

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1. Article 552 s 1 (1) PGR.

 doi:10.1093/tandt/tty054

is managed by the board of directors not on behalf of the beneficiaries but rather in their favour.[2]

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Since a foundation has its own legal personality it can, of course, be party to arbitration proceedings. Be it as claimant, be it as respondent.

Contrary to a foundation a trust is a relationship between a trustee who holds trust assets, contributed to the trust by a settlor, on behalf of the beneficiaries. A trust has no legal personality and can therefore never be party to an arbitration agreement or arbitration proceedings as such.

Arbitration clauses in foundation and trust deeds

Section 634(2) Liechtenstein Code of Civil Procedure (LCCP) explicitly declares arbitration clauses in articles of associations, statutes as well as foundation and trust deeds valid. Accordingly, Liechtenstein law recognizes the possibility of both foundation and trust arbitrations. Moreover, Article 931(2) Persons- and Companies Law (PGR) explicitly provides that if a foreign trust has been established in Liechtenstein, an arbitral tribunal has mandatory jurisdiction to decide about disputes between the trustee and the beneficiaries. Interestingly, even from the historical legislative materials, which are dating back to 1926, it is not clear what kind of arbitral tribunal this provision is referring to. However, Liechtenstein practitioners consider this provision to be a recommendation to submit such disputes to commercial arbitration.[3] Establishing a trust in Liechtenstein which is subject to English law and jurisprudence might thus be an interesting means to circumvent the below outlined limitations of English law in terms of the arbitration of trust disputes.

In this context section 599(1) LCCP stipulates that any claim involving an economic interest can be subject to an arbitration agreement. Since almost all foundation- and trust-related issues are of an economic nature and hence are arbitrable under Liechtenstein law. This is also reflected by the jurisprudence of Liechtenstein courts which considered information requests by beneficiaries,[4] the interpretation of foundation deeds[5] or claims by the foundation against its organs[6] to be arbitrable.

However, there is only one exception to the broadly accepted arbitrability of foundation- and trust-related disputes. Section 599(3) LCCP refuses the arbitrability of matters in the competence of the Liechtenstein courts in their function as supervisory authority in respect to foundations and trusts.[7] Such matters, *inter alia*, consists the withdrawal of members of the foundation council upon request of a beneficiary or another member of the foundation council. The Liechtenstein legislator deems these kind of disputes to be of public interest and thus unsuitable to be submitted to an arbitral tribunal. However, this perception has recently been criticized by Liechtenstein arbitration practitioners and it might well be that a change in legislation takes place in the not so far future.

In this context it is noteworthy that Article 929(1) Persons- and Companies Law (Personen- und Gesellschaftsrecht) gives the parties to a trust the right to agree on another supervisory authority as

2. Liechtenstein Supreme Court, docket no 1 CG.2006.303.
3. Johannes Gasser and Michael Nueber, 'Arbitration of Foundation and Trust Disputes in Liechtenstein' in Klausegger and others (eds), *Austrian Yearbook on International Arbitration* (2018) (C.H.Beck, Manz, Stämpfli) 36.
4. Liechtenstein Court of Appeal, LJZ 2012, 67.
5. Liechtenstein Supreme Court, docket no 04 CG.2008.14.
6. Liechtenstein Supreme Court, LES 2012, 122.
7. Liechtenstein Supreme Court, docket no 05 HG.2015.123.

the one previously outlined. In the light of this exemption it has been advocated that in relation to Liechtenstein trusts even the dismissal of trustees can be subject to an arbitration agreement.[8]

Scope of the arbitration agreement

Having established that almost all foundation- and trust-related issues are arbitrable under Liechtenstein law, it is noteworthy that another important issue in this respect touches the scope of application of arbitration clauses in foundation- and trust deeds. In order to understand the difficulties arbitration clauses in these types of documents might face, it must be recollected that an arbitration clause, in order to have binding effect, requires the unquestionable consent of all parties involved. It is without saying that beneficiaries who are (usually) neither involved in the establishment of a foundation nor in the setting-up of a trust have at no point in time consented to the jurisdiction of an arbitral tribunal to decide in their disputes.

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Fortunately, this issue has been addressed by Liechtenstein Courts in two recent landmark decisions.[9] In their decisions the courts applied the concept of 'deemed acquiescence' or 'conditional transfer', meaning that by accepting a compensation the beneficiary is presumed to have accepted the conditions under which the compensation is given to him and therefore is deemed to acquiescence the arbitration clause as well.[10]

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Drafting the optimal arbitration clause

Despite the arbitration friendly jurisprudence of Liechtenstein courts it is advisable to put some effort in the drafting of arbitration clauses incorporated in foundation and trust deeds. In this context the ICC has published a model arbitration clause for trust disputes. In order to catch all possible situations that might occur in the context of trust disputes, this arbitration clause has become very lengthy and rather complicated in its wording.

In the course of a roundtable one of the authors chaired at the most recent Vienna Arbitration Days the participants agreed on the following points to be necessarily included in arbitration clauses incorporated in a foundation or trust deed:[11]

- The types of disputes the parties wish to submit to arbitration.

8. Gasser and Nueber (n 3) 36.
9. Liechtenstein Court of Appeal, docket no 05 HG.2011.172; Liechtenstein Court of Appeal, docket no 02 CG.2012.367.
10. Michael Nueber and Sofiya Svinkovskaya, 'Venturing into New Fields of Arbitration – Trust and Foundations' in Klausegger and others (eds), *Austrian Yearbook in International Arbitration 2019* (C.H.Beck, Manz, Stämpfli), to be published January 2019.
11. The list follows the proposal by Nueber and Svinkovskaya, ibid.

- Definition of the parties to the potential dispute (e.g. bodies of the foundation, founders).
- The distribution by the trust/foundation should be made conditional upon submission to the arbitration clause.

Despite the fact that it would be the most sensible approach to involve a lawyer when drafting an arbitration clause, the following model clause might serve as guidance in this respect:[12]

> 'All disputes in connection with the foundation/the trust have to be exclusively and finally decided by an arbitral tribunal consisting of three arbitrators. The seat of the tribunal shall be at the seat of the foundation.[13]
>
> The jurisdiction of the arbitral tribunal also includes disputes between members of the foundation's/trust's bodies[14] or between members of the foundation's/trust's bodies and the foundation/the trust. In addition, the arbitral tribunal shall also be competent to decide in disputes between the foundation/trust and the founder/settlor or in disputes between the foundation/trust and the beneficiaries.
>
> Distributions by the foundation/trust are conditional upon the submission to this arbitration clause'.

Arbitration of foundation and trust disputes in England and Wales

We have seen above that Liechtenstein offers a legal regime conducive to arbitrating foundation disputes. Uniquely among civil-law jurisdictions, it also knows the concept of a (common-law) trust, and would in principle allow disputes arising out of trust instruments to be arbitrated (subject to issues such as, in particular, Article 6(1) European Convention on Human Rights (ECHR)).

The position is starkly different under English law. It is a largely academic question whether disputes arising out of a Liechtenstein, Swiss or other foundation would be arbitrable as a matter of English law.[15] Foundations are effectively unknown as an instrument of English law and so it would make little practical sense to make a foundation dispute subject to arbitration in England. In contrast, the arbitration of trust disputes in England is very much a live issue that has been being debated for at least a decade. In the course of that debate—much of which took place in the pages of this journal—the consensus has emerged that certain types of trust disputes should theoretically be arbitral as a matter of English law. Nevertheless, in practice, trust arbitration is virtually unknown in England and Wales, or is at best a rarity.[16] This is because significant uncertainties remain as to the limits of the arbitrability of trust disputes.

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12. See Michael Nueber and Matthias Gass, *Konfliktlösung in Privatstiftungen* (Verlag Österreich), Handbook to be published in fall 2018.
13. Any other location can be chosen as well. However, one must always consider the arbitration law applicable at the seat of the arbitral tribunal before making a final decision in this respect.
14. In case of a trust this would be a dispute between the trustees.
15. In principle, these authors see no reason why foundation disputes should not be arbitrable as a matter of English law, bearing in mind—*mutates mutandis*—our comments on trust disputes below.
16. Mark Herbert, 'Trust Arbitration in England and Wales: The Trust Law Committee' in SI Strong (ed), *Arbitration of Trust Disputes* (OUP 2016) 228–55 at 10.01.

In this section of our article, we:

1. Chart the course of the academic and practitioners' debate on the arbitration of trust disputes in England and Wales.
2. Explain why, in comparison to Liechtenstein and other countries, the current state of the law leaves much to be desired and makes submitting trust disputes to arbitration a risky and uncertain venture. On this basis, we make the case for a renewed push for legislation to provide a firm and certain footing for arbitrating trust disputes in England and Wales.

We proceed on the assumption that arbitration is a dispute resolution instrument that it is desirable to have available, particularly for trust disputes. This contention is not seriously in dispute.[17] Thus, the confidentiality that arbitration affords is a helpful tool, particularly in a family setting. Moreover, the ability of the parties to have a hand in selecting the tribunal will ensure that disputes are resolved by individuals familiar with the subject matter of trusts and, potentially, the specific circumstances in which the particular trust in question arose. Given the often sensitive nature of relationships within a trust, this would clearly be a welcome alternative to the cab-rank system that the Courts tend to operate in assigning judges.

The debate about trust arbitration in England and Wales to date

The issue was first raised in earnest about a decade ago by Wood, Brownbill, and McCall in an unpublished discussion paper.[18] All members of the Executive Committee of the influential Trust Law Committee (TLC), these eminent practitioners concluded that it would be 'plainly impossible under English law for a settlor or testator validly and enforceably to require beneficiaries to submit any dispute to arbitration'.[19] This was principally because the relationship between the trustees on one hand and the beneficiaries on the other hand is not, of course, one of contract. Created by the courts of equity, trusts are subject to the supervision of the English Courts,[20] and it was found to be questionable whether an arbitral tribunal could assume those functions. Furthermore, trust disputes frequently involve the interests of minors or persons under a legal disability, or of beneficiaries not yet born or ascertained. Wherever a trust instrument had, or potentially had, such classes of beneficiaries, the TLC concluded that it would be impossible to arrive at a valid agreement to arbitrate.

The discussion paper by Wood *et al* became the nucleus of a more detailed position paper which the TLC issued in 2010.[21] The committee called for legislation amending the Arbitration Act 1996 (the 1996 Act), which would enable the arbitration of trust disputes. The TLC argued that this proposed legislation could and should in principle cover all forms of trusts, public, private, and commercial (albeit that the committee did not foresee much scope for applying arbitration to charitable trusts in practice). The committee further proposed to exclude disputes about the validity of the underlying trust disposition—commonly known as the 'rocket launcher'—from the proposed legislation, akin to a similar law then recently enacted by the state of Florida.[22]

The TLC noted that trust disputes may well involve questions that fall under Article 6(1) of the European Convention on Human Rights (which, as we have seen, would be the case in Liechtenstein also). TLC concluded that as long as all parties to the arbitration

17. All authors cited in this section of our article have made this point. We are not aware of any scholar or practitioner who has argued that it would be better not to be able to submit trust disputes to arbitration.

18. Summarized in Herbert (n 16) at 10.23.

19. ibid.

20. (The courts of law and of equity having been merged in the 1870s.). cf *Schmidt v Rosewood Trustees* [2003] UKPC 26.

21. The paper has since been reprinted (with minor revisions) several times. The latest iteration (to our knowledge) is Trust Law Committee, 'Arbitration of Trust Disputes', *Trusts & Trustees* Vol 18 No4 (May 2012), 296–306.

22. Herbert (n 16), points out at 10.16–10.17 that it should be possible in principle to determine 'rocket launcher' issues by way of arbitration, so there appears to be scope for debating whether the proposed English legislation need really be as narrow as the Florida law in this regard.

are of full capacity, there would be no issue in terms of their waving the Article 6(1) rights by virtue of arbitration provision. However, legislative provisions would have to be made in order to ensure that the arbitration of the rights of minors, otherwise incapacitated beneficiaries, and unborn beneficiaries would not clash with Article 6(1).

On this basis, the TLC made detailed proposals for the contents of the proposed amendment to the 1996 Act, the centre pieces of which were:

1. A substantive provision expressly validating the arbitration of trust disputes.
2. A section providing for the arbitrator to be able to exercise the statutory and other powers currently only available to the Courts in relation to trusts.
3. An appropriate mechanism for binding minors, incapacitated beneficiaries and unborn/unascertained beneficiaries to arbitration agreements relating to trusts.
4. Appropriate amendments to sections 67–69 of the 1996 Act. In particular, it would be necessary to ensure that section 69—which provides for appeals on point of law and is non-mandatory—could not be excluded by the parties. Given the supervisory jurisdiction of the Courts over trusts, and also the Article 6(1) requirements for a public forum, it would not be possible for that provision to be excluded validly for trust disputes.

The proposal for legislation was endorsed in principle by the Law Commission, the independent body mandated by Parliament to recommend statutory reforms for England and Wales. However, that support was rather lukewarm. The Law Commission did not include the proposed legislation in its Eleventh Programme of Law Reform (its then-current programme of work). The Commission stated that it '*does not have the capacity to include this work*'.[23]

Since then, the proposal to legislate on the arbitration of trust dispute has been floating around in the English legal community. No commentator has criticized its substance. There is virtual unanimous agreement that it would be a desirable improvement on the current English arbitration law. By the same token, however, the proposed legislation has not come any closer to actually being implemented in the past eight years. The Law Commission has not made any further moves after its initial endorsement, failing to include trust arbitration in either its Twelfth Programme or the current Thirteenth Programme.[24] Nor does the proposal appear to have attracted any meaningful political support.

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In the meantime, several commentators have developed thoughts on the extent to which trust arbitration is possible under English law even in the absence of specific legislative provisions. It was not in doubt at any point that trust disputes would be arbitrable by way of an ad-hoc agreement, so long as all parties to the arbitration were at full capacity and actively consented to arbitration.[25] The TLC had specifically noted this in its position paper.[26]

23. Trust Law Committee (n 21) at 296.
24. See, respectively, <https://s3-eu-west-2.amazonaws.com/lawcom-prod-storage-11jsxou24uy7q/uploads/2015/03/lc354_twelfth_programme.pdf> and <https://www.lawcom.gov.uk/project/13th-programme-of-law-reform/> both accessed 11 March 2018.
25. As we noted above, the TLC concluded that such an agreement would amount to a waiver of the parties' rights under Article 6(1) ECHR, which are waivable.
26. Trust Law Committee, (n 21), at 297.

Going significantly further, Cohen and Poole, in a 2012 article in this journal, made the closely reasoned case that:

1. The settlor and the trustees as immediate parties to the trust instrument could undoubtedly also enter into an arbitration agreement as to future disputes.
2. Beneficiaries as claimants would be bound by an arbitration provision in the trust instrument. Their basis for this argument was that section 82(2) of The Arbitration Act, read in conjunction with sections 9 and 86(2), effectively requires anybody making a claim to which an arbitration agreement applies to commit to arbitration. This includes any person claiming under or through a party to the agreement, which is what beneficiaries would be doing when making a claim arising out of a trust instrument containing an arbitration clause.[27]

Cohen and Poole acknowledged that minor, incapacitated and unborn/unascertained beneficiaries would present a problem in this regard as they would not be bringing the claim themselves. However, they concluded that appropriate provisions could be made in the arbitration agreement to ensure that their interests were sufficiently protected.

The 2013 decision of the Texas Supreme Court in *Rachal v Reitz*[28] appeared to lend considerable support to Cohen and Poole's hypothesis that beneficiaries could be bound by an arbitration agreement in a trust instrument. Like England (and unlike Florida), Texas does not have any legislation on the arbitration of trust disputes. Like the 1996 Act, Texas law requires a valid, written agreement to arbitrate. In *Rachal v Reitz*, a beneficiary sought to enforce his rights through the courts. The Supreme Court held that while the beneficiary was not party to a contract stipulating arbitration, there was nevertheless an agreement to arbitrate that applied to him (held by the justices to be a broader concept than contracts). The claimant, Mr Reitz, had sought the benefits granted to him under the trust. He was therefore held to be stopped from circumventing the arbitration provision in the trust instrument under a doctrine the Court aptly named 'direct benefits estoppel'.

Rachal v Reitz was widely noted in the English legal community.[29] Academics and practitioners debated whether applying it by analogy could be 'a further and even decisive step towards the authorization of trust arbitration, even in the absence of specific legislative authority'.[30] However, Herbert, in a chapter in the leading (and, to our knowledge, only) book on the arbitration of trust disputes, questioned whether this is the case.[31] He pointed out that:

1. The trust in *Rachal v Reitz* had arisen through a unilateral declaration of trust, and the English courts may well wonder whether this can amount to an 'agreement' to arbitrate, however widely one is inclined to construe that term.
2. Even if the trust in question amounts to an agreement of some form, beneficiaries are not parties to it (leading back to the question posed by Cohen and Poole whether sections 82(2), 9 and 86(2) of the 1996 Act nevertheless operate in such a way as to bind a claimant beneficiary to the arbitration agreement). It could certainly not be said—as Cohen and Poole acknowledged—that minor, incapacitated, unborn and yet-to-be-ascertained beneficiaries are bound by any such agreement.

27. Lawrence Cohen and Joanna Poole, 'Trust Arbitration – Is It Desirable and Does It Work?' 18(4) *Trusts & Trustees* (May 2012) 324–31.
28. *Hal Rachal, Jr, v John W Reitz* (No 11-0708, 3 May 2013).
29. See eg Clifford Chance, *Arbitration Agreements in Trust Instruments – Are They Binding on Beneficiaries?*, June 2013. <https://onlineservices.cliffordchance.com/online/freeDownload.action?key=OBWIbFgNhLNomwBl%2B33QzdFhRQAhp8D%2BxrIGReI2crGqLnALtlyZe4jFyUhOBsv4FGIGwcvi3Hbp%0D%0A5mt12P8Wnx03DzsaBGwsIB3EVF8XihbSpJa3xHNE7tFeHpEbaeIf&attachmentsize=178578> accessed 11 March 2018.
30. Herbert (n 16) at 10.47.
31. ibid at 10.47–10.52.

3. The beneficiaries cannot, in any event, be said voluntarily to have waived their rights under Article 6(1) ECHR merely by seeking or accepting the benefits that the trust bestows upon them.

Herbert also lucidly pointed out an obvious shortcoming of the current position under English law.[32] Even if a claimant beneficiary is (in certain circumstances) bound by an arbitration clause in a trust instrument and to have waived his/her Article 6(1) rights, the same cannot be said of a respondent beneficiary.

On this basis, Herbert concluded that while it may be possible for certain type of trust disputes to be arbitrated, the limits of this possibility were too tightly confined for it to be realistically practicable. In light of this, he reiterated that it would be desirable to have legislation that provided a firmer footing.[33]

The case for a renewed push for legislative reform

Herbert's conclusion appears to be the latest word on the subject. There is, then, significant uncertainty about the extent to which arbitration clauses in trust instruments are workable as a matter of English law.[34] Thus, it remains debated to what extent beneficiary claimants are bound by such clauses. It is almost certain that (absent specific provisions in the arbitration clause) minor, unborn, or incapacitated beneficiaries would not be so bound. It seems doubtful, moreover, that such an arbitration clause would bind beneficiary respondents. Then there is the thorny issue of Article 6(1) ECHR.[35]

In short, it would be perilous for any practicing lawyer to recommend to their clients to subject a trust to an arbitration provision (as opposed to an ad hoc agreement to arbitrate among parties of full capacity). As a result, the arbitration of trust disputes remains virtually unknown in England. Given the increasing competition in the global legal market, this is clearly not a desirable state of affairs. It is to be contrasted with jurisdictions like Liechtenstein that (as we outline above) has made an active effort to encourage and facilitate the arbitration of such disputes.[36]

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In light of these facts, these authors think that the time has come to make a renewed push to provide a statutory basis for arbitrating trust disputes in England. It is unlikely that this particular type of arbitration will develop any further in England unless and until that is achieved. This sort of venture would clearly require a fair amount of tenacity. In the eight years since the TLC's position paper, effectively no progress has been made towards amending the 1996 Act. The current schedule of Parliament is very much dominated by Brexit, and so it is regrettably unlikely that any such change of the law will happen in the

32. ibid at 10.53.

33. ibid at 10.103. This appears to be the unanimous conclusion of all observers; cf Cohen and Poole, ibid at 329.

34. It is obviously a wholly separate matter whether a foreign arbitral award relating to a foundation or trust dispute is enforceable in England and Wales. We do not see any specific 'English' issues in terms of enforcement, particularly given that (i) the has not adopted a 'commercial reservation' under Article I(3) of the New York Convention and (ii) the English courts tend to construe the public policy exception to enforcement under Article V(2)(b) of the Convention narrowly indeed. For an excellent and detailed treatment of the subject, see Sarah Ganz, 'Enforcement of Foreign Arbitral Awards Arising From An Internal Trust Arbitration' in Strong (ed) (n 16) 494–528.

35. It is yet another thorny issue—and one beyond the scope of this short article—what would happen if the trust dispute gave rise to tax issues.

36. Common-law jurisdictions where similar developments have taken place include (to varying degrees) the Bahamas, Guernsey (though not, interestingly, Jersey), Florida (as pointed out above), and Singapore. Strong (ed) (n 16) offers a good overview of these developments. It seems to us that there is a growing global trend towards lawmakers facilitating foundation and trust arbitration, which England is, regrettably, lagging behind.

short term. However, these authors call on the TLC and the wider English trust law community to take a renewed interest in the project and start promoting, if there is to be any chance of achieving it eventually. A first step may be for the TLC to work towards trust arbitration being included in the Law Commissions Fourteenth Programme.

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