



LAW · COMMISSION  
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# REVIEW OF THE LAW OF TRUSTS

A TRUSTS ACT FOR  
NEW ZEALAND

LAW · COMMISSION  
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NEW ZEALAND

The Law Commission is an independent, publicly funded, central advisory body established by statute to undertake the systematic review, reform and development of the law of New Zealand. Its purpose is to help achieve law that is just, principled, and accessible, and that reflects the heritage and aspirations of the peoples of New Zealand.

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The Hon Judith Collins  
Minister Responsible for the Law Commission  
Parliament Buildings  
WELLINGTON

29 August 2013

Dear Minister

REVIEW OF THE LAW OF TRUSTS: A TRUSTS ACT FOR NEW ZEALAND  
(NZLC R130)

I am pleased to submit to you the above Report under section 16 of the Law Commission Act 1985.

Yours sincerely



*Sir Grant Hammond*  
President

# Foreword

Trusts play a central role in New Zealand society. Trusts are used in many sectors of our society and economy. They are utilised, for instance, by families to hold their wealth collectively, by those seeking to contribute to society through charities, by those in business who seek a flexible governance structure for what they are doing, by financiers involved in complex transactions, and by Māori to hold Māori land or provide governance for Treaty settlements. The law that lies behind the trust is, therefore, a key part of New Zealand's legal infrastructure. Our work on this reference has led us to the clear conclusion that the current legislation underpinning trusts is unsatisfactory and in need of reform.

For the following reasons, this Report recommends that a new Trusts Act should be introduced:

- There is confusion in the community about the role of settlors, the duties of trustees and the rights of beneficiaries that in our view threatens the institution of the trust.
- The Trustee Act 1956 is sadly in need of modernisation; in parts it is unreadable, and its provisions are inaccessible when they are most needed to aid with the administration of trusts to allow trusts to fulfil the purposes for which they were set up.
- The default provisions of the Trustee Act 1956 that are essential to trusts working efficiently and effectively no longer represent current good practice, and are a barrier rather an aid to getting trusts right.

This Report concerns the core institution of the trust and looks at how the law might generally support the institution of the trust to ensure its continued efficacy and usefulness. The Law Commission intends to continue to look at more specialised areas of trust law, such as charitable and other purpose trusts, and the use of companies and other corporates as trustees.

The Law Commission received the reference on which this Report is based in 2009, as a result of the Select Committee report and 2007 Bill, based on the 2002 Law Commission Report *Some Problems in the Law of Trusts*. Similar references have been pursued across the Commonwealth by other law reform agencies that, like us, have been charged with improving the law underpinning the trust. In conducting our review we have been mindful throughout that flexibility as well as inventiveness have always been at the heart of the English, and now New Zealand, tradition of trusts. We have seen our role as one of ensuring that trust law is as robust as it can be for 21st century New Zealand, rather than making recommendations as to uses to which trusts might be put. Part of ensuring that robustness requires the law to be clear as to what is, and what is not, a trust, and the fundamental duties trustees must owe.

Our primary recommendation is the enactment of a Trusts Act which would incorporate, modernise and make more efficacious the current provisions of the Trustee Act. The Trustee Act simply does not provide New Zealand with all that a modern trusts statute ought to. Our central aim is to make the day to day administration of trusts easier, and make resolution of difficulties less expensive and more efficient.

A new Trusts Act would not only deal with the matters currently dealt with by the Trustee Act. While we have not attempted the codification of the law of trusts, we have proposed that the new statute set out the characteristics of express trusts, both to signal the sorts of arrangements that would be subject to the new Act and also to provide guidance to New Zealanders as to what constitutes an express trust.

In short, the expanded provisions of the Trusts Act will provide New Zealanders and others, be they settlors, trustees or beneficiaries, with much clearer guidance as to what their rights, obligations and duties are. We recommend an expanded statute that would set out expressly the duties that all trustees must always owe, and those duties that trustees owe in the absence of modification in a particular trust. We have also made important recommendations relating to the provision of information to beneficiaries.

In addition to our proposals for a new Trusts Act, we make a recommendation that would make an important change to remedies available under section 44C of the Property (Relationships) Act 1976. The change would allow courts to order the transfer of trust assets that, but for being placed in trust, would have been available as relationship property. We also recommend changing the Family Proceedings Act 1980 by extending the provision in section 182 that aids the expectations of married beneficiaries of trusts settled in expectation of their marriage to beneficiaries who are in a de facto relationship. These reforms do not in our view upset basic trust principles, but remedy substantial injustices that we have been made aware of. In our view such a targeted response to these injustices makes more sense than the current procedure by which courts are asked to unpick complex trust arrangements under the headings of “sham” or “illusion”, when what is really alleged is that the arrangements have defeated legitimate expectations of one spouse.

Many will, of course, ask how our proposed reforms would affect existing trusts. We have been conscious throughout our review that the rules of the game should not be changed to the detriment of settlors, trustees or beneficiaries. In fact, the vast majority of reforms shore up current practice and clarify the application of the existing law. Where there are changes, these are designed to make life easier rather than harder. There are some areas where we have, for good and sufficient reasons, pushed beyond current law and practice. The way we have phrased these recommendations is designed to mitigate any perceived ill effect. We have carefully considered these and have recommended an appropriate lead-in period so that practice can adjust, and, if desired, settlors and trustees can make changes to specific trust deeds. Of course, trustees will need to keep under review their administration of trusts, but they are already so obliged and such a review should be easier rather than harder as a result of our recommended reforms. But our sense, and the sense from the extensive consultation that we have undertaken, is that there is much in our recommended statute that is helpful for trustees and the trusts that they administer, and there are real costs in the cumbersome and outdated procedures enshrined in the current Act.

This Report, and the new Trusts Act it recommends, give New Zealand the chance to get its trust law fit for the 21st century.



*Sir Grant Hammond*  
President

# Acknowledgements

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The Law Commission is grateful to all those who have assisted during the course of this project.

In particular, we acknowledge the generous contribution of time and expertise from our reference group:

- Kerry Ayers, Helmore Ayers
- Andrew Butler, Russell McVeagh
- Chris Kelly, Greg Kelly Law
- Greg Kelly, Greg Kelly Law
- Jessica Palmer, Senior Lecturer, University of Otago
- Bill Patterson, Patterson Hopkins
- Professor Nicola Peart, University of Otago

We are grateful for the valuable contribution of the Parliamentary Counsel Office in assisting with the preparation of indicative draft provisions.

We are appreciative of the assistance provided by the New Zealand Law Society, Auckland District Law Society and New Zealand Institute of Chartered Accountants in giving us extensive feedback and in organising consultation meetings with their members. We are thankful to Tompkins Wake in Hamilton and Cooney Lees Morgan in Tauranga for hosting consultation meetings.

The Commissioners responsible for this reference are the Honourable Sir Grant Hammond and Dr Geoff McLay. The legal and policy advisers for this Report were Marion Clifford, Jo Dinsdale and Sophie Klinger. We also acknowledge the contribution of present and past legal and policy advisers who have undertaken work on this project: Susan Hall, Janet November, Rachel Hayward, Eliza Prestidge-Oldfield and Joanna Hayward.



# Dedication

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## **GEORGE TANNER QC**

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The Commissioner initially responsible for the Review of the Law of Trusts was George Tanner QC. It had been intended that once the initial policy work was done, George would draft a Trusts Bill to accompany the Report. Unfortunately, George became ill in July 2011 before any drafting had begun, ultimately passing away the following January. While we have since been fortunate to have the assistance of the Parliamentary Counsel Office in drafting some of the key provisions of the new Act, all involved with this project wish to record their sadness that George was not able to complete the Report and Trusts Bill as he had planned. We acknowledge that George was very much in our thoughts as we completed this Report in his absence.



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# Summary

## INTRODUCTION

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- 1 The *Review of the Law of Trusts: A Trusts Act for New Zealand* completes the first stage of the Law Commission's Trusts reference. This Report concerns the core institution of the trust and recommends a modern Trusts Act to replace the outdated Trustee Act 1956.
- 2 The Report is divided into five parts. Part 1 sets out the principles that guide our recommendations and sets out the case for reform. It also explains the relationship between the reforms and the law of trusts as it currently stands. Parts 2 to 5 contain our specific recommendations and should be considered as a package. Rather than repeating material that we have previously discussed in issues papers or the *Preferred Approach Paper*,<sup>1</sup> we have sought in the individual chapters to build on that earlier analysis.
- 3 Included in the Report are indicative drafts (prepared with the assistance of the Parliamentary Counsel Office) of some of our most significant recommendations.
- 4 The Commission will follow this Report with a review of charitable trusts and other purpose trusts (the charitable and purpose trusts review) and a review of statutory trustee companies and other corporate trustees (the corporate trustee review).

## PART 1 BACKGROUND AND CONCEPTUAL ISSUES

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### Why review the law of trusts?

- 5 The trust is a central piece of the legal infrastructure of New Zealand and other jurisdictions that share our common law heritage. Trusts provide an effective way to separate the ownership of property from those who are to benefit from that ownership, and enable assets to be held collectively rather than individually. While the exact number is unknown, and probably unknowable, estimates of the number of trusts currently in New Zealand range between 300,000 to 500,000.
- 6 Use of the trust form reaches from the modest family home through to high finance. Māori make extensive use of trusts as a mechanism for the holding of Māori land,<sup>2</sup> and as a way to govern and hold assets from the Treaty settlement process.<sup>3</sup> It is clear that trusts form an important part of economic and social life. A new Trusts Act is, therefore, very important. Our aim for the new Act is to ensure the law supporting this central piece of legal infrastructure is fit for purpose in 21st century New Zealand.

### *Principles underpinning the reforms*

- 7 The Law Commission's approach in both the *Preferred Approach Paper* and in this final Report was guided by three core principles:

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1 Law Commission *Review of the Law of Trusts – Preferred Approach* (NZLC IP31, 2012).

2 At [1.14]–[1.17].

3 Office of Treaty Settlements *Post Settlement Governance Entities: A Guide* (2012) < [www.ots.govt.nz](http://www.ots.govt.nz) > .



- Upholding the trust as a robust instrument with core obligations – the understanding of what is a trust and what is not a trust must be robust. We hope to reduce misconceptions as to what might be permissible as a “trust” by embedding a common understanding as to what a trust is.
- Fit for the New Zealand context but consistent with overseas trust law – it is essential that New Zealand’s trust law be fit for purpose, but also consistent with trust law in other common law countries to which New Zealand often compares itself.
- Respecting individuals’ rights to hold and transfer property as they wish – the trust is one way in which people can legitimately choose to hold property, transfer property to others, or set up a charity, and the focus of this project is to get the core institution of the trust into as good a shape as possible.

### *The case for reform*

- 8 An important role of the Trustee Act has been to provide administrative procedures to deal with unforeseen circumstances where the existing structure and processes of a trust fail or become unsatisfactory. This includes issues like the appointment of a trustee where there are no remaining trustees, or to allow for variation to the terms of the trust to deal with unforeseen difficulties. Such administrative machinery is not only important for the particular trusts that need to use it, but is also central to the integrity of the institution of the trust, because this depends on such procedures being available if necessary. Our view, shared by many whom we consulted, is that the procedures currently in the Trustee Act are inaccessible or inapplicable in situations where accessible and applicable law is most needed.
- 9 The Trustee Act is important legislation used on a day to day basis by those dealing with trusts. For such an important statute, it has become outdated and convoluted. Not only are some provisions unnecessarily complex and difficult to understand, but some are simply unreadable.<sup>4</sup> Even more importantly, the default settings that the Act establishes, such as the default powers of trustees, no longer line up with how trusts are administered in practice. Many of these reflect practices of an earlier time.
- 10 We believe a new Trusts Act is essential. It should provide simplified procedures to enable the business of trusts at minimal expense. It is also vital that the default provisions reflect modern realities and expectations rather than legal doctrines whose relevance, importance and justification have long since passed. Our recommendations are aimed at achieving this while balancing the need to preserve the overall integrity of the settlor’s intentions and the rights of the beneficiaries to benefit from the trust, as established by the settlor.
- 11 A new Trusts Act should set out the core characteristics of the trust, and the duties of trustees, thereby strengthening the common understanding of the institution of the trust and providing guidance to individual trustees who need to understand, without reference to large tomes or compendia of cases, what their basic obligations as trustees are. In making these recommendations we are aligned with developments in a number of other areas of New Zealand law. The Companies Act 1993 included directors’ duties to make clear to directors what their obligations might be.<sup>5</sup> This articulation of duties has also been a feature of recent finance sector legislation.<sup>6</sup>

4 Peter Blanchard “Towards a modern law of trusts” (paper presented to New Zealand Law Society Trusts Conference, 2001).

5 Companies Act 1993, ss 131–138.

6 See for instance the Financial Advisors Act 2008 and the Financial Markets Conducts Bill 2011 (342-2).

## Nature of the new Trusts Act

- 12 We propose a Trusts Act that is not simply an updated, revised and reformulated Trustee Act, although such updating or reformulation is also envisaged. Rather, we propose an enlarged statute that, in addition to covering the matters currently dealt with in the Trustee Act, will cover such matters as the duties of trustees and the circumstances in which such duties may be avoided. The new Act would also set out a more comprehensive characterisation of what a trust is.

### *Flexibility of equity preserved*

- 13 However, it is not our intention to create a code that completely supplants the case law, principles of equity or the creative role of judges. Courts will continue to have flexibility to deal with situations that do not fit neatly within the terms of the new statute. We do not intend the new Act to be a code to be interpreted simply on its own terms without recourse to equitable principles and case law. Rather, the characteristics of the trust and the duties set out in the new Act should be read against that history of flexibility and principle that has given rise to them. Courts will continue to have flexibility to deal with situations that do not fit neatly within the terms of the new statute. Also the supervisory jurisdiction of the courts over trusts will not be affected by our proposals. The Trusts Act will be the primary source of trust law in New Zealand, but it will not contain everything that conceivably needs to be known about the law of trusts in New Zealand.

### *Ambit of the new Act*

- 14 We recommend that the Act include a provision that sets out the characteristics of an express trust. This means that the courts would be able to find, on rare occasions, that arrangements that fall outside the definition used for the application of the Act are still trusts. Rather than preventing the courts from recognising trusts outside this Act, our definition is intended to act as a “gatekeeper” for access to the provisions of the Trusts Act. The advantages of falling within the scope of the proposed Trusts Act will be considerable.

### *Relationship with other statutes*

- 15 It is important to ensure that the interrelationship between the new Trusts Act and other statutory schemes involving trusts continues to be clear. Our general principle is that the general trust law presented in the new Act will be the baseline of the obligations that apply wherever the express trust form is used, but that specific legislation or case law can establish a context-specific approach to particular duties, obligations or procedures. The interaction between the proposed new Act and other statutory schemes is particularly important in relation to three types of trusts.

### *Trusts under the Financial Markets Conduct legislation<sup>7</sup>*

- 16 Financial markets legislation applies an additional layer of regulation to some commercial trusts, such as debt securities, KiwiSaver and retirement schemes. Some provisions of the Financial Markets Conduct Bill mirror, overlap and in some cases extend the obligations and regulation of those acting in the position of a trustee, for the protection of investors. Specific regulation of commercial trusts by financial markets legislation takes precedence over other trust law, including the new Trusts Act. However, because the provisions do not completely

<sup>7</sup> Financial Markets Conduct Bill 2011 (342-2). Changes are currently being made to the Securities Act 1978, the Units Trusts Act 1960, the Superannuation Schemes Act 1989 and the KiwiSaver Act 2006 by the major reforms to be introduced by the Financial Markets Conduct Bill 2011 (342-2).

overlap or oust general trust law, it remains the back-stop for financial instruments structured as trusts.

#### Māori land trusts

- 17 Te Ture Whenua Maori Act 1993 provides a specific statutory regime for land owned by Māori, including land held in Māori land trusts. Māori land trusts are generally not created by settlors, but by order of the Māori Land Court. There are a number of provisions under Te Ture Whenua Maori Act that differ from the proposed new Act and general trust law. It is our intention that the Māori Land Court and Appellate Court would continue to exercise its current jurisdiction in relation to trusts, and would continue to apply general trust law in a way that reflects this particular context. We are making a recommendation to ensure this continues.

#### Treaty settlement trusts

- 18 Trusts are the most commonly used mechanism for holding and managing property following a Treaty settlement. These trusts are established by deed, but are enabled by legislation. In many respects, these trusts reflect traditional trust law principles and much of the new Act will be applicable to them in the same way it is to other large trusts. However, aspects of general trust law do not apply, such as the limit to the duration of a trust. Also, because these trusts have large numbers of beneficiaries, these trust deeds will make alternative provision to some of the recommended default provisions in the new Trusts Act. The courts, and those involved in the administration of the trusts, will continue to be able to apply the general law of trusts to Treaty settlement trusts in a manner that acknowledges and incorporates cultural values and the particular purpose of these types of trusts.

#### *Application to existing trusts*

- 19 Generally our approach is that the new Act should apply to existing trusts as well as new trusts, as many of the recommendations restate the existing case law rather than altering it. There are a few provisions for which we have proposed a transition period in order that there be sufficient opportunity for those involved to be able to adapt to the changed obligations.

## **PART 2 CORE TRUST CONCEPTS IN THE NEW ACT**

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### **Characteristics and creation of a trust**

- 20 Chapter 4 presents our recommendation that new legislation include provisions setting out the characteristics and requirements for the creation of an express trust. These provisions would set out the key features of a trust as drawn from traditional trust law and represent the current legal position. They would act as a statutory definition for the purposes of the new Trusts Act. The intention is that these provisions would summarise in one place what makes a trust a trust, but would not override the existing case law. Rather than being words intended to stand completely on their own, the characteristics and requirements for the creation of a trust should be read against the history of equitable flexibility and principle that has given rise to trusts. This recommendation is central to fulfilling one of the core aims of this review: to make the law of trusts clearer and more accessible to those who are involved with trusts. We have included indicative draft provisions (clauses 1 to 6, see Appendix A) to illustrate how this recommendation could be translated into legislation.
- 21 One of the important effects of having a statutory statement of what a trust is would be that it would be clear to the courts that, if an arrangement does not accord with the statutory characteristics and requirements for the creation of a trust, the court should find that there is no trust. Our view is that this is likely to be the best approach for handling cases where there

is a question regarding the validity of a trust, rather than using potentially problematic causes of action such as “sham trust”, “alter ego”, “bundle of rights” or “illusory trust”. We have not recommended statutory intervention in relation to these causes of action.

## Trustees’ duties

### *Mandatory and default duties*

- 22 We recommend, in chapter 5, that the new Trusts Act should state the duties of trustees. As with the statement of the characteristics and requirements for the creation of a trust, the statute should set out the duties in a way that summarises and restates well-accepted principles of trust law and would not preclude recourse to rules of equity to add detail and shades of meaning. The function of the duties provisions would be to educate by making the law clear and accessible, and to enable clear and comprehensive deed drafting that addresses matters essential to the trust relationship and the role of a trustee.
- 23 We recommend expressly providing for six mandatory duties that are essential to the existence of a trust. These duties must be present in every trust. If a trust deed attempts to exclude the mandatory duties, they will either override the exclusion or provide evidence towards a finding that there was no intention to create a trust. We also recommend including 11 default duties, which are present in a trust unless the terms of the trust indicate otherwise by excluding or modifying them.

### *Trustee exemption and indemnity clauses*

- 24 Chapter 5 also addresses clauses in trust deeds that attempt to avoid or modify the consequences of a breach of trust. If the new statute is to assist people in clearly understanding the extent of trustees’ duties, it needs to address potential limitations to liability through trustee exemption or indemnity clauses. These clauses potentially undermine the importance and real effect of the duties if they are not restricted. We recommend that the terms of a trust must not limit a trustee’s liability or grant a trustee an indemnity against the trust property in respect of a breach of trust arising from the trustee’s own dishonesty, wilful misconduct or gross negligence. This limitation is an advance upon the current law by making it clear that such clauses cannot exclude liability for gross negligence. The line we propose between valid and invalid exemption and indemnity clauses balances the need to protect trustees with the need to uphold the reality of the trust. We also address the concern that many settlors are not aware of the meaning and effect of exemption and indemnity clauses by requiring trust advisers of new trusts to take reasonable steps to ensure that the settlor is aware.

### *Obligations relating to information*

- 25 The trustees’ duties are integrally related to how a trustee handles information about the trust. We include recommendations in chapter 5 that state the types of information that a trustee must retain and that provide a process for how a trustee should manage the disclosure of information to beneficiaries. These recommendations will aid the clarity of trust law in this area and will enable trustees to better carry out their role. The disclosure of information to beneficiaries, in particular, is an area that is difficult for trustees and is of some concern in many trusts. The recommendation is not intended to significantly alter the law, but rather to present the current law in a way that is more applicable to trustees with some clarification about the presumptions that apply and the factors that can be considered in deciding to withhold information.
- 26 Clauses 7 to 43 of the indicative draft provisions give effect to the trustees’ duties recommendations (see Appendix A).

## PART 3 TRUSTEES

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### Trustees' powers

- 27 Rather than having the current statutory default provisions that restrict and confine the powers of trustees in ways that are now considered undesirable and are seldom followed in trust deeds, we propose in chapter 6 powers provisions that broadly empower trustees. Within the scheme of the new Act, the statements of the duties on trustees and the standard of care for the exercise of powers will guard against the inappropriate use of powers by trustees. The new Act will better reflect modern deed drafting and so will be much more useful.
- 28 This chapter also includes a reform to the age of majority in trusts, changing it from 20 years to 18 years, so that it better accords with the general law. We recommend modernisation of the statutory powers to appoint agents and delegates, and new powers to appoint custodians and nominees.
- 29 Chapter 6 also discusses our recommendation to introduce a statutory default standard of care for trustees when exercising a power of management or administration. This reflects the current law but provides greater clarity. Indicative draft provisions of the standard of care are included (see Appendix A, clauses 22 and 25).

### Investment

- 30 In chapter 7 we recommend some minor changes to the current provisions in Part 2 of the Trustee Act. These changes are intended to address existing uncertainty over the coverage of some provisions, deal with specific, relatively self-contained issues, or repeal provisions that are now historical and unnecessary. The duty to invest prudently and the standard of care pertaining to investment remain fundamentally unchanged. Clauses 23 and 26 in the indicative draft provisions illustrate how these obligations fit within the broader framework of duties and powers (see Appendix A).
- 31 Chapter 7 also includes three more significant reforms relating to investment. The objective of these reforms is for the legislation to better support modern portfolio investment.

#### *Distinction between capital and income*

- 32 To better facilitate total return investment and allow trustees to invest funds without regard to whether the return is technically “income” or “capital”, we recommend that trustees should have discretion to determine whether any return is to be treated as income or capital for the purposes of distribution. The key point here is that investment decision-making should be separated from distributional issues to allow trustees to adopt a total return investment policy. The default provisions in the new Act should not require trustees to select investments with regard to their legal category rather than overall return. Within the parameters of their duty of prudence, trustees should be able to maximise the total gain to the trust portfolio.

#### *Apportionment of receipts and outgoings*

- 33 The current rules on the apportionment of receipts and expenses on the basis of whether they are classified as income or capital should also be replaced. Determining the correct apportionment in some situations under current rules is difficult and can require complex calculations of very small sums of money. Again the reform proposed here gives trustees discretion to apportion receipts and outgoings. When exercising that discretion trustees are bound by their underlying duties to ensure they maintain a fair balance between the interests of all beneficiaries.

### *Use of investment managers*

- 34 A new provision should be introduced to enable trustees to appoint investment managers and give them authority to make investment decisions.

### **Appointment and removal of trustees**

- 35 In chapter 8 we address the provisions relating to the appointment and removal of trustees, an area where great practical improvement can be made. The areas covered are:
- acceptance or rejection of trusteeship;
  - who may be appointed as a trustee;
  - the discharge and replacement of a trustee, including grounds for removal, who may remove a trustee and appoint a replacement trustee, appointment of a replacement trustee when a trustee dies while in office, and the retirement of trustees;
  - whether persons removing and appointing trustees should be subject to duties;
  - whether trustees who are removed should always be replaced and whether the new Act should provide for a minimum number of trustees; and
  - the transfer of trust property when a trustee is removed.
- 36 The provisions in the Trustee Act regarding these areas are of limited usefulness. They commonly require that an application is made to court to effect a change of trustees, even where the change is straightforward and uncontested. Our recommendations modernise the statutory provisions and make them clearer and more comprehensive. They also provide options that avoid the need to apply to court by empowering other persons to effect a change of trustees. Where there is a risk that such a process could be abused, we recommend safeguards involving the notification of beneficiaries and the oversight of the Public Trust.

### **Custodian and advisory trustees**

- 37 Custodian and advisory trustees are included in the Trustee Act, but the provisions relating to them contain ambiguity. In chapter 9, we recommend that these provisions be updated to be modern and comprehensive. In order to avoid confusion, we recommend that advisory trustees are renamed “special trust advisers” because they are not actually trustees at law.

## **PART 4 COURT POWERS AND JURISDICTION**

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### **Revocation and variation of trusts**

- 38 The law has long recognised that there are circumstances where, notwithstanding the general rule, trusts should be able to be varied, brought to an end or even resettled on to new trusts.
- 39 The reforms proposed in chapter 10 aim to bring greater clarity and certainty to the existing law in this area, and give the courts some further flexibility when it is called upon to approve a variation. In particular, we recommend that the new Trusts Act include:
- statutory provisions restating (and clarifying the breadth of) the rule in *Saunders v Vautier* regarding revocation and variation by beneficiaries;
  - a power of the court, following consideration of specified factors, to waive the requirement for consent of any person and approve a revocation, variation or resettlement or change to the scope or nature of trustees’ powers; and

- a power of the court to make amendments to the non-distributive administrative provisions of any trust deed where necessary to enable the trustees to efficiently manage trust property.

40 Clauses 52 to 57 of the draft provisions would give effect to our recommendations here (see Appendix A).

### Reviewing the actions of trustees

41 In chapter 11, we recommend retaining the statutory review procedure under section 68 of the Trustee Act for reviewing the exercise of trustees' powers in the new Trusts Act. We recommend extending the courts' power of review of actions and decisions made under the trust instrument, as well as those made under the Act.

42 The proposed reform broadens the ability to have trustees' decisions reviewed, although this is subject to a threshold of evidence that is needed before an application is considered by the courts. To strike a balance between the interests of trustees and beneficiaries, we recommend a two stage process under which the applicant beneficiary is first required to put some evidence before the court that raises a genuine and substantial dispute as to whether the trustees have acted properly in the exercise of their powers (first stage). If the court is satisfied that the applicant has raised a genuine and substantial dispute, the trustee should be required to appear before the court and put forward evidence that their action or decision was a proper one in the circumstances (second stage). By the term substantial we mean that the matter genuinely in dispute is not trivial.

43 Clauses 50 to 51 of the draft provisions illustrate our recommendations for an expanded two stage review process (see Appendix A).

### Other powers of the court

44 A wide variety of unrelated powers are conferred on the court by different sections of the Trustee Act. Chapter 12 deals with the issues raised by:

- section 66 – applying to court for directions;
- section 72 – authorising payment of commission;
- section 74 – a power to make a beneficiary indemnify for breach of trust;
- section 75 – barring claims and future claims;
- sections 77 to 79 – payment of trust money to the Crown;
- section 76 – distribution of shares of missing beneficiaries; and
- section 35 – protection against creditors by means of advertising.

45 In broad terms, we recommend that each of these provisions be modernised and retained. Where we have recommended reform, it is generally to improve clarity and to modernise. There are no significant policy changes in these areas.

### Jurisdiction of the courts

46 Chapter 13 of the Report considers the respective jurisdictions of the High Court and District Court to determine proceedings under the proposed new Trusts Act, and the jurisdiction of the Family Court to make orders and give directions under the new Act.

47 We consider that it makes little sense for the District Court to have, as it does under section 34 of the District Courts Act 1947, the same general equitable jurisdiction as the High Court but not to have jurisdiction to exercise powers under a new Trusts Act. Consequently, we consider

that the District Court should have all the tools that are necessary to effectively exercise its equitable jurisdiction in respect of trusts and thus should have concurrent jurisdiction with the High Court for matters under a new Trusts Act. This is consistent with the District Court now being a court of general civil jurisdiction.

- 48 We recommend that the District Court should have concurrent jurisdiction with the High Court to determine any proceeding under the new Trusts Act where the amount claimed or the value of the property at issue is within its jurisdiction level. Although currently \$200,000, that level will soon rise to \$350,000 as a result of the Government's proposed new courts legislation. The District Court should also have concurrent jurisdiction to determine proceedings where there are no claims for money or property.
- 49 We also propose that the Family Court should have jurisdiction to exercise powers and make orders under new trusts legislation to provide a remedy where a matter is already within its jurisdiction.

### Resolving disputes outside of the courts

- 50 Chapter 14 recommends that the new Trusts Act include provisions relating to the use of alternative dispute resolution (ADR) in trust disputes. Primarily these provisions would clarify that ADR can be used and would facilitate the use of ADR by alleviating potential procedural difficulties. This recommendation accords with the aim to modernise trusts legislation and make it fit for use.

### The Public Trust

- 51 In several places in the Report we recommend giving the Public Trust new roles. Chapter 15 discusses our general approach to the Public Trust. It recommends that the new Trusts Act makes it clear that the Public Trust should not act in situations where there is an element of dispute or contention, or where there is significant complexity. It also recommends that the Public Trust be accountable to the Government for the exercise of its roles under the new Act and that the Public Trust should be able to charge a reasonable fee for carrying out its roles. The roles recommended for the Public Trust are those where it would be in the position of standing in the shoes of a trustee and those which involve a formal certification and validation process, both of which are akin to its current roles under other statutes. The recommendations in this Report would see the Public Trust:
- having the power to make decisions on behalf of a trustee where the trustee is temporarily unavailable and cannot be contacted for any reason and no delegation is in place;
  - overseeing the removal and/or replacement of a trustee in the following situations where there is no one with the power to do so:
    - a sole trustee on the ground of incapacity or similar;
    - a sole trustee who dies while in office;
    - a sole trustee who wishes to retire; and
  - providing a vesting certificate to confirm that assets are vested in a named new trustee where a former trustee has not and cannot now transfer the trust assets.
- 52 In addition, under the modernised form of section 83B of the Trustee Act, which we recommend, the Public Trust would continue to have the role of agreeing to the appointment of an auditor after an application for an audit of trust accounts by a trustee or beneficiary.



53 We consider it necessary for there to be a neutral fiduciary power holder to fill the proposed roles, if the new Act is to accomplish the aims of providing greater efficiency, reduced costs and more robust processes for those involved with trusts. Expanding the roles of the Public Trust will reduce the dependence on the courts for administrative processes without having to establish a new standalone body, the costs of which are likely to be prohibitive. The Public Trust presents an attractive option because it is subject to a public accountability process, and has expertise in managing and overseeing trust matters.

## **PART 5 GENERAL TRUST ISSUES**

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### **Areas relating to corporate trustees to be considered in later review**

54 Various proposals made in the *Preferred Approach Paper* have been deferred in order to consider them in the Commission's later corporate trustee review. These include proposals relating to:

- the liability of directors of companies acting as trustees to creditors and beneficiaries;
- disclosure that a company is acting as a trustee; and
- a liquidator of a trust and other areas concerning the insolvency of corporate trustees.

55 We believe that more consideration is needed of the wider implications of proposals in these areas and the interaction of companies acting as trustees with company and insolvency law. Nonetheless, the Commission remains of the view that reform is needed to strengthen the position of creditors and prevent unfairness to those dealing with trusts who have given value to the trust. Therefore, while we are deferring consideration of some proposals made previously in the *Preferred Approach Paper*, we recommend in chapter 16 other changes that do fit more appropriately within the rest of this review.

### **Trustee's indemnity, receivers, and standing of the Official Assignee**

#### *Trustee's indemnity*

56 Chapter 16 sets out recommendations relating to the trustee's indemnity, and others relating to insolvency. Recommendations in this chapter are intended to clarify and modernise the law, and make certain features of trust law more accessible. Well-understood principles relating to the trustee's indemnity are to be set out in legislation, including the personal liability of the trustee, the trustee's entitlement to be reimbursed or pay directly out of the trust property, and that the indemnity cannot be limited or excluded by the terms of the trust.

57 We also recommend a provision for the trust deed to rank the order in which the trust property may be used to meet the trustee's expenses through the indemnity. We anticipate this mechanism will provide some level of protection for specific property if for some reason it is inappropriate that the trustee or creditors could potentially acquire an interest in the trust assets through recourse to the indemnity. For example, this may be the case if the property is significant for cultural or commercial reasons.

58 We recommend giving a creditor a limited claim to satisfy a liability through the trustee's indemnity, even where the indemnity is impaired and the trustee would not be entitled to rely on it. This would only be available if the creditor has acted in good faith and given value, and the trust property retains the benefit. This prevents beneficiaries from receiving a windfall, based on an unjust enrichment approach.

59 Clauses 45 to 49 of the indicative draft provisions illustrate our recommendations in this area (see Appendix A).

### *Standing of the Official Assignee*

60 A further recommendation provides for the Official Assignee to have standing to challenge the validity of a trust, which will require an amendment to the Insolvency Act 2006. This provision would clarify and provide more certainty about the position of the Official Assignee in proceedings that involve challenging a trust.

### *Receivers*

61 The High Court's ability to appoint a receiver will be confirmed in legislation. The court currently has this ability under its inherent jurisdiction but this is rarely exercised. We consider it will be useful to set out this jurisdiction in the Trusts Act to make this feature more accessible and modern. The statutory provision would specify some key elements of the process including:

- the grounds on which a receiver may be appointed;
- who may act as a receiver;
- the powers and duties of a receiver;
- priorities of those involved;
- a process for terminating the receivership; and
- provision for the receiver's fees to be paid out of the trust property.

### **The rule against perpetuities and the maximum duration of a trust**

62 Chapter 17 addresses the rules against perpetuities and accumulations, which have the effect of setting a maximum duration for a trust. We recommend reform to simplify and modernise the law in this area. The current law is complex and causes considerable problems in practice. It causes uncertainty and there is a risk it may invalidate legitimate dispositions. It is not well understood, and so trust deeds may inadvertently fall foul of its requirements.

63 We consider that extending the maximum duration of trusts is more appropriate than permitting trusts to continue indefinitely. In our view, there are strong policy reasons to retain some form of limit on the duration of private trusts.

64 Our recommendation is to replace the current judge-made rules and the Perpetuities Act 1964 with a clear, simple maximum duration rule for trusts of 150 years. The rule against accumulations and the Property Law Act 2007 would also be updated to reflect the abolition of the rule against perpetuities and remoteness of vesting. The new law would be much easier to understand and would improve certainty in trust dealings. There are advantages to a bright line rule that provides certainty at the outset of the creation of the trust. The 150 year period will allow a high degree of flexibility for settlors to dispose of property as they choose.

65 Trusts that are subject to existing statutory exemptions to the perpetuities rules will need consequently to be exempted from the rule limiting the duration of trusts, including those exempted in the Perpetuities Act, and trusts exempted in their own legislation.

66 Existing trusts will continue to operate according to their own terms. They will not automatically gain the benefit of the 150 year period, and must abide by the period set out in their trust deed unless that period can be validly changed. Our view is that it is not appropriate to be able to easily alter the period for existing trusts because this will also alter beneficial interests. Extending the period automatically would risk upsetting the balance chosen by the settlor between different classes of beneficiaries. Once settled, trusts should be binding unless flexibility is provided for in the terms of the trust.

## Relationship property and trusts

67 Chapter 19 addresses an issue that arises at the interface between trusts and relationship property. Although our overall approach to this review of the law of trusts has been to address matters of core trust law rather than problems that arise at the point where trust law interacts with other policy areas, we have included two reforms to address problems at the interface between relationship property and trusts, because of the potential for injustice under the current law.

### *Section 44C of the Property (Relationships) Act 1976*

68 After carefully considering the competing arguments, we determined that section 44C does not currently strike the right balance between the interests of a partner whose rights have been defeated by a transfer of relationship property to a trust and those beneficially interested in the trust. The constraints on the compensation powers mean that it is too easy for one partner to circumvent the framework of the Property (Relationships) Act 1976 and place relationship property beyond the reach of the court.

69 We have recommended that section 44C(2)(c) be amended. We think the courts should have the power to make an order requiring the trustees to pay a specified sum or transfer property of the trust to compensate the partner whose rights were defeated by the disposition of relationship property to the trust. That power to order compensation would only be available where it was not possible to otherwise compensate the defeated partner and would be restricted to the current value of the relationship property that was transferred to the trust. This recommended change would essentially give effect to the original proposal that was put forward by the Ministerial Working Group on Matrimonial Property and Family Protection in 1988 to address dispositions to trusts.

### *Section 182 of the Family Proceedings Act 1980*

70 Under section 182 of the Family Proceedings Act 1980 the court may vary the terms of ante- and post-nuptial settlements, including trusts, when the marriage or civil union of the parties comes to an end. Section 182 jurisdiction is separate from the Property (Relationships) Act rules and the concept of equal sharing in the Property (Relationships) Act is not directly relevant to a determination under section 182.

71 Whether or not section 182 was overlooked at the time the Property (Relationships) Act was enacted, it provides an additional and alternative option in some circumstances where property has been settled on a trust as an ante- or post-nuptial settlement. It, however, applies only to married and civil union couples. It does not apply to de facto relationships so rather unfairly only provides a remedy for some couples and not for others. We consider that this inconsistency in the treatment of de facto couples is now an anomaly that must be addressed. We, therefore, recommend amending section 182 so it applies to de facto partners as well as married and civil union partners.

# Summary of recommendations

## CHAPTER 4 – CHARACTERISTICS AND CREATION OF A TRUST

R1 The new Trusts Act should:

- (1) Provide that the new Act applies only to express trusts, but that the court may apply sections of the Act where appropriate to resulting trusts and constructive trusts.
- (2) Provide that the characteristics of an express trust are:
  - (a) it is a legal relationship in which the trustee holds or deals with trust property on behalf of another person or persons (the beneficiaries) or for a purpose permitted at law;
  - (b) the trustee is bound by a fiduciary duty to deal with the trust property for the benefit of the beneficiaries or for the purposes of the trust;
  - (c) any beneficiary, or the Attorney-General in the case of a charitable trust, may enforce the trustee's duties against the trustee;
  - (d) the beneficiaries have equitable rights in or in respect of the trust property; and
  - (e) a trust must not have the sole trustee as the sole beneficiary of the trust.
- (3) Provide that an express trust may be created:
  - (a) by the settlor by words or actions doing the following (collectively known as "the three certainties"):
    - identifying the beneficiaries, or permitted purpose; and
    - identifying the trust property; or
    - indicating an intention to create a trust;
  - (b) if a statute provides for the creation of an express trust, in accordance with that statute.
- (4) Define the terms trustee, beneficiary, discretionary beneficiary, settlor and trust property for the purposes of the Act.
- (5) Provide that a trust must satisfy all of the three certainties ((3)(a)) or be created under a statute ((3)(b)) if it is to be an express trust.
- (6) Provide that nothing in the new Act affects any provision of Te Ture Whenua Maori Act 1993 or the jurisdiction of the Māori Land Court over trusts created under that Act.

**Mandatory and default duties**

R2 The new Trusts Act should provide that:

- (1) The following are the mandatory duties of a trustee (which will be implied into every trust and cannot be excluded from the trust relationship):
  - (a) to be familiar with the terms of the trust;
  - (b) to act in accordance with the terms of the trust;
  - (c) to act honestly and in good faith;
  - (d) to act for the benefit of the beneficiaries or to further the purpose of the trust, in accordance with the terms of the trust;
  - (e) to exercise stewardship over the trust property for the beneficiaries or the purpose of the trust; and
  - (f) to exercise powers for a proper purpose.
- (2) In the exercise of any duty, there is no requirement that beneficiaries are treated equally, as long as they are treated in accordance with the terms of the trust.

R3 The new Trusts Act should provide that:

- (1) The following are the default duties of a trustee (which apply if and to the extent that they are not excluded or modified, explicitly or implicitly, by the terms of the trust or by statute):
  - (a) not to exercise any power directly or indirectly for the trustee’s own benefit;
  - (b) to actively and regularly consider the exercise of the trustee’s powers;
  - (c) not to fetter the future exercise of the trustee’s powers;
  - (d) to avoid a position of conflict of interest;
  - (e) to maintain accounts of the trust property that adequately identify the assets, liabilities, income and expenses of the trust and are appropriate to the value and complexity of the trust property;
  - (f) not to be unfairly partial to some beneficiaries to the detriment of others;
  - (g) not to make a profit (that has not been permitted by the beneficiaries);
  - (h) to act without reward except where it has been permitted by the beneficiaries or is in accordance with the trustee’s right to be reimbursed for legitimate expenses and disbursements;
  - (i) where there is more than one trustee of a trust, to act unanimously;
  - (j) to manage the trust with reasonable care and skill; and
  - (k) to invest prudently.

- (2) These duties may be excluded or modified, explicitly or implicitly, by the terms of the trust but not to the extent that such alterations are inconsistent with the mandatory duties.

### Trustee exemption and indemnity clauses

- R4 (1) The new Trusts Act should provide that:
- (a) the terms of a trust must not limit or exclude a trustee's liability for a breach of trust or grant the trustee an indemnity against the trust property in respect of liability for a breach of trust arising from the trustee's own dishonesty, wilful misconduct or gross negligence;
  - (b) a clause that purports to have the effect stated in (a) is invalid (and is effectively severed from the terms of the trust), provided it is found that the settlor's overall intention was in fact to create a trust as opposed to some other type of relationship;
  - (c) any paid trust adviser or trust drafter who causes a settlor to include a clause in the terms of the trust that has the effect of limiting or excluding liability for negligence, or of granting an indemnity against the trust property in respect of liability for negligence, must before the creation of the trust take such steps as are reasonable to ensure that the settlor is aware of the meaning and effect of the clause; and
  - (d) if a person who is paid to advise on the terms of a trust or the drafting of a trust deed fails to meet the obligation in (c) and is a trustee of the trust, the exemption or indemnity clause will have no effect in respect of that trustee.
- (2) Professional regulatory bodies relevant to trusts should provide guidance for their members as to what steps would be reasonable to ensure that a settlor is made aware of the meaning and effect of any trustee exemption clauses.
- (3) The new Act should re-enact an equivalent of section 73 of the Trustee Act 1956, which gives the court the power to relieve a trustee wholly or in part from personal liability for a breach of trust if the trustee acted honestly and reasonably, and ought fairly to be excused.

### Retention of information by trustees

- R5 The new Trusts Act should provide that:
- (1) In exercising the mandatory duties of a trustee, a current trustee is required, so far as is reasonable, to retain the following:
    - (a) the trust deed;
    - (b) any variations made to the trust deed or terms of the trust, including variations made to the beneficiaries of the trust;
    - (c) a list of all of the assets currently held as trust property and liabilities of the trust;
    - (d) any records of trustee resolutions made during that trustee's trusteeship;

- (e) any written contracts entered into during that trustee's trusteeship;
  - (f) any accounting records and financial statements prepared during that trustee's trusteeship;
  - (g) deeds of appointment and retirement of trustees;
  - (h) any expression of the intention or wishes of the settlor; and
  - (i) any of the above documents retained by a former trustee during that trustee's trusteeship and passed on to the current trustee.
- (2) Where there is more than one trustee, it is not necessary for every trustee to hold a copy of the documents, except for the documents in R5(1)(a) and (b). One trustee may hold the documents on behalf of the other trustees as long as the documents are available to the other trustees on request.
- (3) A trustee is required, so far as is reasonable, to retain the documents for the duration of his or her trusteeship of the trust and, if the trust continues, to pass on the documents to at least one replacement or continuing trustee when he or she retires or is removed.

### Provision of information to beneficiaries

R6 The new Trusts Act should provide that:

- (1) Trustees have a mandatory obligation to provide sufficient information to sufficient beneficiaries to enable the trust to be enforced;
- (2) There is a presumption that trustees must:
  - (a) notify qualifying beneficiaries (those who the settlor intended to have a realistic possibility of receiving trust property under the terms of the trust) as soon as is practicable of the fact that a person is a beneficiary, names and contact details of trustees and the right of beneficiaries to request a copy of the trust deed or trust information; and
  - (b) provide trust information to a beneficiary who requests it within a reasonable time.
- (3) The presumptions in (2) do not apply if a trustee reasonably considers that the information should not be provided after taking into account the following factors:
  - (a) the nature of the interests held by the beneficiaries, including the degree and extent of a beneficiary's interests or a beneficiary's likely prospects of receiving trust property in the future;
  - (b) whether there are issues of personal or commercial confidentiality;
  - (c) the expectations and intentions of the settlor at the time of the creation of the trust as to whether beneficiaries would be notified;
  - (d) the age and other circumstances of the beneficiaries;
  - (e) the impact on the trustees, other beneficiaries, and third parties;
  - (f) whether, in the case of a family trust, notification or non-notification may embitter family feelings and the relationship between the trustees and beneficiaries to the detriment of the beneficiaries as a whole;

- (g) the practicality of providing information to all beneficiaries or members of a class of beneficiaries in a trust where there are large numbers of beneficiaries or unascertainable beneficiaries;
  - (h) whether some or all of the documents can be disclosed in full or in redacted form; and
  - (i) whether safeguards can be imposed on the use of the documents (for example, undertakings or professional inspection).
- (4) "Trust information" is defined to include any information regarding the terms of the trust, the administration of the trust, or the trust property that it is reasonably necessary for the beneficiary to have in order for the trust to be enforced, but does not include reasons for trustees' decisions.
  - (5) A beneficiary may be charged for the reasonable costs of being provided with the trust information.
  - (6) Trustees are entitled to apply to the court for an order as to whether they are required to notify a beneficiary or class of beneficiaries under (2)(a), or for an order as to whether they are required to provide a beneficiary with trust information under (2)(b). A beneficiary is entitled to apply to court for an order that the trustees supply trust information. The court is able to review the exercise of the trustees' discretion and merits of the trustees' decision.

## CHAPTER 6 – TRUSTEES' POWERS

### Administrative powers

- R7 The new Trusts Act should:
- (1) Provide that a trustee has the same powers in relation to trust property that the trustee would have if the property were vested in the trustee absolutely and for the trustee's own use, that is, the trustee has the powers of a natural person.
  - (2) Provide that in exercising any powers enabled under (1), the trustee is subject to the trustees' duties, the standard of care and the purpose of the trust.
  - (3) Include a schedule setting out some commonly used powers of a trustee which are included in the powers enabled under (1) and stating that "for the avoidance of doubt, the powers of a trustee granted under [the general powers provision in (1)] include, but are not limited to, the following: ...". The schedule should include the power to:
    - sell or lease trust property;
    - borrow money and create a security interest in the trust property;
    - give a guarantee;
    - seek legal, financial or other advice.
  - (4) Provide that this is a default provision capable of being overridden by the terms of the trust.



## Powers of maintenance and advancement

- R8 The new Trusts Act should:
- (1) Re-enact section 40 of the Trustee Act 1956 in modernised form with the following reforms:
    - (a) defining the phrase “maintenance, education, advancement or benefit” in the legislation in a way that ensures they are interpreted broadly and include the concepts of “comfort” and “wellbeing”;
    - (b) removing the current test for the exercise of power in section 40(1)(a): “as may, in all the circumstances, be reasonable”; and
    - (c) removing the requirement in section 40(1)(a)(i) to take into account other trust funds to which a beneficiary may have access.
  - (2) Re-enact section 41 of the Trustee Act 1956 in modernised form with the following reforms:
    - (a) defining the phrase “maintenance, education, advancement or benefit” as in (1)(a) above;
    - (b) removing the limits on the amount of the advancement; and
    - (c) clarifying that those who hold contingent interests under a double or multiple contingency are not eligible.
  - (3) Provide that this is a default provision capable of being overridden by the terms of the trust.

## Age of majority

- R9 The new Trusts Act should:
- (1) Set the age of majority for the purposes of the Trusts Act and trust law generally (including wills) at 18 years.
  - (2) Clarify that the Age of Majority Act 1970 does not apply.

## Appointment of agents, custodians and nominees

- R10 The new Trusts Act should adopt the approach taken in section 5 of the Select Committee version of the Trustee Amendment Bill 2007, which proposed new sections 29–29E to replace section 29 of the Trustee Act 1956, with amendments. The redrafted provision in the new Act should:
- (1) Allow a trustee to employ an agent to exercise or perform a trustee’s “administrative functions”. “Administrative functions” should be defined as any power, right or function other than a “trustee function”, that is necessary or desirable to exercise or perform in executing the trust, administering any asset of, or property that is subject to, the trust, or both. The provision would define a “trustee function” as any of the following powers, rights or functions vested in the trustee:

- (a) a function related to a decision regarding the distribution, use, possession, or other beneficial enjoyment of trust property;
  - (b) a power to decide whether any fees should be paid or other payment should be made out of income or capital;
  - (c) a power to decide whether payments received should be appropriated to income or capital;
  - (d) a power to appoint a person to be, or to remove, a trustee of the trust;
  - (e) a power of appointment (including a power to appoint a person to be, or to remove, a beneficiary);
  - (f) a power to appoint or change the distribution date of trust funds;
  - (g) a power to resettlement the trust, or to amend, revoke, or revoke and replace terms or provisions of a trust deed;
  - (h) a right conferred by this Act to apply to the court; and
  - (i) the power to authorise an agent to perform any of the functions of the trustees or trustee.
- (2) Require trustees to keep under review the agency arrangements and the way the arrangements are being put into effect, to consider whether to intervene, and to intervene if necessary. In reviewing the agency and actions of the agent, the trustee must consider whether a trustee exercising the standard of care (R13) would intervene and must do so if such a trustee would consider it necessary.
  - (3) Provide that trustees are not liable to a beneficiary for the acts or defaults of an agent, unless the trustee failed to meet the duty of good faith and honesty (R2(1)(c)) and standard of care (R13) in making the appointment, or the trustee failed to review the agency and agent's actions, or the trustee's actions to intervene did not comply with the duty of good faith and honesty and standard of care.
  - (4) Require that the authorisation of an agent is in writing, is given or delivered to the agent and may be subject to conditions.
  - (5) Allow the trustee to pay the agent a reasonable fee for the agent's services.
  - (6) Not include the list of example professionals that may be appointed as agents as was proposed for new section 29(1)(a) of the Trustee Act 1956 in the Trustee Amendment Bill 2007.
  - (7) Add the following non-exhaustive criteria that a trustee must consider when appointing an agent:
    - whether the intended agent has the appropriate skills, expertise and experience to carry out the task; and
    - the fees the intended agent will charge and whether employing the agent is a cost-effective option.
  - (8) Provide that R10 is a default provision capable of being overridden by the terms of the trust.

R11 The new Trusts Act should include a power to appoint nominees and custodians of trust property and apply the same framework as will apply to agents under R10(2)–(5) and (8), including:

- (a) a power for trustees to appoint a person to act as the trustee’s nominee in relation to some or all of the trust property and to vest that property in the nominee;
- (b) a power for trustees to appoint a person to act as custodian in relation to some or all of the trust property whereby that person undertakes the safe custody of the property or of any documents or records relating to the property;
- (c) a nominee or custodian must be either:
  - (i) a person who carries on a business that consists of or includes acting as a nominee or custodian;
  - (ii) a body corporate that is controlled by the trustee; or
  - (iii) an incorporated law practice;
- (d) the requirement on trustees to keep the arrangement under review (R10(2)), the provision restricting the trustee’s liability (R10(3)), the requirement that the appointment is made in writing (R10(4)) and the power to pay a reasonable fee (R10(5)); and
- (e) that the provision is capable of being overridden by the terms of the trust.

### **Power to appoint delegates**

R12 The new Trusts Act should, as a default position, allow a trustee, by power of attorney, to delegate the execution of all or any of the trustee’s powers, duties and discretions (that the trustee either holds as a sole trustee or jointly with another person). The provision should:

- (1) Add temporary mental incapacity to absence from New Zealand and temporary physical incapacity as the circumstances in which the power of delegation can be exercised.
- (2) State that the delegation:
  - (a) commences as provided by the instrument creating the power or, if the instrument does not provide for the commencement of the delegation, on the date of the execution of the instrument by the trustee; and
  - (b) continues for 12 months or any shorter period provided by the instrument, with one extension by the delegating trustee of up to an additional 12 months.
- (3) Require a trustee delegating the powers (or the delegate, where the trustee is incapable of doing so) to, within seven days of the instrument of delegation taking effect, notify any co-trustees and any person with a power to appoint and remove trustees of:
  - (a) the date on which the delegation comes into effect;
  - (b) the duration of the delegation;
  - (c) the identity of the delegate;
  - (d) the reason for the delegation; and

- (e) which powers, duties and discretions are delegated, where only some are delegated.
- (4) Require sole trustees who are delegating to notify any person with the power to appoint and remove beneficiaries, or if none, all competent adult beneficiaries, or where that is unreasonable or impractical in the circumstances, a reasonably representative sample of beneficiaries.
  - (5) Require notification, as specified in (3), each time an instrument of delegation takes effect.
  - (6) The failure to notify would be considered a breach of trust, but would not, in favour of a person dealing with the delegate, invalidate any act done or instrument executed by the delegate.
  - (7) Retain the current position that trustees are only liable to beneficiaries for the actions or default of a delegate if the trustees did not exercise the duty of good faith and honesty (R2(1)(c)) and the standard of care (R13) in the appointment of the delegate.
  - (8) Clarify that the default position is that a delegate may exercise the power to resign on behalf of a trustee who has delegated the trustee's powers.
  - (9) Retain the current position of allowing delegation to a sole co-trustee only if that co-trustee is a statutory trustee corporation.
  - (10) Allow for a co-trustee or a beneficiary to apply to the Public Trust for the Public Trust to consent to become the delegate for a trustee who is unable or unavailable to make a decision, and cannot be contacted for any reason, and there is no delegation in place.

## Standard of care

R13 The new Trusts Act should:

- (1) Provide that, when exercising a power of administration, including a power to:
  - hold trust property;
  - maintain and develop trust property;
  - deal with trust property;
  - transfer trust property to any person;
  - insure trust property;
  - carry on a business;
  - appoint an agent, nominee or custodian;
  - appoint a delegate; and
  - any other power affecting the administration of trust property,

a trustee must exercise such care and skill as is reasonable in the circumstances, having regard in particular –

- (a) to any special knowledge or experience that the trustee has or holds himself or herself out as having; and
  - (b) if a person acts as a trustee in the course of a business or profession, to any special knowledge or experience that it is reasonable to expect of a person acting in the course of that kind of business or profession.
- (2) The standard of care does not apply to the exercise of a discretion to distribute trust property.
- (3) The standard of care does not apply if or in so far as it appears from the terms of the trust that the duty is not meant to apply.

## CHAPTER 7 – INVESTMENT

### Powers and duties

- R14 (1) The new Trusts Act should provide that:
- (a) a trustee should have the power to invest any trust funds in any property;
  - (b) the power of a trustee to invest in any property set out in (a) above should apply only to the extent that it is not overridden or excluded by the terms of the trust or the terms of the trust do not otherwise limit or modify it; and
  - (c) when exercising the power to invest in property a trustee should comply with any relevant requirements contained in the terms of the trust, including any requirement relating to obtaining consent or compliance with any direction with respect to the investment of the trust fund.
- (2) The new Act should provide that:
- (a) when investing a trustee should have a duty to exercise the care, diligence, and skill that a prudent person of business would exercise in managing the affairs of others;
  - (b) where a trustee has any special knowledge or experience or holds him or herself out as having special knowledge or experience, the trustee should have a duty to exercise the level of care, diligence, and skill that it is reasonable to expect of a person with that special knowledge or experience; and
  - (c) the duties in (a) and (b) apply to a trustee to the extent that they are not excluded or modified, explicitly or implicitly, by the terms of the trust.
- (3) The new Act should make it clear that the power to invest in property and the duty to do so prudently do not of themselves preclude trustees from taking account of other relevant matters when determining how to manage trust funds, or from purchasing or retaining property for purposes other than investment, where this is appropriate to give effect to the objectives or purpose of a trust.

- (4) The powers and duties set out in R14(1) and (2) above should replace sections 13A–13D and sections 13F–13H of the Trustee Act 1956.
- (5) Section 13E of the Trustee Act 1956 (which lists the matters trustees may have regard to when investing) should be re-enacted in the new Act. It should be redrafted to provide that trustees may take into account their overall investment strategy when exercising their powers of investment (as well as the other matters currently listed).
- (6) Section 13M of the Trustee Act 1956 (which lists a number of matters the courts may take into account when considering whether a trustee should be liable for breach of trust in respect of an investment) should be re-enacted in the new Act.
- (7) Section 13Q of the Trustee Act 1956 (which provides that in an action for breach of trust the court may set off a loss arising from an investment against a gain from any other investment) should be re-enacted in the new Act. For the avoidance of doubt, the new Act should clarify that the rule of general trust law that requires the assessment of the decisions of a trustee on an investment by investment basis if the decisions are called into question (the anti-netting rule) is abolished.
- (8) Sections 13I, 13J, 13K, 13L, 13N, 13O and 13P of the Trustee Act 1956 should not be re-enacted because these provisions are now unnecessary.

### Distinction between income and capital

R15 The new Trusts Act should provide that:

- (1) To facilitate total return investment and allow trustees to invest trust funds without regard to whether the return on investment is technically of an income or capital nature, trustees should have discretion to determine whether a return is to be treated as income or capital for the purposes of distribution.
- (2) Trustees should be required to exercise their discretion on how a return is to be treated in a manner that is consistent with their duties as trustees and fairly and reasonably takes into account the interests of all beneficiaries.
- (3) Trustees should ensure that a reasonable level of income is made available for income beneficiaries in situations where there are defined classes of beneficiaries.

#### **Note**

The discretion of trustees to decide what is to be treated as income or capital is for the purposes of trust law and does not in any way alter or override the definitions and application of the revenue statutes, for the purposes of taxation.

## Apportionment of receipts and outgoings

R16 The new Trusts Act should provide that:

- (1) A trustee may:
  - (a) apportion any receipt or outgoing in respect of any period of time between the income and capital accounts, or charge any outgoing or credit any receipt exclusively to or from either income or capital as the trustee considers to be fair and reasonable in all the circumstances and in accordance with accepted business practice;
  - (b) transfer funds between capital and income accounts to recover or reimburse an outgoing previously charged to the account that is to receive the funds where such corrections are fair and reasonable in all the circumstances and are undertaken in accordance with accepted business practice;
  - (c) transfer funds between capital and income accounts to recover or deduct any receipt previously credited to the account from which the funds are to be recovered where such corrections are fair and reasonable in all the circumstances and are undertaken in accordance with accepted business practice; and
  - (d) deduct from income an amount that is fair and reasonable in all the circumstances to meet the cost of depreciation, and add the amount to capital, in accordance with accepted business practice.
- (2) Subject to (5) below, the trustee's powers under (1) above should replace the traditional rules concerning apportionment between capital and income, and those traditional rules are abolished.
- (3) The trustee's powers under (1) above should apply to all trusts established before the date on which the new Act comes into force despite anything to the contrary in the terms of the trust.
- (4) In relation to trusts established on or after the date on which the new Act comes into force, (1) above should be a default provision that applies unless it is modified by the terms of the trust.
- (5) The apportionment rules in the Property Law Act 2007 will continue to apply where the trustee is the landlord, tenant, vendor or purchaser of land.

## Investment managers

R17 The new Trusts Act should provide that:

- (1) Trustees are authorised to appoint investment managers and give them authority to make investment decisions.
- (2) The appointment of investment managers should be subject to the following legislative safeguards:
  - (a) trustees must act honestly and in good faith (R2(1)(c)) and exercise the reasonable care, diligence and skill of a prudent person of business (R14(2)) when appointing an investment manager, and must review the investment manager's performance periodically;

- (b) trustees must create a written policy statement that gives guidance as to how investment functions are to be exercised by an investment manager setting out the general investment objectives, and require investment managers to agree to comply with the policy statement; and
- (c) trustees are liable for any default of their investment manager where the trustees have failed to act honestly and in good faith (R2(1)(c)) and exercise the reasonable care, diligence and skill of a prudent person of business (R14(2)) when making the appointment of a manager or monitoring the investment manager's performance.

## CHAPTER 8 – APPOINTMENT AND REMOVAL OF TRUSTEES

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### Acceptance and rejection of trusteeship

R18 The new Trusts Act should provide that:

- (1) A person who is appointed as a trustee of an express trust may accept or reject the trusteeship.
- (2) Acceptance of a trusteeship must be either express (in writing or oral) or clearly implied through conduct, unless otherwise specified in the terms of the trust.
- (3) Rejection of trusteeship need not be in writing (unless the terms of the trust specify otherwise), but must be communicated to the person specified under the terms of the trust (such as the settlor or appointer) in clear and unambiguous terms.
- (4) If a trustee does nothing to accept or reject a trusteeship within three months of receiving notice of the appointment, the trustee will be deemed to have rejected the trusteeship.
- (5) If a trustee rejects the trusteeship, the property vests in the remaining trustees.

### Who may be a trustee?

R19 The new Trusts Act should provide that any natural person or body corporate may be appointed as trustee of a trust, except:

- (a) a natural person under 18 years of age;
- (b) an undischarged bankrupt (an undischarged bankrupt may be appointed with the consent of the court);
- (c) a person who is subject to a property order made under section 31 of the Protection of Personal and Property Rights Act 1988 or a person for whom a trustee corporation is acting as manager under sections 32 or 33 of that Act; and
- (d) a corporation that is in receivership, liquidation or voluntary administration (or any similar status).



## Mandatory and discretionary grounds for removal of a trustee

R20 The new Trusts Act should:

- (1) Require the removal of certain trustees by imposing an obligation on persons with the power to appoint and remove trustees under R21(1) to remove a trustee when the following mandatory grounds are met:
  - (a) the trustee is incapacitated; and
  - (b) the trustee is subject to either an enduring power of attorney in relation to property or a property order, or has a trustee corporation appointed to act as a manager under the Protection of Personal and Property Rights Act 1988; and
  - (c) the trustee's powers have not been delegated by a delegation authorised by statute or by the terms of the trust.
- (2) Empower (but not require) persons with the power to appoint and remove trustees under R21(1) to remove a trustee and appoint a replacement, if it is desirable for the proper functioning of the trust, when one or more of the following discretionary grounds are met:
  - (a) the trustee refuses or fails to act as a trustee;
  - (b) the trustee, being a corporate trustee, enters into receivership or liquidation, ceases to carry out business, is dissolved, enters into a compromise with creditors or voluntary administration under Parts 14 or 15A of the Companies Act 1993, or does not satisfy the solvency test in section 4 of that Act;
  - (c) the trustee is no longer considered suitable to continue to hold office as a trustee because of circumstance or conduct, for instance, this may be the case when:
    - (i) the whereabouts of the trustee is unknown and the trustee cannot be contacted;
    - (ii) the trustee is not capable of fulfilling the role because of sickness or injury;
    - (iii) the trustee is adjudged bankrupt;
    - (iv) the trustee is convicted of a dishonesty offence;
    - (v) the trustee becomes precluded from serving as a director under the Companies Act 1993 because of a breach of that Act or the Securities Act 1978, or is the subject of a current banning order under the Financial Markets Conduct legislation;
    - (vi) the court finds the trustee has committed serious misconduct in the administration of the trust; or
    - (vii) the trustee, being a lawyer, chartered accountant or financial adviser, is found to have seriously breached the applicable ethical standards of that profession, resulting in the trustee being struck off, losing a license or being disqualified.
- (3) Retain the court's general discretion to remove trustees if expedient, including the discretion to remove a trustee without appointing a replacement in accordance with R25.

- (4) Provide that nothing in (1) or (2) is to be read as limiting the grounds on which a person nominated under the terms of the trust with a power to remove and appoint trustees is entitled to exercise that power.

### Who may remove a trustee and appoint a replacement

R21 The new Trusts Act should provide that:

- (1) In absence of any contrary intention in the terms of the trust, the following persons have the power to remove and appoint trustees by deed when the grounds in R20 are met:
  - (a) the person nominated under the terms of the trust with a power to remove and appoint trustees; or
  - (b) if there is no person in (a) or if that person is unavailable or unwilling to make a decision, the remaining trustees; or
  - (c) if there is no person in (a) or (b) or if that person is unavailable or unwilling to make a decision, whichever of these representatives of the trustee being removed is relevant:
    - (i) a property manager appointed over the trustee under the Protection of Personal and Property Rights Act 1988;
    - (ii) the holder of an enduring power of attorney over property of an incapacitated trustee; or
    - (iii) the liquidator of a corporate trustee that enters into liquidation.
- (2) Where a representative of the trustee listed in (1)(c) acts to remove and replace, the following process applies:
  - (a) the representative should provide notification of the intended discharge of the trustee and of the person selected as replacement, and a statement of the trust accounts to all competent adult beneficiaries, or where it is unreasonable or impractical to do so, to a reasonably representative sample of beneficiaries;
  - (b) the beneficiaries should be given 20 working days from the date that notification is received to object to the intended replacement trustee or to anything in the statement of trust accounts;
  - (c) at the end of the notice period, if no one has objected the representative should apply to the Public Trust to confirm the discharge and replacement of the trustee;
  - (d) the Public Trust, if it is satisfied that due notice and information was given to the beneficiaries and that no objections have been made, may confirm the discharge and replacement of the trustee by deed;
  - (e) if a beneficiary objects, an application will need to be made to the court for the trustee to be removed and replaced;
  - (f) if the Public Trust:

- (i) is not satisfied regarding the notice and information given to the beneficiaries; or
- (ii) has concerns because of issues raised by the beneficiaries, disagreement between the parties, or any other reason,

it may decline to confirm the discharge and replacement of the trustee. An application will need to be made to court for the discharge and replacement of the trustee and the court will be able to make any other necessary directions about the management of the trust.

### **Appointment of replacement when trustee dies while in office**

R22 The new Trusts Act should provide that, in absence of any contrary intention in the terms of the trust:

- (a) if a trustee dies while in office and it is necessary, either because the trustee was a sole trustee or because the terms of the trust require it, or desirable for the trustee to be replaced, the replacement may be appointed by deed by:
  - (i) the person nominated under the terms of the trust with a power to remove and appoint trustees; or
  - (ii) if there is no person in (i) or if that person is unavailable or unwilling to make a decision, the remaining trustees; or
  - (iii) if there is no person in (i) or (ii) or if that person is unavailable or unwilling to make a decision, the executor or administrator of the trustee; and
- (b) if the deed of replacement is to be made by the executor or administrator, the process of notification of beneficiaries and confirmation by the Public Trust in R21(2) should apply.

### **Retirement and replacement of trustee**

R23 The new Trusts Act should provide that, in absence of any contrary intention in the terms of the trust:

- (a) if a trustee wishes to retire, the trustee may be discharged by deed by:
  - (i) the person nominated under the terms of the trust with a power to remove and appoint trustees; or
  - (ii) if there is no person in (i) or if that person is unavailable or unwilling to make a decision, the remaining trustees; or
  - (iii) if there is no person in (i) or (ii) or if that person is unavailable or unwilling to make a decision, the retiring trustee and a replacement trustee, selected by the retiring trustee, together; and

- (b) if (a)(iii) applies, which will be the case if the retiring trustee is a sole trustee or if the persons in (a)(i) and (ii) are unavailable or unwilling, the process of notification of beneficiaries and confirmation by the Public Trust in R21(2) applies (with necessary amendments).

### Exercise of power to remove and appoint trustees

R24 The new Trusts Act should provide that:

- (1) Those who exercise a power to discharge and/or appoint trustees under the new Act (under R20, R22 and R23) rather than because they are appointed by the terms of the trust are subject to a mandatory duty to exercise the power in good faith, honestly and for a proper purpose (R2).
- (2) The court may remove and replace someone with the power to discharge and appoint trustees under the terms of the trust if that person has exercised the power unlawfully, or if that person has been removed as a trustee, or if otherwise expedient.
- (3) A person with the power to appoint trustees would be entitled to apply to the court for directions in the exercise of that power.

### Numbers of trustees

R25 The new Trusts Act should provide, in absence of any contrary intention in the terms of the trust, that:

- (a) trustees can be removed without being replaced, provided that this will not result in there being fewer trustees than the minimum number prescribed in the terms of the trust; and
- (b) if a sole trustee is removed or dies in office, the trustee may be replaced with more than one replacement trustee, unless the terms of the trust provide otherwise.

### Transfer of trust property

R26 The new Trusts Act should:

- (1) Impose a duty on a departing trustee to transfer property to the continuing trustees, including to complete formalities for the transfer of registered property interests.
- (2) Provide that a trustee shall be divested of all trust property if validly removed from office (including through death or voluntary discharge), and provide that the trust property shall vest in the continuing trustees, subject to liabilities attaching to the trust property.
- (3) Provide, as a default provision, that where a trustee has been removed but has not transferred the trust property to a continuing trustee:
  - (a) the continuing trustee must give the departing trustee notice that the departing trustee will be divested of the trust property after 20 working days;

- (b) if the departing trustee objects within 20 working days, the continuing trustee must apply to court for a transfer order;
- (c) if the departing trustee does not object within 20 working days, the Public Trust may, upon request of the continuing trustee, issue a statutory certificate of vesting confirming that the deeds which remove the departing trustee and appoint the continuing trustees have been validly executed (a vesting certificate issued by the Public Trust will not be ineffective for failure of the notice provisions);
- (d) the Public Trust may refuse to grant a vesting certificate when it considers that the property arrangement is complex or it is not clear whether the trustee was properly removed or for any other reason, and the continuing trustee must apply to the court for a transfer order;
- (e) the continuing trustee may submit the vesting certificate to registries of property interests, in which case the statutory certificate of vesting shall be sufficient and complete proof of change of ownership of property, and:
  - (i) must be accepted as complete documentation under section 99A of the Land Transfer Act 1952; and
  - (ii) must be accepted as proof of transfer of any other registered interest recorded in a register under New Zealand law;
- (f) the departing trustee must be given the documents demonstrating that the property is no longer in the departing trustee's name once transfer and registration are complete; and
- (g) a registry that transfers property in reliance on a statutory vesting certificate is not liable for any loss caused as a result of the transfer of property.

## CHAPTER 9 – CUSTODIAN AND ADVISORY TRUSTEES

### Custodian trustees

R27 The new Trusts Act should re-enact section 50 of the Trustee Act 1956 in modernised form with the following clarifications, additions and reforms:

- (a) continue to provide for the appointment of a corporation as a custodian trustee;
- (b) provide that, subject to the terms of the trust:
  - (i) the role of the custodian trustee is to hold the trust property, invest funds and dispose of the assets as the managing trustee directs in writing;
  - (ii) the trust property vests in the custodian trustee as if the custodian trustee were the sole trustee;
  - (iii) the management of the trust property and exercise of all powers and discretions exercisable by the trustee under the trust remain vested in the managing trustees as if there were no custodian trustee;
  - (iv) the custodian trustee has all the administrative powers of a trustee but none of the discretionary powers;

- (v) the custodian trustee has the power to execute any documents or perform any administrative action directed by the managing trustee; and
- (vi) the custodian trustee may be appointed over part of the trust fund.
- (c) provide that the custodian trustee must act on the instructions of the managing trustee and is liable for loss caused by:
  - (i) failing to execute the instructions of the managing trustee; or
  - (ii) acting without the authority of the managing trustee;
- (d) provide that the custodian trustee is not liable for executing instructions of the managing trustee where the managing trustee is in breach of trust;
- (e) provide that the custodian trustee may apply to the court for directions if it receives instructions from the managing trustee that it suspects are in breach of trust, but shall not be liable for a failure to do so;
- (f) provide that, in addition to any remuneration or commission payable to the custodian trustee, the custodian trustee has the benefit of the right of indemnity in respect of costs incurred by the custodian trustee; and
- (g) provide that the appointment of a custodian trustee must be in writing.

#### **Advisory trustees (special trust advisers)**

- R28 The new Trusts Act should re-enact section 49 of the Trustee Act 1956 in modernised form with the “advisory trustee” renamed the “special trust adviser” and with the following clarifications and reforms:
- (a) a special trust adviser may advise the trustee on any matter relating to the trust;
  - (b) a special trust adviser is not a trustee, and does not have the powers and duties of a trustee;
  - (c) the trustee is not liable for anything done or omitted by the trustee by reason of following the special trust adviser’s advice unless the trustee is acting dishonestly, in wilful breach of trust or grossly negligent in following the advice (replacing proviso (c) to section 49(3) of the Trustee Act 1956); and
  - (d) the trustee is not liable for a breach of trust merely because the trustee elects not to follow the special trust adviser’s advice.

## CHAPTER 10 – REVOCATION AND VARIATION

### Revocation and variation by beneficiaries

R29 The new Trusts Act should:

- (1) State the common law rule (known as the rule in *Saunders v Vautier*) which provides that:
  - (a) where they are in agreement, legally capable adult beneficiaries who hold the entire beneficial interest in the trust property may act together to revoke a trust and require the trustees to distribute the trust property as they direct; and
  - (b) a legally capable adult beneficiary of a fixed share of trust property may, where the beneficiary has an absolute vested interest in that share, request the trustees to transfer that share to him or her. The trustees may only refuse to do so where the property is not in a form, or cannot be changed into such a form, that allows the beneficiary's share to be transferred to the beneficiary without detrimentally affecting the interests of other beneficiaries.
- (2) Clarify that where they are in agreement, and with the agreement of the trustees, legally capable adult beneficiaries who hold the entire beneficial interest in the trust property may act together to confer new powers upon trustees or deviate from, or vary, the terms of the trust.
- (3) Clarify that legally capable adult beneficiaries who hold the entire beneficial interest in the trust property may consent to a resettlement of a trust, as well as a variation or revocation.

### Revocation and variation by the court

R30 The new Trusts Act should provide that:

- (1) The court may:
  - (a) approve any revocation, variation or resettlement of a trust or any change to the scope or nature of the powers of the trustees to manage or administer the trusts on behalf of the following beneficiaries:
    - (i) persons under the age of 18 years;
    - (ii) incapacitated persons;
    - (iii) persons who may become entitled at a future date or on the happening of a future event or once they become a member of a certain class; and
    - (iv) future persons; and
  - (b) waive the requirement for the consent of any other person and approve any revocation, variation or resettlement of a trust or any change to the scope or nature of the powers of the trustees to manage or administer the trusts.
- (2) When considering whether to approve or waive the requirement for consent to a revocation, variation or resettlement of a trust or any change to the scope or nature of the powers of the trustees under (1) the court must take into account the following factors:

- (a) the nature of any person's interest and the effect any proposed varying arrangement may have on that interest;
  - (b) the benefit or detriment to any person that may result from the court approving any proposed varying arrangement;
  - (c) the benefit or detriment to any person that may result from the court declining to approve any proposed varying arrangement; and
  - (d) the intentions of the settlor to the extent these can be ascertained.
- (3) The court must not make an order under (1) of the proposed provision if its effect would be to reduce or remove any fixed indefeasible interest or interest that has vested absolutely in a beneficiary.
- (4) Any order of approval or waiver that is made by the court under (1) should be binding on all persons on whose behalf it is made (including any person who is the subject of an order of waiver) and the trusts should take effect as rearranged.

### Extension of trustees' powers by the court

R31 The new Trusts Act should provide that:

- (1) The court may make amendments to the non-distributive administrative provisions of the terms of any trust where it considers this necessary to enable the trustees to efficiently manage trust property.
- (2) Under (1) the court may amend the terms of a trust to enlarge or extend the scope of the powers available to the trustees for administering or managing trust property.
- (3) The court may not make amendments to the terms of a trust that alter or otherwise change the beneficial interests under the trust under this recommendation.

## CHAPTER 11 – REVIEWING THE ACTIONS OF TRUSTEES

R32 The new Trusts Act should include a review provision to replace section 68 of the Trustee Act 1956 with the following features:

- (1) The court should be able to review the act, omission or decision (including a proposed act, omission or decision) of a trustee on the grounds that the act, omission or decision was not reasonably open to the trustee in the circumstances.
- (2) The procedure for review should be a two stage process:
  - (a) an applicant for review should be required to put forward evidence that raises a genuine and substantial dispute as to whether the act, omission or decision in question was reasonably open to the trustee in the circumstances (first stage); and
  - (b) if the court is satisfied that the applicant has established a genuine and substantial dispute, the court must allow the trustee the opportunity to appear before the court and put forward evidence establishing that the act, omission or decision was reasonably open to the trustee in the circumstances (second stage).



- (3) Where the court finds, on a balance of probabilities, that the trustee's act, omission or decision was not reasonably open to the trustee in the circumstances, the court may set aside the act or decision, restrain the trustee from acting or deciding the case, or in the case of an omission direct the trustee to act.
- (4) The court must not make any order under the provision that affects:
  - (a) a distribution of the trust property that has been made not in breach of trust and before the trustee had notice of the application; or
  - (b) any right or title acquired by a person in good faith and for value.
- (5) A trustee's act, omission or decision under a power either in the new Act or the terms of the trust would be subject to review under the new provision.
- (6) An application for review may only be made by:
  - (a) a beneficiary; or
  - (b) any personal representative of a beneficiary who lacks capacity (such as a parent or guardian of a minor beneficiary, or a property manager or holder of an enduring power of attorney for an incapacitated beneficiary).

## CHAPTER 12 – OTHER POWERS OF THE COURT

### Section 66 – Power of court to give directions

R33 The new Trusts Act should provide:

- (1) That any trustee may apply to the court for directions concerning any property subject to a trust, or respecting the management or administration of any such property, or respecting the exercise of any power or discretion vested in the trustee (replacing section 66 of the Trustee Act 1956).
- (2) Whenever possible, a trustee should present to the court a proposed course of action or possible course of action regarding the matter on which the trustee seeks directions.
- (3) Every application for directions should be served upon, and the hearing attended by, any person interested in the application or such interested persons as the court otherwise determines.
- (4) For the avoidance of doubt:
  - (a) a court may refuse to provide directions if it would be more expedient for the issues to be addressed through a different form of proceedings;
  - (b) an application for directions under the section can only be made by a trustee for the time being of the trust in question; and
  - (c) the court's power to give directions under (1) does not restrict the ability of the trustee to apply to the court for a declaration as to the interpretation of the trust instrument.

## Section 72 – Payment of a commission to a trustee

R34 The new Trusts Act should re-enact section 72 of the Trustee Act 1956 (under which the court may authorise payment of a reasonable fee or remuneration to a trustee out of trust property) subject to the following modifications:

- (1) The new provision (replacing section 72) should provide that when determining what payment would be just and reasonable the court must consider:
  - (a) the total amount that has already been paid to any trustee of the trust, whether pursuant to the terms of the trust or to any earlier order of the court or to any agreement or otherwise;
  - (b) the amount and difficulty of the services rendered by the trustee;
  - (c) the liabilities to which the trustee is or has been exposed, and the responsibilities imposed on the trustee;
  - (d) the skill and success of the trustee in administering the trust;
  - (e) the value of the trust property;
  - (f) the time and services reasonably required of the trustee;
  - (g) whether any payment that might otherwise have been allowed should be refused or reduced due to the conduct of the trustee in the administration of the trust; and
  - (h) all other circumstances that the court considers relevant.
- (2) The court should only authorise payment under the provision where the trustee has provided services above and beyond what would normally be expected from a trustee.

## Section 74 – Beneficiary indemnity for breach of trust

R35 The new Trusts Act should:

- (1) Re-enact section 74 of the Trustee Act 1956, under which the court may, where a trustee has committed a breach of trust at the instigation or request or with the consent in writing of a beneficiary, make any order the court considers just indemnifying the trustee from the beneficiary's interest in the trust property.
- (2) Remove the antiquated reference to "married women restrained from anticipation".

## Section 75 – Barring claims and future claims

R36 The new Trusts Act should:

- (1) Include a provision (replacing section 75 of the Trustee Act 1956) under which a trustee may give notice to any claimant or potential claimant requiring the trustee to take proceedings within three months from the date of service; or to enforce the claim through the court.
- (2) Provide that where a potential claimant on whom notice has been served fails to take proceedings, or fails to enforce the claim through the courts, the trustee may apply to the court for an order to have the claim barred.

- (3) Provide that, as is currently provided in section 75, nothing in the new provision applies to any claim under the Family Protection Act 1955.

### **Sections 77 to 79 – Payments to the Crown**

R37 The new Trusts Act should re-enact, with the following changes, the provisions in sections 77 to 79 of the Trustee Act 1956 under which trustees may pay unclaimed monies over to the Crown where they are unable to find beneficiaries and distribute the monies:

- (1) The requirement for trustees to file an affidavit should be abolished and trustees should be required to give the Secretary to the Treasury information about the trust and beneficiaries (such as a copy of the trust deed and a statement of accounts).
- (2) The Secretary to the Treasury should have a power to refuse to accept money where he or she is not given the required information about the trust and its beneficiaries.
- (3) The obligation on the Secretary to the Treasury to publish a statement of all money held annually in the Gazette should be replaced by a more general requirement that he or she make that information publicly available in a manner that is likely to bring it to the attention of potential claimants. The obligation could in practice be fulfilled by putting the information into an online directory of unclaimed funds on a website.
- (4) There should be no requirement on the Crown to pay any interest to claimants on any of the funds held under the provisions.
- (5) The Crown should have a power to deduct any reasonable costs and expenses before making payment to any claimant.

### **Section 76 – Distribution of shares of missing beneficiaries**

R38 The new Trusts Act should re-enact section 76 of the Trustee Act 1956 (under which the court has broad powers to approve distributions by trustees where beneficiaries cannot be traced). The following changes should be made to the advertising requirements in the provision:

- (1) Trustees should be required to give notice advertising for potential beneficiaries in a manner that is likely to bring the notice to the attention of potential beneficiaries.
- (2) Trustees may seek directions from the court where there is doubt as to what notice advertising for potential beneficiaries is appropriate.

### **Section 35 – Protection against creditors by means of advertising**

R39 The new Trusts Act should re-enact section 35 of the Trustee Act 1956, which protects trustees from liability where they advertise and give notice to potential creditors before distributing property under a trust. The following changes should be made to the advertising requirements in the provision:

- (1) Trustees should be required to give notice advertising for claims in a manner that is likely to bring the notice to the attention of potential claimants.
- (2) Trustees may seek directions from the court where there is doubt as to what notice advertising for claims is appropriate.

## CHAPTER 13 – JURISDICTION OF THE COURTS

### High Court and District Court jurisdiction

R40 The new Trusts Act should provide that:

- (1) The High Court has jurisdiction to hear any matter and make any order under the proposed new Trusts Act. It should have exclusive jurisdiction to determine any proceeding under the new Act where the amount claimed, or the value of the property claimed or in issue, is more than the upper limit of the equitable jurisdiction of the District Court specified in section 34(1) of the District Courts Act 1947 (currently \$200,000) or any replacement provision.
- (2) The District Court should have jurisdiction under the new Act (concurrent with the High Court) to determine any proceeding where the amount claimed or the value of the property claimed or in issue is not more than the upper limit of the equitable jurisdiction of the District Court (currently \$200,000).
- (3) The District Court should also have jurisdiction (concurrent with the High Court) to determine any proceedings or applications (such as an application to appoint or remove a trustee) that does not involve any claim for money or property.
- (4) Where the District Court and High Court have concurrent jurisdiction the person who commences proceedings (the applicant) may decide whether to commence the proceedings in the District Court or High Court.
- (5) Section 43 of the District Courts Act 1947 should apply to the transfer of proceedings commenced in the District Court. The effect of this would be that:
  - (a) where the proceedings involve a claim for money, relief or property with a value that exceeds the amount specified in section 43 (currently \$50,000) a defendant may object to the proceeding being determined in the District Court and have the proceeding transferred (as of right) to the High Court; and
  - (b) where the proceedings do not include a claim for money, relief or property with a value that exceeds the amount specified in section 43 a defendant wishing to transfer the proceedings must apply to the District Court for an order removing the proceedings to the High Court. Proceedings that do not include any claim for money, relief or property fall within this category under section 43.

#### Notes

- (1) The Government has announced, in response to the Law Commission Report *Review of the Judicature Act 1908: Towards a New Courts Act* that new courts legislation soon to be introduced will increase the upper financial limit of the District Court's equitable jurisdiction from \$200,000 to \$350,000 and will increase the threshold specified in

section 43 over which claims may be transferred as of right to the High Court from \$50,000 to \$90,000.

- (2) Section 237 of Te Ture Whenua Maori Act 1993 will apply to give the Māori Land Court all of the powers of the High Court under the proposed new Trusts Act in respect of trusts to which Te Ture Whenua Maori Act 1993 applies.

### Family Court jurisdiction

R41 Where the Family Court has jurisdiction under section 11 of the Family Courts Act 1980 to hear and determine proceedings:

- (1) The Family Court should be able to make any order or give any direction available under the new Trusts Act during those proceedings where the Court considers such order or direction necessary to:
  - (a) protect or preserve any property or interest until the proceedings before the Court can be properly resolved; or
  - (b) to give proper effect to any determination of the proceedings before the Court.
- (2) Where the parties consent, the Family Court should also be able to make any orders under the new Trusts Act to resolve any closely related dispute or issue between the parties where this is necessary or would assist the resolution of the substantive proceedings between the parties.

#### Note

The Family Court's jurisdiction under the new Trusts Act would not be subject to financial limits.

## CHAPTER 14 – RESOLVING DISPUTES OUTSIDE OF THE COURTS

R42 The new Trusts Act should:

- (1) Clarify that trustees have a power to use alternative dispute resolution (ADR) to settle an internal dispute (between trustees and beneficiaries) or an external dispute (between trustees and third parties), other than a dispute as to the validity of all or part of a trust. This should be a default power that applies unless explicitly excluded or modified by the terms of the trust.
- (2) Make any provision in the terms of a trust that requires the settlement of a dispute by ADR enforceable, other than a dispute as to the validity of all or part of a trust.
- (3) Give trustees a specific power to give future assurances of actions that have been agreed to as a part of an ADR settlement.
- (4) Provide that trustees will not be liable to other parties for agreeing to the settlement if they acted honestly and in good faith while doing so.
- (5) Provide that by virtue of this provision, an ADR settlement cannot override creditor priority rules as they affect creditors that are not party to the settlement.

- (6) Provide that a beneficiary or trustee can make a request to the court that ADR be used to resolve a dispute rather than court proceedings and that the court can require ADR to be used. It should be open to the court to allow the costs of the mediation to be paid from the trust.
- (7) Provide that the court can appoint representatives of unascertained and incapacitated beneficiaries, who may be other beneficiaries, who can agree to a binding ADR settlement on behalf of the unascertained and incapacitated beneficiaries, subject to the court's approval of the settlement.

## CHAPTER 15 – THE PUBLIC TRUST

R43 The new Trusts Act should provide that:

- (1) Where carrying out any of the roles it has under the new Trusts Act would involve any element of dispute or contention or significant complexity, the Public Trust should not act.
- (2) The Public Trust should be accountable to the Government for the exercise of its roles under the new Trusts Act.
- (3) The Public Trust could charge a reasonable fee for carrying out the roles under the new Trusts Act.

### Note

The roles recommended for the Public Trust in the Report are:

- the power to make decisions on behalf of a trustee where the trustee is temporarily unavailable and cannot be contacted for any reason and no delegation is in place (R12);
- overseeing the removal and/or replacement of a sole trustee on the ground of incapacity or similar where there is no one else with authority to do this apart from the court (R21);
- overseeing the appointment of a replacement of a sole trustee who dies while in office where there is no one with the power to appoint a new trustee under the trust deed (R22);
- overseeing the retirement and replacement of a sole trustee when there is no one else with the power to appoint a new trustee under the trust deed (R23);
- providing a vesting certificate to confirm that assets are vested in a named new trustee where a former trustee has not and cannot now transfer the trust assets (R26).

R44 The new Trusts Act should re-enact section 83B of the Trustee Act 1956, relating to an application for the accounts of trust property to be audited, in modernised form and with modification so that the process continues to rely on an application to the Public Trust, but no longer also requires an application to a judge in chambers as is currently the case.

**Standing of the Official Assignee to challenge a trust**

R45 The Insolvency Act 2006 should be amended to provide that the Official Assignee has standing to apply to the court to challenge the validity of a trust regardless of whether the bankrupt could have done so prior to the bankruptcy.

**Appointment of a receiver for trusts**

R46 The new Trusts Act should:

- (1) Recognise the court’s jurisdiction to appoint a receiver of a trust, which could manage the trust property, on application or on its own motion.
- (2) Provide that applications for appointment of a receiver of a trust would be heard only in the High Court.
- (3) Specify the grounds on which a receiver may be appointed; who may act as a receiver; the powers and duties of a receiver; priorities of those involved; a process for terminating the receivership; and provision for the receiver’s fees to be paid out of the trust property.

**Trustee’s right to indemnity**

R47 The new Trusts Act should include a provision setting out the following principles:

- (1) A trustee assumes personal liability for expenses and liabilities incurred by the trustee when acting on behalf of the trust.
- (2) A trustee is entitled to be reimbursed from the trust property, or may pay out of the trust property, expenses and liabilities reasonably incurred by the trustee when acting on behalf of the trust.
- (3) A trustee’s indemnity in (2) cannot be limited or excluded by the terms of the trust and applies regardless of any contrary intention expressed in the terms of the trust.
- (4) Notwithstanding (3), the terms of the trust may rank the order in which the trust property may be used to meet the trustee’s expenses through the trustee’s indemnity; this ranking may be set aside on application to court by a trustee, creditor or beneficiary, if the court considers it appropriate, for example on the basis of fraud.
- (5) The indemnity in (2) is available to a former trustee in respect of actions taken by the trustee when acting as trustee.

## Creditors dealing with trustees

R48 The new Trusts Act should provide that:

- (1) A creditor to whom a trustee has incurred liability (or the Official Assignee) can rely on the trustee's indemnity to claim against the trust property to satisfy the liability, even if the trustee is not entitled to be fully indemnified.
- (2) This section would only apply where the creditor has given value and the trust property has received a benefit from the transaction between the trustee and the creditor.
- (3) This section would only apply where the creditor has acted in good faith and would not apply if the creditor had knowledge of the circumstances that impaired the trustee's indemnity at the time the transaction was entered into.
- (4) The creditor would take priority over beneficiaries under this section, subject to a decision of the court.
- (5) The creditor would only be able to rely on the trustee's indemnity to the extent of the value that they have given.

## CHAPTER 17 – PERPETUITIES AND THE MAXIMUM DURATION OF TRUSTS

R49 The new Trusts Act should:

- (1) Repeal the Perpetuities Act 1964 and provide that the common law rule against perpetuities is of no application in New Zealand from the date of the repeal forward.
- (2) Provide a default duration of 150 years for all trusts (a shorter period may be specified in the terms of the trust).
- (3) Provide that at the expiry of 150 years from the date of the establishment of a trust, all trust property is to be vested in accordance with the provisions contained in the terms of the trust, or if the trust deed is silent about who is to receive the property, it is to be vested in all surviving beneficiaries in equal shares.
- (4) Provide that trusts which include a mechanism to calculate the vesting date rather than specifying a duration shall continue until the earlier of the date resulting from the calculation, or 150 years from the establishment of the trust.
- (5) Provide that, notwithstanding these reforms, distributions which were valid under the Perpetuities Act 1964 at the date they occurred remain valid.
- (6) Repeal section 59(2) of the Property Law Act 2007 to reflect the abolition of the rule against perpetuities.
- (7) Update the rule against accumulations to reflect the abolition of the rule against perpetuities, and clarify that trustees may accumulate income, provided the terms of the trust do not prevent this, and provided the accumulated income is distributed upon or before the termination of the trust.



- (8) Carry over the existing exemptions allowing the trusts referred to in section 19 of the Perpetuities Act 1964 to continue indefinitely and apply these exemptions to the rule limiting the duration of trusts (trusts for retirement schemes under the Financial Markets Conduct legislation, currently referred to as superannuation schemes, and certain trusts of a share purchase scheme under section YA1 Income Tax Act 2007), as well as trusts currently exempted in their own legislation.
- (9) Provide that these reforms will apply to all trusts, not only express trusts within the new Act.

## CHAPTER 19 – RELATIONSHIP PROPERTY AND TRUSTS

- R50 Section 44C(2)(c) of the Property (Relationships) Act 1976 should be amended to provide that the court may make an order requiring the trustees of the trust to pay to one spouse or partner a specified sum of money from the trust property or to transfer to one spouse or partner any property of the trust. A consequential amendment would need to be made to the wording in section 44C(3)(b)(i) to replace the reference in that subsection to “distribute the income of the trust” with something like “distribute a sum of money or property of the trust”. Section 44C should otherwise remain unchanged.
- R51 Section 182 of the Family Proceedings Act 1980, under which the courts may vary the terms of ante- and post-nuptial settlements, including trusts, when a marriage or civil union is dissolved, should be amended to also cover de facto relationships. The following changes should be made to the jurisdictional requirements of section 182:
- (a) the terms “de facto partner” and “de facto relationship” should have the same meaning as these terms have in sections 2C and 2D of the Property (Relationships) Act 1976;
  - (b) the triggering event that allows an application to be made to the court, or the court to make an order varying any qualifying settlement, should be changed from when a marriage or civil union is dissolved to when the parties to a relationship separate; and
  - (c) an application to the court should be able to be made in respect of relationship settlements rather than nuptial settlements. The term “relationship settlement” may need to be defined.



# Part 1

## BACKGROUND AND CONCEPTUAL ISSUES



LAW · COMMISSION  
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# Chapter 1

## Introduction

### FIRST REPORT ON THE TRUSTS REFERENCE

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- 1.1 This Report is the Law Commission's first report from its Trusts reference. It concerns the core institution of the trust. We recommend replacing the outdated and outmoded Trustee Act 1956 with a modern Trusts Act. While this Report marks the end of this stage of the Commission's reference, we intend that it be followed by a review of charitable and other purpose trusts, and a review of statutory trustee companies and other companies and bodies corporate that act as trustees.
- 1.2 This Report is the culmination of four years' work at the Law Commission. Over that period the Commission has produced five issues papers that have considered both broad issues relating to the law of trusts and particular matters of detail within the current Trustee Act. We received submissions on these papers. In addition, we produced a *Preferred Approach Paper* in October 2012,<sup>8</sup> and consulted over the summer of 2012/2013 on the proposals in that paper. We have taken careful account of the submissions received. The Commission has also been fortunate to be able to draw upon a distinguished reference group of practitioners and academics who provided great assistance as we formulated the issues papers, the *Preferred Approach Paper* and this final Report.

### STRUCTURE OF THIS REPORT

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- 1.3 We intend that this Report record our recommendations and also that it provide an important resource for those involved in interpreting the new Trusts Act as to how the reforms relate to the general law of trusts.
- 1.4 This Report is set out in five parts. Part 1 sets out our general approach and the principles that have guided our reform. We seek here to explain not only the justification for the recommendations set out in the second part, but also to set out the relationship that we see between our reforms and the law of trusts as it currently stands and indeed the general law.
- 1.5 We also seek to explain how our proposals ought to be considered as a package and interpreted as such when implemented. As we explain in Part 1, the proposed new Trusts Act will interact with the current law in different ways. First, some of the provisions in the new Act reflect what is generally understood as the current law. The intention of recommending the statutory recognition of the duties of trustees, for example, is to clarify rather than reform the current law. It would be appropriate to interpret these provisions as reflecting their equitable principles and understandings. Second, at times we recommend what might be considered modifications, or tailoring, of current law, and it would be appropriate to interpret those modifications or alterations in light of case law, but also in light of the intentions behind our recommendation for modification. Third, we sometimes recommend the considerable alteration, or even reversal, of the current equitable principles or case law.

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<sup>8</sup> Law Commission *Review of the Law of Trusts – Preferred Approach* (NZLC IP31, 2012) [*Preferred Approach Paper*].

- 1.6 Parts 2 to 5 of this Report contain our particular recommendations. The division into parts broadly replicates the divisions used in the *Preferred Approach Paper*. We have included a narrative description of recommendations and their justifications, and at times also indicate why we have chosen a particular form of recommendation.
- 1.7 One of the persistent concerns in submissions and at consultation meetings was exactly how recommendations setting out the characteristics of trusts, articulating duties of trustees, or restricting exemption clauses might look in the proposed Trusts Act. With the assistance of the Parliamentary Counsel Office, we are able to include indicative drafting of these provisions as well as those giving effect to our recommendations on the review of trustee decisions, the setting out of trustee indemnities and the variation and revocation of trusts. Where appropriate, we have annotated these provisions with comments explaining why we have reached particular drafting outcomes.
- 1.8 Chapters deal with particular topics. Rather than repeating the material that we have previously discussed in issues papers or the *Preferred Approach Paper*, we have sought in the individual chapters to build on that analysis. At some points, it may be necessary for those who seek particular detail to refer back to the relevant issues paper or the *Preferred Approach Paper*. We have included description and analysis of the submissions we have received on our *Preferred Approach Paper*, and have indicated where we have altered our position as a result of those submissions or further analysis. Where, as is sometimes the case, we have continued with the original proposal despite submissions to the contrary, we have stated why we have reached that conclusion.

## THE ORIGINS OF THE REFERENCE

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- 1.9 This Report, and all of the work on which it is based, has its origins in an earlier Law Commission Report, *Some Problems in the Law of Trusts*, issued in April 2002.<sup>9</sup> As the title indicates, rather than the comprehensive review of the law of trusts that we have undertaken, the Law Commission was then concerned with a limited number of problems relating to the law of trusts:
- trustees' power of delegation;
  - exculpating trustees;
  - remuneration of trustees;
  - protectors;
  - trustees' powers to insure;
  - trading trusts;
  - challenging the exercise of powers of appointment;
  - trustees' obligation to provide information; and
  - conflicts of law issues.
- 1.10 The Trustee Amendment Bill 2007 would have given substance to many of the particular recommendations made by the Law Commission in *Some Problems in the Law of Trusts*. While the Bill was considered and reported back by the Justice and Electoral Committee, it was never given a second reading. The Bill was discharged in March 2012, because of this project. The

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<sup>9</sup> Law Commission *Some Problems in the Law of Trusts* (NZLC R79, 2002).

report of the Select Committee had, however, been a critical impulse for the beginning of this review within the Law Commission.

- 1.11 While the majority of the committee was prepared to recommend the Bill for a second reading, the Select Committee recorded:<sup>10</sup>

Although we agree in principle with this amendment bill we do not think it reforms the law relating to trusts extensively enough. During the course of our examination of this bill many related issues that were outside the scope of this bill were brought to our attention, ... We urge the Government to conduct a comprehensive review of the law relating to trusts as soon as practicable.

- 1.12 The Select Committee report included a list of other topics that it thought would be a desirable part of such a review:<sup>11</sup>

- the rule against perpetuities;
- the removal of trustees;
- New Zealand becoming a signatory to the Hague Convention on the Law Applicable to Trusts and on their Recognition;
- supervision of, and trust principles in relation to, superannuation trusts;
- the extent to which a settlor or trustee can contract out of trustee duties;
- the irreducible core of trustee duties;
- trading trusts;
- access to trust information by beneficiaries; and
- statutory powers to vary and resettlement a trust.

- 1.13 The National Party members of the Select Committee, then in opposition, provided a comment that expressed the need for a more comprehensive review of the Trustee Act and was stronger in its criticism of the limited scope of the Bill:<sup>12</sup>

[T]his is very poor legislation which results from an ancient Law Commission report. It misses some big issues while concentrating on a series of minor ones. The real need is to repeal the out-of-date Trustee Act 1956 and replace it with legislation which is relevant and up to date.

- 1.14 This reference was, in essence, the Government's response to the recommendation by the Select Committee that there be a wider inquiry into the law of trusts than the Commission's 2002 Report. The proposals in this Report cover the additional topics identified by the Select Committee with the exception of accession to the Hague Convention (which must wait until the charitable and purpose trusts review) and trading trusts (which will be considered further when we look at companies acting as trustees). The principal recommendation of this Report is that there be a new Trusts Act.

## CONDUCT OF THIS REVIEW

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- 1.15 The Law Commission began work on this reference in March 2009. Being conscious that the law of trusts was a potentially vast subject, the Commission sought at an early juncture to divide the project into three stages. This Report represents the culmination of the Commission's first project on trust law: looking at the Trustee Act 1956, which had been the focus of the

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<sup>10</sup> Trustee Amendment Bill 2007 (144-2) (select committee report) at 3–4.

<sup>11</sup> At 3–4.

<sup>12</sup> At 4.

- Select Committee, and trust law generally. There are two further reviews of areas of trust law to complete our full suite of work on the law of trusts. One of these, intended to deal with the charitable trusts and the Charitable Trusts Act 1957, has now been expanded to include consideration of purpose trusts (the charitable and purpose trusts review). The other was initially intended to deal with the trustee companies' legislation. However, the Commission has come to view this review as being more appropriately focused not just on the statutory trustee companies but on companies and other body corporates that act as trustees, an important subset of which are the statutory trustee companies (the corporate trustee review).<sup>13</sup>
- 1.16 As part of its work programme the Commission has issued five issues papers:
- *Introductory Issues Paper* (IP19) – primarily a background paper;<sup>14</sup>
  - *Second Issues Paper* (IP20) – covering concerns with the use of trusts (especially family trusts) in New Zealand;<sup>15</sup>
  - *Third Issues Paper* (IP22) – addressing the rule against perpetuities and the revocation and variation of trusts;<sup>16</sup>
  - *Fourth Issues Paper* (IP26) – focusing on trustees (trustee duties, the office of trustee, and trustee powers);<sup>17</sup> and
  - *Fifth Issues Paper* (IP28) – addressing remaining issues such as trading trusts, registration of trusts, court jurisdiction and obligations of trust advisers.<sup>18</sup>
- 1.17 In total we received 98 submissions on these five issues papers. Having reviewed these submissions, the Commission formulated what it termed its “preferred approach” and released the *Review of the Law of Trusts: Preferred Approach* in October 2012.<sup>19</sup> Our motivation for circulating the *Preferred Approach Paper*, before going on to issue a final Report, was to ensure our recommendations were in line with actual practice in New Zealand, as well as with the theory of trusts.
- 1.18 After the *Preferred Approach Paper* was published, the Commission undertook an extensive programme of consultation with trust practitioners around New Zealand to “road test” the proposals. We were fortunate to be assisted in this by the New Zealand Law Society, which organised meetings with their members in various centres around New Zealand. The Auckland District Law Society also arranged two meetings with its members in Auckland for us. We had meetings with special interest groups of the New Zealand Institute of Chartered Accountants in Wellington and Auckland. The Institute also organised a general consultation meeting with its members. We met also with lawyers who provide advice in relation to the trusts that have been set up as part of the Treaty settlement process with the Government. In addition to consultation with the private sector, we also consulted with various government agencies with an interest in trust law.

13 See Trustee Companies Act 1967, Trustee Companies Management Act 1975, and the Trustee Companies Management Amendment Act 1978 for the statutory arrangements applying to statutory trustee companies.

14 Law Commission *Review of Trust Law in New Zealand: Introductory Issues Paper* (NZLC IP19, 2010) [*Introductory Issues Paper*]. All Issues Papers in the review of the law of trusts are available at < [www.lawcom.govt.nz/trusts](http://www.lawcom.govt.nz/trusts) > .

15 Law Commission *Some Issues with the Law of Trusts: Review of the Law of Trusts – Second Issues Paper* (NZLC IP20, 2010) [*Second Issues Paper*].

16 Law Commission *Perpetuities and the Revocation and Variation of Trusts: Review of the Law of Trusts – Third Issues Paper* (NZLC IP22, 2011) [*Third Issues Paper*].

17 Law Commission *The Duties, Office and Powers of a Trustee: Review of the Law of Trusts – Fourth Issues Paper* (NZLC IP26, 2011) [*Fourth Issues Paper*].

18 Law Commission *Court Jurisdiction, Trading Trusts and Other Issues: Review of the Law of Trusts – Fifth Issues Paper* (NZLC IP28, 2011) [*Fifth Issues Paper*].

19 *Preferred Approach Paper*, above n 8.

- 1.19 We have received 73 submissions on the *Preferred Approach Paper*. We have been fortunate in these submissions and the submissions we have received on the original issues papers, and have given them careful consideration. In part, the strength of the submissions on the *Preferred Approach Paper* has led us to defer final recommendations on some proposals until we can fully consider the matters raised. For example, the submissions relating to companies acting as trustees have meant we have deferred final recommendations until our planned corporate trustee review.
- 1.20 In countless areas of detail, we have taken account of comments in consultation meetings and formal submissions. This Report and our recommendations are considerably improved as a result. Inevitably, we received submissions that we have not agreed with, and we have not adopted some suggestions made. Criticism of the proposals that we made in the issues papers or the *Preferred Approach Paper* has often deepened our understanding of the issues involved. Urgings to go further than we had proposed in particular areas were an invaluable check on the limits to reform that we had perceived, even if we did not ultimately agree that particular reforms were appropriate, or appropriately pursued within the scope of this Report or the proposed Trusts Act.



# Chapter 2

## Why a new Trusts Act?

### INTRODUCTION

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- 2.1 This chapter looks at why a new Trusts Act is necessary. It first argues that trust law is central to the legal infrastructure of this country. Then, by way of background, we present a summary of the different types of trust that are in use, which illustrates how widely and diversely they are used. We then present the principles behind the review and the case for a new Trusts Act, before considering the approaches taken in other jurisdictions.

### TRUST LAW AS A CORE PART OF LEGAL INFRASTRUCTURE

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- 2.2 The trust is unquestionably one of the great inventions of the common law mind, and is a central piece of the legal infrastructure of New Zealand and other jurisdictions that share a common law heritage. Trusts provide an effective way to separate the ownership of property from those who are to benefit from that ownership, and enable assets to be held collectively rather than individually.
- 2.3 Trusts form an important part of New Zealand’s economic and social life. While the exact number of trusts is unknown, and probably unknowable, we have heard throughout this review that there may be anything between 300,000 to 500,000 trusts currently in New Zealand. The uses of trusts reach from holding the family home to high finance. Trusts are an important mechanism for the holding of Māori land,<sup>20</sup> and have been extensively used by iwi as way to hold, and provide governance, for assets from the Treaty settlement process. The trust is the mechanism which the Government prefers iwi to use as “post settlement governance entities”.<sup>21</sup> This makes New Zealand heavily dependent on the trust mechanism for the holding and governing of a large amount of its wealth, and consequently trusts are an important component of the economy.
- 2.4 Similar to the Companies Act 1993, which aimed to get company law right,<sup>22</sup> and the Personal Property Securities Act 1998, which aimed to get personal securities law right,<sup>23</sup> getting the underlying infrastructure behind such an important institution in the New Zealand economy as the trust correct is a critical goal for New Zealand law. Unlike those two statutes, we do not recommend a wholesale revision of the underlying law, and in the case of the Personal Property Securities Act, the abandonment of a long legal heritage. Nonetheless, this review is as important as those were. Its aim is to ensure the law that supports trusts is as fit for purpose in 21st century New Zealand as it can be.

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20 Law Commission *Review of the Law of Trusts – Preferred Approach* (NZLC IP31, 2012) at [1.14]–[1.17].

21 Office of Treaty Settlements *Post Settlement Governance Entities: A Guide* (2012) < [www.ots.govt.nz](http://www.ots.govt.nz) > .

22 See Law Commission *Company Law: Reform and Restatement* (NZLC R9, 1989), which led to the Companies Act 1993.

23 See Law Commission *A Personal Property Securities Act for New Zealand* (NZLC R8, 1989), which led to the Personal Property Securities Act 1998.

## TYPES OF TRUSTS

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- 2.5 At points in this review we have focussed on express private trusts, and in particular family trusts, in the discussion of the issues and possible reforms to trust law. We want to make it clear that trust law applies to a variety of types of trusts and to emphasise the variety of circumstances in which trusts can be involved.
- 2.6 Private trusts benefit individuals and may be enforced by the beneficiaries. Charitable trusts aim to benefit the public by achieving a charitable purpose and are enforced by the Attorney-General.<sup>24</sup> Charitable trusts are a form of purpose trust. New Zealand law only allows limited purpose trusts other than charitable trusts, such as trusts for animals or for the maintenance of monuments.<sup>25</sup>
- 2.7 Express trusts are created deliberately as a result of a settlor's intention to create a trust. Some express trusts are intended to come into effect after the settlor's death (testamentary trusts). Testamentary trusts are nearly always created by a will.<sup>26</sup> An express trust that takes effect during a settlor's lifetime is known as an inter vivos trust. Express trusts may also be either fixed or discretionary. In a fixed trust, the trustee has no discretion about which beneficiaries will receive trust property and in what shares, while in a discretionary trust, the trustee does have these discretions. Family trusts are a form of express trust. They can be fixed or discretionary, but are commonly discretionary. They are set up by families for a range of purposes that benefit family members. Some family trusts and other express trusts are established to run a business. In these business trusts, the trust holds the shares in a company which owns the business assets. Protective trusts, which can prevent a beneficiary's interest from being lost in the event of bankruptcy, are a form of express discretionary trust.<sup>27</sup>
- 2.8 Trusts are used for a variety of commercial purposes and functions. Trading trusts are trusts in which the trust property is used to carry on business. They often have a structure that involves a company acting as a trustee, holding property on trust for certain beneficiaries, where the company has very few or no assets owned beneficially. Trusts can be used as a vehicle for managing collective investments. Trusts are used for securitisation programmes, under which a trustee is appointed to hold assets in a separate entity from the entity from which receivables assets, such as loans, originate. Trusts are used for the issuance of debt securities to the public, the syndicated bank lending to corporate borrowers, where a trustee holds security over the borrower's assets for the benefit of a number of lenders who share the security, and the issuance of covered bonds by New Zealand registered banks.<sup>28</sup>
- 2.9 Unit trusts are a form of collective investment constituted under a trust deed. Superannuation trusts are trusts for managing retirement benefits for employees. All superannuation schemes that register under the Superannuation Schemes Act 1989 must have a trust deed.<sup>29</sup> A member of a scheme is a beneficiary of the trust. Trustees are responsible for the management and

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24 Andrew S Butler "The Trust Concept, Classification and Interpretation" in Andrew S Butler (ed) *Equity and Trusts in New Zealand* (2nd ed, Thomson Reuters, Wellington, 2009) 43 at 58. Where there is a legacy to a named charitable organisation, the organisation itself can undertake proceedings to enforce it.

25 At 58.

26 At 61.

27 Law Commission *Review of Trust Law in New Zealand: Introductory Issues Paper* (NZLC IP19, 2010) at [2.73]–[2.74].

28 Information provided by Chapman Tripp in its submission on the *Preferred Approach Paper*.

29 Superannuation Schemes Act 1989, s 3. The Unit Trusts Act 1960 and the Superannuation Schemes Act 1989 would be repealed by the Financial Markets Conducts Bill 2011 (342-2) which is currently before Parliament. This Bill replaces the existing schemes for these statutory investment trusts with a new scheme that regulates matters including misleading or deceptive conduct, disclosure of information to investors, duties of persons associated with such schemes, powers of supervision, the licensing of certain financial market securities providers, and financial reporting obligations. As with the existing statutory trust schemes, where provisions of the new specific legislation conflict with trusts legislation and trust law, the specific scheme will prevail.

- investment decisions. Other sorts of employee trusts are used for holding long-term benefits for employees, such as shares or share options. These trusts enable shares or options to be held until a distribution date, held in individual packages within the trust, or held for long-term dividend income for the benefit of existing or retired employees. Employee trusts can be more flexible and have fewer administration costs and reporting obligations than superannuation trusts.
- 2.10 Energy trusts were formed after the Energy Companies Act 1992 required all municipal electricity departments and power boards to be corporatised and allowed individual communities to determine how the shares in the new energy companies were to be held. Many local communities allocated shares to a local energy trust.<sup>30</sup> Energy trusts vary considerably. Some are charitable trusts where the income of the trust, which is principally in the form of dividends from its shareholding in the electricity lines company, is used for charitable purposes. Others distribute directly to electricity consumers or members of the local community, for instance, through an annual rebate.<sup>31</sup>
- 2.11 Trusts may also be simple or special. The classification of a simple trust (bare trust) is legislatively created and so can vary from one statute to another, but there are several views of what bare trusteeship involves.<sup>32</sup> The most common view of a bare trustee is that it refers to a trustee who has no duties, or if he or she did originally have duties, the trustee can be compelled in equity by the beneficiary to convey the trust property to the beneficiary or by the beneficiary's direction.<sup>33</sup> Bare trusts are often used in the acquisition of assets where it is desirable that the legal owner's identity remains undisclosed during the acquisition process. A special trust is one where the trustee has duties.
- 2.12 Statutory trusts are created or implied by statute. Examples include trusts created under section 77 of the Administration Act 1969 for children of the deceased when he or she dies intestate or partially intestate, trusts relating to land held by local bodies for public purposes,<sup>34</sup> and community trusts established to acquire the shares in the capital of the trustee banks' successor companies for community benefits.<sup>35</sup> Trusts are created under Te Ture Whenua Maori Act 1993 (TTWMA) (discussed below).
- 2.13 Trusts are established for Treaty of Waitangi settlements and utilised by the statutes carrying out these settlements.<sup>36</sup> These trusts can have tens of thousands of beneficiaries, and have their own procedures for registration of beneficiaries and for keeping them informed. These trusts are commonly exempted from the rule against perpetuities.
- 2.14 There are also trusts that are not express trusts in that they do not require an express intention to create a trust. Resulting trusts occur when a transferor of property can be presumed not to have intended the recipient of the legal title to be the beneficial owner. As a result the recipient of the legal title must retain the property for the transferor, in the absence of any contrary intention.<sup>37</sup> Jessica Palmer places resulting trusts in two categories: "apparent gifts" which covers voluntary conveyance and purchase of property in the name of another person,

30 (7 May 1992) 524 NZPD 8349; Andrew S Butler "Trusts and Commerce" in Andrew S Butler (ed) *Equity and Trusts in New Zealand* (2nd ed, Thomson Reuters, Wellington, 2009) 1107 at 1120.

31 At 1120.

32 Butler "The Trust Concept, Classification and Interpretation", above n 24, at 58–59.

33 *Christie v Ovington* (1875) Ch D 279 at 281.

34 Butler "The Trust Concept, Classification and Interpretation", above n 24, at 59.

35 See Trustee Banks Restructuring Act 1988 (now repealed) and Community Trusts Act 1999.

36 For instance, Ngāi Tahu Claims Settlement Act 1998, Waikato-Tainui Raupatu Claims (Waikato River) Settlement Act 2010 and Ngāti Pāhauwera Treaty Claims Settlement Act 2012.

37 Jessica Palmer "Resulting Trusts" in Andrew S Butler (ed) *Equity and Trusts in New Zealand* (2nd ed, Thomson Reuters, Wellington, 2009) 307 at 308.

and “failing trusts” which covers express trusts that fail because of uncertainty and other invalidating reasons, and incomplete disposal of a beneficial interest.<sup>38</sup> Constructive trusts arise when no trust has been declared, either directly or indirectly, but it would be unconscionable for the person on whom the court imposes the trust to assert a beneficial ownership.<sup>39</sup> An institutional constructive trust arises on the happening of certain events by operation of the principles of equity. A remedial constructive trust is imposed by the court as a remedy in circumstances where previously no trust existed, and so depends on the court for its very existence.<sup>40</sup> While they are covered by the current Trustee Act, the Act’s provisions and most of the matters discussed in this review are of little relevance to resulting and constructive trusts. It seems likely that the courts will continue to develop the law in this area.

### Māori land trusts

- 2.15 Māori land trusts are unique to New Zealand and make up a significant proportion of New Zealand’s trusts. Unlike the express trusts discussed above, Māori land trusts are generally not settlor-made but are created by order of the Māori Land Court. They are primarily land management structures. They continue in perpetuity and are mostly fixed trusts.<sup>41</sup>
- 2.16 Māori land trusts have a different historical origin from other trusts. There is evidence that trusteeship of Māori land may have arisen from the cultural institution of rangatira who made decisions in relation to land and communities on behalf of the communities, which means they are more akin to implied trusts.<sup>42</sup>
- 2.17 Under Part 12 of TTWMA, the Māori Land Court has exclusive jurisdiction to constitute the following five types of Māori land trusts:
- Whānau trusts – discretionary trusts primarily aimed at enabling interest in Māori land or general land owned by Māori to be held in perpetuity under the name of a tupuna (ancestor). The beneficiaries are the descendants of the tupuna, though none have a fixed interest. The trust is intended to prevent ongoing succession to land interests and their consequential fragmentation.<sup>43</sup>
  - Ahu whenua trusts – fixed trusts that are the primary land management trusts under TTWMA. The trustees hold the land and assets on trust for the beneficial owners in proportion to their several interests.<sup>44</sup> However, the beneficial owners may still succeed to, sell or gift their interests independently of the trustees, but subject to the alienation restrictions in TTWMA.
  - Whenua topu trusts – discretionary land management trusts that operate to promote and facilitate the use and administration of land in the interests of the iwi or hapū as collectives.<sup>45</sup>

38 At 314. It can be difficult to distinguish between different types of resulting and constructive trusts, and commentators differ in their views as to whether different situations that are said to fall into these categories actually qualify as trusts. See also *Prest v Petrodel Ltd* [2013] UKSC 34.

39 Noel C Kelly, Chris Kelly and Greg Kelly *Garrow and Kelly Law of Trusts and Trustees* (6th ed, LexisNexis, Wellington, 2005) at [15.1.2].

40 *Fortex Group Ltd (in rec & liq) v MacIntosh* [1998] 3 NZLR 171 (CA) at 172–173.

41 Te Ture Whenua Maori Act 1993, s 235. Additionally some of the text in this chapter is based on information provided by the Māori Land Court in its submission on the *Fourth Issues Paper*.

42 Commentary on this is included in Waitangi Tribunal *The Orakei Claim* (Wai 9, 1987) at 5.1; Waitangi Tribunal *Rekohu – A Report on Moriori and Ngāti Mutunga Claims in the Chatham Islands* (Wai 64, 2001) at 9.7.2; Waitangi Tribunal *Mohaka ki Ahuriri Report* (Wai 201, 2004) at 6.7.6 and 12.7; Waitangi Tribunal *Hauraki Report* (Wai 686, 2006) vol 2 at 685, 697 and 698; and Waitangi Tribunal *He Maunga Rongo – Report on the Central North Island Claims* (Wai 1200, 2008) at 447 and 523.

43 Te Ture Whenua Maori Act 1993, s 214.

44 Te Ture Whenua Maori Act 1993, s 215. The Wellington Tenths Trust is an example of an Ahu Whenua trust set up over Māori reserved land.

45 Te Ture Whenua Maori Act 1993, s 216.

- Putea trusts – fixed share management trusts for managing impractical or otherwise undesirable minimal value interests, or interests where the beneficiary is unknown.<sup>46</sup>
  - Kaitiaki trusts – fixed trusts that are constituted over Māori land interests or other land or property of any persons under a disability, including minors under 20 years.<sup>47</sup>
- 2.18 The Registrar of the Māori Land Court maintains a record of the legal and beneficial ownership of Māori land.<sup>48</sup> The Court advised us that there are 9,230 whānau trusts, 5,575 ahu whenua trusts, 33 whenua topu trusts, three putea trusts, and 2,726 kaitiaki trusts. TTWMA provides much of the law regarding the constitution and administration of Māori land trusts and powers of the court in relation to these trusts. The provisions of the Trustee Act and general trust law are applicable to Māori land trusts where TTWMA is silent. The Government is currently conducting a review of TTWMA to consider legislative intervention to enable the best use of Māori land and this may result in some amendment to the TTWMA regime.<sup>49</sup>

### Foreign trusts

- 2.19 Like England, Canada and Australia, New Zealand has a long tradition of resident trusts and a taxation system that imposes tax on income from those trusts.<sup>50</sup> Since 1987 the New Zealand Government has made the policy decision to allow trusts to be settled by non-residents and administered by trustees within New Zealand without incurring New Zealand tax.<sup>51</sup> This means that New Zealand is an attractive jurisdiction for foreign individuals wishing to make investments through the use of trusts. New Zealand has traditionally been seen as an “onshore” trusts jurisdiction where the traditional plurality of trusts has been for domestic as opposed to foreign wealth.<sup>52</sup> However, in not imposing tax on foreign trusts, New Zealand has a feature in common with the “offshore” jurisdictions that have traditionally been used for the settlement of trusts by foreign investors with foreign wealth, such as jurisdictions in the Channel Islands and Caribbean. Unlike some of the offshore jurisdictions, New Zealand has retained the traditional concept of a trust without extending its bounds far outside its historical starting point and has relatively light regulation of the trust industry.<sup>53</sup> New Zealand is considered to have sophisticated levels of advice from lawyers and accountants and a judiciary that is relatively advanced in understanding trusts.<sup>54</sup>
- 2.20 Tax legislation requires the disclosure of details of foreign trusts by New Zealand resident trustees of foreign trusts. The Inland Revenue advise that since October 2006 when a registration requirement for foreign trusts was introduced there have been 7,738 foreign trust registrations.<sup>55</sup> The New Zealand resident trustee must belong to an approved organisation, such as the New Zealand Institute of Chartered Accountants, the New Zealand Law Society or the Society of Trust and Estate Practitioners (New Zealand branch). The trustee is also required to keep financial and other records relating to each foreign trust for New Zealand tax purposes

46 Te Ture Whenua Maori Act 1993, s 212.

47 Te Ture Whenua Maori Act 1993, s 217.

48 Te Ture Whenua Maori Act 1993, s 127.

49 New Zealand Government “Te Ture Whenua Maori Act Review Announced” (press release, 3 June 2012); Te Ture Whenua Maori Act 1993 Review Panel *Discussion Document* (March 2013).

50 Mark Bridges “Recent international trust cases that will have a material impact on the trust industry” (paper presented to Society of Trust and Estate Practitioners New Zealand Trust Conference, Auckland, March 2012).

51 John Prebble “The New Zealand offshore trust regime” (2012) 2 VUWLRP 28/2012 at 1.

52 Tim Hunter “NZ foreign trusts among global tax havens” (22 August 2012) < www.stuff.co.nz > .

53 Bridges, above n 50.

54 Bridges, above n 50.

55 Data as at 30 June 2012, provided by Inland Revenue (email from Graham Tubb (Inland Revenue) to Marion Clifford (Law Commission) regarding foreign trusts (10 July 2012)).

and is obliged to provide these details to the Inland Revenue if requested.<sup>56</sup> If the trustee does not comply with these requirements he or she may be subject to sanctions, such as prosecution for knowingly failing to disclose or keep the required information. In certain circumstances, the resident foreign trustee may be taxed in New Zealand on the foreign trust's worldwide income.<sup>57</sup>

## PRINCIPLES BEHIND THE REVIEW

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- 2.21 The Law Commission's approach has been guided by three core principles. The reforms should:
- be fit for the New Zealand context but consistent with overseas trust law;
  - respect individuals' right to choose how they deal with, and hold, their property; and
  - uphold the trust as a robust instrument with a core of fundamental obligations that apply in every trust.

### Fit for the New Zealand context but consistent with overseas trust law

- 2.22 We have been clear throughout our review process that the new Trusts Act must be fit for purpose in the context of 21st century New Zealand. Indeed, one of our principal intentions in releasing our *Preferred Approach Paper* was to "road test" our proposals against New Zealand practice so that we were not proposing something that would unnecessarily impinge on legitimate practice.
- 2.23 It is not enough, however, that New Zealand trust law be fit for purpose in New Zealand. In our view, it is essential that New Zealand trust law be largely consistent with overseas trust law, in particular the trust law of England and Wales, Australia, Canada and other common law countries to which New Zealand often compares its law. There would be little to be gained, and an enormous amount to be lost, by trying to invent a peculiarly New Zealand institution. There is the general point that New Zealand courts and lawyers, and through them New Zealanders and their businesses, can only gain by being part of a wider legal family. Departures from the common law norm should be examined closely before being recommended. New Zealand lawyers and their clients benefit on a daily basis from overseas learning and development in what is very much a shared common law institution. In relation to trust law, both those with domestic and foreign wealth who are considering establishing trusts in New Zealand will be sceptical of an institution that is too peculiarly New Zealand, and too different from the trusts offered by other jurisdictions.

### Respecting individuals' rights to hold and transfer property as they wish

- 2.24 One of the core values of both New Zealand society, and its legal system, is that individuals ought to be able to hold property in the ways in which they wish to hold it, subject always to other legal requirements. The trust has traditionally been, and will remain, one of the ways in which people can legitimately choose to hold their property, transfer their property to others, or set up a charity. We have taken a neutral approach to the underlying uses the trust might be put to and the advantages that might be sought through their use. Rather, the focus of this project has been getting the core institution of the trust in as good a shape as it can be, leaving regulation of the consequences of the use of trusts to more specific policy areas. In this sense our project is similar to that carried out by the Law Commission in relation to the Companies Act, the focus of which was getting the core institution of the company correct, as opposed to trying to regulate the uses to which companies might be put.

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<sup>56</sup> Prebble, above n 51, at 1–2.

<sup>57</sup> Tax Administration Act 1994, ss 3(1), 22(2)(fb) and (m), 22(2C), 22(7)(d), 59B, 61(1B), 81(4)(mb), 143(1B), 143(IC), 147(2B) and 147B.

## Upholding the trust as a robust institution with core mandatory obligations

2.25 An important corollary of respecting New Zealanders' decisions in relation to how they wish to hold or transfer property, is that notions of what is a trust, and what is not a trust, including the obligations that must be present in a trust, ought to be robust. During the consultation period we have been somewhat alarmed by general misconceptions as to what might be permissible as a "trust". Indeed, the lack of clarity among some as to what constitutes a trust has led to the courts making use of doctrines such as "sham" or "illusion" as ways of describing what purported to be a trust, but which is not, in some instances. Our new statute is designed to provide that degree of robustness. However, robustness does not only mean that there should be a commonly identified understanding as to what a trust is. It requires the law that underpins the trust to be fit for purpose to enable settlor intentions and beneficiary expectations to be given effect to by trustees, and when they cannot, the law should contain appropriate mechanisms to enable the terms of the trust to be altered.

## THE CASE FOR A NEW TRUSTS ACT

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2.26 The Commission is convinced that the Trustee Act must be replaced with a new Act. As discussed above, trusts are a core part of New Zealand's legal infrastructure. There is, therefore, a strong case for ensuring that trust law is in good working order. New legislation is needed in order to achieve this for the following reasons:

- the current Trustee Act contains inaccessible or inapplicable administrative procedures;
- many of the current Trustee Act's provisions are convoluted and out of date; and
- the law on trusts, although relevant to many people, is inaccessible.

2.27 Furthermore, as we discuss below, the reforms we recommend are in line with moves from relevant jurisdictions throughout the Commonwealth towards updating and replacing trusts legislation.

2.28 In our view it is vastly preferable that a complete new Act is introduced than that the Trustee Act is amended. We are recommending significant changes. The scope of issues that we recommend should be covered by the new Act is much broader than the current Act. Most sections of the Trustee Act would need to be totally rewritten and the structure of the Act would need to be revised.

2.29 Throughout the Report we have carefully considered how a new Trusts Act would affect existing trusts. Our changes to the administrative and mechanical provisions of the Trustee Act will be of considerable benefit to existing as well as to new trusts. We have sought throughout to develop reforms that will make the administration of trusts more straightforward. We have seen the current dependence on applications to the High Court as the sole way of remedying problems and resolving disputes as a hindrance to good trusts infrastructure. We are making several recommendations in order to build a more cost-effective, efficient, accessible framework for trusts. This includes modernised, workable processes for remedying difficulties without the resort to court, a supervisory role for the Public Trust in some of these processes, greater opportunity to use alternative dispute resolution and, where a court decision is necessary, a broader ability to have a matter resolved in the District Court and in some circumstances, the Family Court.

2.30 A new Trusts Act affords an opportunity to address problems in the law of trusts. It would enable matters that are currently uncertain or not settled to be given certainty. It would allow rectification where the current law is causing unfairness, for instance, in the areas of the

availability of the trustee's indemnity to creditors.<sup>58</sup> The new Act would correct the balance between different interests where the law has become skewed towards the interests of some parties, for instance, in relation to trustee exemption clauses.<sup>59</sup>

### Making the Act's procedures accessible and applicable

2.31 One of the important roles of the Trustee Act is to provide administrative procedures to deal with difficulties not foreseen by the trust drafter at the time of formation. Provisions of this nature currently in the Act include the ability to appoint a trustee where there are no remaining trustees, or to allow variation of the terms of a trust. These provisions are not only important for particular trusts that require help but are also central to the integrity of the institution of the trust itself, which depends on such procedures being available if necessary. It is our view, and the view of many who we have consulted, that the procedures provided in the Trustee Act are inaccessible or inapplicable in situations where accessible and applicable law is most needed. These opaque or unsuitable procedures lead to increased costs for trustees and beneficiaries through inefficient trust administration.

#### *How the new Act would address this*

2.32 Our recommendations for a new Trusts Act provide simplified procedures that enable the business of trusts with minimal expense. Our reforms are aimed at achieving this while balancing the need to preserve the overall integrity of the settlor's intentions and the rights of the beneficiaries to benefit from the trust, as established by the settlor. We intend that the new Act include processes that are useable and which will fill gaps where there is currently no straightforward way of achieving a desired end.<sup>60</sup>

### Making the Act modern and understandable

2.33 The Trustee Act is a critical piece of legislation for those who deal on a day to day basis with trusts. It is needed to address some of the difficulties created by settlors in their trust documents, and created by the courts in the way they have developed particular doctrines over centuries. For such an important statute, it is convoluted and needs simplification. Not only are some provisions hard to understand, in some cases they are simply unreadable.<sup>61</sup> The Trustee Act sets defaults that are designed to aid drafters of trust documents and it allows trustees to be relieved from the consequences of breaches in appropriate cases.<sup>62</sup> Perhaps even more importantly, the default settings which it establishes for the law of trusts in such areas as the description of trustees powers, do not line up with how trusts are actually administered in practice, but rather reflect much older notions of the way things ought to be done, often without modern justification.

2.34 Similarly, the Act does not deal with some of the more problematic default settings developed in case law, such as the allocation of receipts or expenses to the historic categories of income or capital, requiring trust deed drafters to remove the difficulties created by old cases.<sup>63</sup>

2.35 Thus, drafters not only need to customise the trust with the settlor's particular arrangements, but also set out basic and common understandings of trusts. In addition, drafters have to exclude

58 See ch 16.

59 See ch 5.

60 For example, some recommendations in this Report that aim to make the statutory procedure more accessible and applicable include the appointment of agents and delegates in ch 6, the appointment and discharge of trustees in ch 8, the variation and revocation of trusts in ch 10 and the review of actions of trustees in ch 11.

61 Peter Blanchard "Towards a modern law of trusts" (paper presented to New Zealand Law Society Trusts Conference, 2001).

62 Trustee Act 1956, s 73. See for example *Church Property Trustees v Attorney-General* [2013] NZHC 678, [2013] 2 NZLR 428.

63 See ch 7.



the operation of doctrines that almost everyone concludes should no longer be part of our law, and essentially write in doctrines that almost everyone considers ought to be part of the underlying law. Our view is that a new Trusts Act ought to do this for all trusts.

*How the new Act would address this*

- 2.36 The recommendations in this Report minimise or avoid the inefficiencies resulting from the problematic and outdated default settings. We propose that the new Trusts Act contain defaults that are in line with modern trust law conventions, including modern deed drafting. This would simplify and streamline the process of drafting trust deeds and reduce the complexity of trust documents. The recommended provisions reflect modern ways of doing business and managing personal affairs. A complete new Act would be drafted in plain English, refer to modern concepts and would be structured in a logical, easy-to-follow manner.
- 2.37 It is vital that New Zealand trust law adequately represent the expectations of those entering into trust arrangements. It is also essential that the default provisions trust deed drafters include in such arrangements reflect modern realities and expectations rather than legal doctrines whose relevance, importance and justification has long since passed, and which are themselves poorly understood.<sup>64</sup>

**Making trust law accessible**

- 2.38 It is commonly observed that the use of trusts in New Zealand has vastly expanded over the last few decades.<sup>65</sup> Large numbers of people find themselves as trustees or beneficiaries of trusts, or contemplate becoming settlors. This includes many who are not legally trained. There appears to be confusion amongst many of those trustees as to their appropriate role or duties as trustees, and amongst beneficiaries as to what they can and cannot expect of trustees. There is also confusion amongst those who are settling trusts as to what the effect of those settlements are. This has led to a general community misunderstanding as to the nature of the trust. There appears to be, for instance, a decrease in understanding that the trustee holds property on behalf of the beneficiaries, and is bound by important duties to respect the trust obligations and to act on behalf of the beneficiaries.
- 2.39 The current inaccessibility of key parts of trust law and the resultant lack of understanding about trusts can lead to further problems. If settlors and trustees are confused or unclear as to the nature and effect of settling a trust, and their obligations, there is a greater risk of trusts being improperly administered. This can increase the likelihood of disputes and litigation between settlors, trustees, and beneficiaries.

*How the new Act would address this*

- 2.40 The new Act would aim to remove some of the mystery of trust law by setting out basic principles in the Act. The new Act would draw together key parts of trust law that are presently only accessible in case law. Including the core characteristics of the trust and the duties of trustees would strengthen the common understanding of the institution of the trust and provide guidance to individual trustees who need to understand, without reference to large tomes or compendia of cases, what their basic obligations as trustees are. The clarification the new Act would provide as to the nature of trusts, the duties of a trustee, and processes for revocation and variation, should provide more certainty and minimise the potential for disputes and litigation

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64 For instance, some recommendations in this Report that aim to make the new Act modern and understandable include the administrative powers, powers of maintenance and advancement and power to appoint nominees and custodians in ch 6, the apportionment of receipts and expenses in ch 7 and the powers of the court in ch 12.

65 See Law Commission *Some Issues with the Law of Trusts: Review of the Law of Trusts – Second Issues Paper* (NZLC IP20, 2010).

on these matters. It would also help to maintain public confidence in the institution of the trust. The new Act would be a much more complete source of the law applying to trusts than is the current Trustee Act.

- 2.41 In making these recommendations we are aligned with developments in a number of other areas. The Companies Act in 1993 included a code of directors' duties to make clear to directors what their obligations might be.<sup>66</sup> This articulation of duties has also been a feature of recent finance sector legislation.<sup>67</sup> In the recent Report on the Incorporated Societies Act 1908, the Law Commission identifies that one of the significant difficulties facing incorporated societies and their members is the lack of awareness of the obligations that might be associated with being on a committee. A key aim of the reform recommended in that Report was to bring home to those many members what those obligations might be.<sup>68</sup> We understand from documents prepared in relation to the current review of Te Ture Whenua Maori Act (the Act governing the holding of Māori land), that trustees in that area also do not understand the obligations that being a trustee impose upon them. There is desire as part of that review to make these obligations clearer.<sup>69</sup>

## APPROACH IN OTHER JURISDICTIONS

- 2.42 A number of comparable common law jurisdictions have recently reviewed and updated their trust legislation, in light of the archaic nature of much of the existing legislation, changing social and business contexts, and the importance of trusts for asset management within those countries' economies.<sup>70</sup> All of these are driving forces behind our review as well. Our review also shares many common purposes and themes with these overseas reforms, in particular: providing a clearer and more modern trusts statute; facilitating effective and efficient trust administration; supplying relevant and useful statutory defaults; reducing or removing outdated limits on trustees' powers; and focusing on the obligations and liabilities of trustees.
- 2.43 Below we highlight some key areas where our recommendations are aligned with these overseas approaches. The approach taken in this review is that trust law should reflect the unique features of the New Zealand trust context. However, because New Zealand is a small nation with relatively limited trusts jurisprudence, it is important for New Zealand law not to move too far out of line with internationally accepted trust law principles. Departure from the law in comparable jurisdictions should occur only where it is justifiable based on the New Zealand context, and then only with caution. Accordingly, in general the recommendations are consistent with recent reforms and accepted approaches in comparable common law jurisdictions, particularly England and Wales, Scotland, Ireland, Canada and Hong Kong.<sup>71</sup>
- 2.44 There are certain areas in which our recommendations have gone slightly further than or departed from the positions of some jurisdictions, such as in setting out in statute the range of trustees' duties and characteristics of an express trust, and in retaining a maximum duration period for trusts. However, these instances are rare and either do not alter the substantive law or offer only incremental changes that are appropriate for New Zealand trust law.

66 Companies Act 1993, s 131–138.

67 See for instance the Financial Advisors Act 2008 and the Financial Markets Conduct Bill 2011 (342-2).

68 Law Commission *A New Act for Incorporated Societies* (NZLC R129, 2013).

69 Te Ture Whenua Maori Act 1993 Review Panel, above n 49, at 26–31.

70 See for example Hong Kong Financial Services and the Treasury Bureau *Detailed Legislative Proposals on Trust Law Reform* (March 2012) at [1.6]–[1.10].

71 The United States has also been moving towards modernising trust law and including more content in statute. The Uniform Trust Code is being widely enacted, see John H Langbein "Why did trust law become statute law in the United States?" (2007) 58 Ala L Rev 1069. In Australia, the Queensland Law Reform Commission is conducting a review of the Trustee Act 1973 (Qld).

- 2.45 England and Wales brought in the Trustee Act 2000 which implemented the changes recommended by the Law Commission of England and Wales, along with the Scottish Law Commission, regarding trustees' duties, powers and delegation.<sup>72</sup> Following this Act there have been further changes in areas such as trustee exemption clauses,<sup>73</sup> classification and apportionment of capital and income,<sup>74</sup> and perpetuities and accumulations.<sup>75</sup> Our expression of the trustee's duty of care is based on the wording of the Trustee Act 2000.<sup>76</sup> We have also adopted a number of other approaches from the United Kingdom legislation, including the requirement for trustees to prepare a policy statement for delegation of investment powers,<sup>77</sup> and the recommendation for a rule of practice requiring disclosure and explanation of exemption clauses in trust deeds.<sup>78</sup> Like England and Wales, we have also recommended reform of the rule against perpetuities, rather than wholesale abolition, as we have recommended a maximum duration period for trusts.<sup>79</sup>
- 2.46 Scotland's Law Commission is currently conducting a wide-ranging review and modernisation of trust law. It has completed eight discussion papers, two consultation papers, and a report, covering areas such as the nature and constitution of trusts, trustees and trust administration, variation and termination, and apportionment of receipts and outgoings. It is working on a report covering the majority of the topics on which it has consulted, along with a draft Trusts (Scotland) Bill to replace the existing legislation.<sup>80</sup> The Irish Law Reform Commission has also been reviewing the law of trusts, and produced a report on general proposals along with a draft Trustee Bill in 2008.<sup>81</sup> The Bill is to be included as a Trusts Bill as part of the Government Legislation Programme Summer Season 2013.<sup>82</sup>
- 2.47 The Uniform Law Conference of Canada resolved in 2012<sup>83</sup> to adopt and recommend for enactment a Uniform Trustee Act,<sup>84</sup> based on the 2004 Report of the British Columbia Law Institute.<sup>85</sup> The purpose of the proposed Uniform Trustee Act is:<sup>86</sup>

... to provide a modernized statute that addresses as comprehensively as is practicable the administration of trusts, including the appointment and removal of trustees, the vesting of trust property, the duties and powers of trustees, trustee remuneration and accounts, and the variation, termination and resettlement of trusts.

The Report on the proposed Uniform Trustee Act notes that it is not a code, but rather is “enabling and supplementary to the general, and largely non-statutory, law of trusts”, and

72 Law Commission (England and Wales) and Scottish Law Commission *Trustees' Powers and Duties* (Law Com No 260 Scot Law Com No 172, 1999).

73 Law Commission (England and Wales) *Trustee Exemption Clauses* (Law Com No 301, 2006).

74 Law Commission (England and Wales) *Capital and Income in Trusts: Classification and Apportionment* (Law Com No 315, 2009); Trusts (Capital and Income) Act 2013, which received Royal Assent on 31 January 2013.

75 Law Commission (England and Wales) *The Rules against Perpetuities and Excessive Accumulations* (Law Com No 251, 1998); Perpetuities and Accumulations Act 2009, which received Royal Assent on 12 November 2009.

76 See R13.

77 See R17.

78 See R4.

79 See R49.

80 See Scottish Law Commission “Trusts” (11 April 2013) < [www.scotlawcom.gov.uk/law-reform-projects/trusts/](http://www.scotlawcom.gov.uk/law-reform-projects/trusts/) > .

81 See Ireland Law Reform Commission *Trust Law: General Proposals* (LRC92, December 2008) and Draft Trustee Bill 2008.

82 See Ireland Law Reform Commission “Table of Implementation” (2013) < [www.lawreform.ie/publications/table-of-implementation-of-law-reform-commission-recommendations.171.html](http://www.lawreform.ie/publications/table-of-implementation-of-law-reform-commission-recommendations.171.html) > .

83 “Civil Section Resolutions” (Uniform Law Conference of Canada, Whitehorse YK, August 2012), accessible at < [www.ulcc.ca](http://www.ulcc.ca) > .

84 “Uniform Trustee Act” (Uniform Law Conference of Canada, Whitehorse YK, August 2012), accessible at < [www.ulcc.ca](http://www.ulcc.ca) > [*Uniform Trustee Act of Uniform Law Conference of Canada*].

85 Committee on the Modernization of the Trustee Act *A Modern Trustee Act for British Columbia* (BCLI R33, October 2004).

86 “Uniform Trustee Act – Final Report of the Working Group” (Uniform Law Conference of Canada, Whitehorse YK, August 2012) at [12], accessible at < [www.ulcc.ca](http://www.ulcc.ca) > .

retains a default character, “[e]xcept for certain provisions which are essential to the operation of trusts and expressly stated to prevail over a conflicting term of a trust instrument”.<sup>87</sup>

- 2.48 Likewise, our recommended reforms are largely default in nature, aside from those provisions which are considered to be essential to the operation of trusts and therefore should be mandatory elements. The significant reforms provided for in the Uniform Trustee Act are very similar to those recommended here, including: providing that the powers of a trustee are equivalent to those of an individual with full legal capacity;<sup>88</sup> giving statutory form to the trustee’s good faith duty of care, with professional trustees held to a higher standard;<sup>89</sup> obligations for reporting and provision of information to beneficiaries;<sup>90</sup> giving trustees discretion regarding apportionment of receipts and outgoings between income and capital;<sup>91</sup> permitting delegation of administrative powers;<sup>92</sup> permitting variation without court approval if all beneficiaries of full capacity consent;<sup>93</sup> providing default processes for appointment and removal of trustees;<sup>94</sup> and addressing the effect of exemption and indemnity clauses.<sup>95</sup>
- 2.49 There are some areas where the Uniform Trustee Act differs from our recommended reforms, such as by abolishing the rule against perpetuities without introducing a limit to the duration of trusts,<sup>96</sup> and permitting trustees to be compensated and to act by majority as default provisions.<sup>97</sup> We have differed from that approach to perpetuities on a principled policy basis.<sup>98</sup> Remuneration of trustees and majority trustee decision-making are available where permitted by the trust deed or by another statute (or where permitted by the court in the case of remuneration).
- 2.50 Hong Kong this year introduced the Trust Law (Amendment) Bill 2013, which is currently through its second reading before the Legislative Council. This Bill also contains a great deal of common ground with the reforms recommended in this Report, including imposing a statutory duty of care,<sup>99</sup> and limits on exemption clauses including those covering gross negligence.<sup>100</sup>
- 2.51 Overall, the recommendations in this Report are in keeping with current developments and established approaches to the law regarding trusts and trustees in similar jurisdictions. It is essential that New Zealand remain in line with the international trend towards more modern and comprehensive trust legislation.

87 At [13].

88 *Uniform Trustee Act of Uniform Law Conference of Canada*, above n 84, at cl 24; compare with R7.

89 At cl 26; compare with R13.

90 At cls 28–29; compare with R6.

91 At cls 37–40; compare with R16. Although our reforms go further, because of the predominance of discretionary trusts, and give trustees a similar discretion when distributing. The Canadian proposed Act instead uses the percentage trust model as its default, but allows for the discretionary approach we recommend where the trust deed permits this.

92 At cl 47; compare with R12.

93 At cl 59; compare with R29.

94 At pt 2; compare with R20–R23.

95 At cls 81–82; compare with R4.

96 At cl 88; compare with R49.

97 At cls 64 and 53; compare with R3 respectively.

98 See ch 17.

99 Trust Law (Amendment) Bill 2013, cl 3A; compare with R13.

100 Trust Law (Amendment) Bill 2013, cl 41W; compare with R4.

# Chapter 3

## The new Trusts Act

### INTRODUCTION

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- 3.1 Chapter 3 explores the nature of key aspects of the Law Commission’s package of recommendations. It looks at the proposal that there be a new Trusts Act, and addresses the concern that this is an attempt at codification. The chapter discusses the way that the recommendations address the nature of trusts, and then explores how the recommended new Act interacts with the rules of equity, and addresses issues over the validity of trusts. The chapter also considers the importance of the settlor’s intention and the balance that we have attempted to strike in relation to this in the recommendations. Finally, chapter 3 discusses how the proposed Act would interact with particular types of existing statutory trusts, which rely upon the trust form, and how the recommendations apply more generally to existing trusts.

### THE PROPOSAL FOR A NEW TRUSTS ACT

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- 3.2 We are proposing a Trusts Act that is not simply an updated, revised and reformulated Trustee Act 1956, although such updating or reformulation is keenly needed. Rather, we are proposing an enlarged statute that, in addition to covering the matters currently dealt with in the Trustee Act, will cover such matters as the duties of trustees and the circumstances in which liability for such duties can be avoided. We have set out a more comprehensive characterisation of what a trust is and recommend expressly confirming that the courts ought to have the power, as they now have, to declare that what purports to be a trust is in fact not a trust.
- 3.3 Once enacted, the new Trusts Act will therefore include important matters that are not covered by the current Trustee Act. However, it is not our intention, in recommending the enactment of a new Trusts Act, to create a code which completely supplants the common law, principles of equity, or the creative role of judges.

### The “codification” critique

- 3.4 In general our proposals have been well received. Submitters and consultees have provided comments and suggestions on most of the particular proposals, and we have taken these into account in formulating this Report. Some of the more critical comments have related to our proposal to set out in statute the characteristics of an express trust, and the mandatory and default duties of trustees. Some of the criticism has related to matters of detail, and we have tried to incorporate responses to that criticism within the recommendations we have made. Other criticism has been focused on the general wisdom of providing a definition of trust or explication of duties at all. This criticism is concerned that something would be lost in the translation of general equitable principles into statutory form, and that what we are proposing will stultify and freeze notions of the trust and trustees’ duties.

#### *Response to the “codification” criticism*

- 3.5 The Commission, however, is determined that the new Trusts Act should contain both the characteristics of an express trust and duties, both mandatory and default, that are owed by trustees. There would be, in our view, real costs in not taking the opportunity provided by

a new Trusts Act to set out basic matters that all settlors, trustees and beneficiaries ought to know. Indeed, it is the very popularity of the trust in New Zealand, and the democratic nature of its use, that have led us to this conclusion. Trusts in New Zealand are not settled or administered by only a learned few, but by many New Zealanders, who are entitled to know what legal obligations they owe and are owed, and what their rights are. Moreover, we firmly believe that the main threat to the institution of the trust comes not from the articulation of the characteristics of express trusts or of duties, but from the general lack of appreciation of what those characteristics and duties are.

- 3.6 We have been somewhat reassured about our position through discussions of our proposals with our reference group and through consultation meetings. Initial concern has often dissipated into a degree of acceptance, and the reflection that these general provisions are of real value. We are providing indicative drafting of the first part of the proposed Act to show how we believe that the necessary balance of certainty and flexibility in the provisions can be maintained.
- 3.7 Some of the criticism that has been directed at the articulation of the characteristics of the express trust, or of the duties, is not dissimilar to the criticisms that common lawyers make of codification exercises in general.<sup>101</sup> There is always the fear that statutory interpretation will replace legal reasoning, or settled, if flexible, legal principle. In the end, such criticism misunderstands what we have attempted to do, and the likely way that we would expect lawyers and judges to respond to the new provisions. Rather than being words intended to stand completely on their own, the characteristics of the trust and the duties will be read against that history of flexibility and principle that has given rise to them. Moreover, we are not proposing a code. Courts will continue to have flexibility to deal with situations that do not fit neatly within the terms of the new statute. As we explain below, there is likely to be a complex relationship between the existing law and the statute that we have proposed. We do not intend to create a code to be interpreted simply on its own terms without reference to the judge-made law, as the Commission did in relation to the law of evidence (leading to the enactment of the Evidence Act 2006).<sup>102</sup>
- 3.8 In any event, there are important limitations both on how the new Trusts Act will operate and in its scope. The articulation of the characteristics of the trust, and the articulation of trustees' duties, will make the Trusts Act the primary source of trust law in New Zealand, but it will not contain everything that conceivably needs to be known about the law of trusts. For example, we have taken the view that little would be gained, and much would be complicated, by the attempt to articulate remedies that might flow from the finding that there is no express trust, or the finding that a trustee's obligation has been breached. Equity in this area has, in our view, developed a sophistication that will be extremely difficult for a statute to match.

## THE NEW TRUSTS ACT AND THE NATURE OF TRUSTS

### The new Trusts Act in the context of debate on the nature of trusts

- 3.9 There has been much recent debate both amongst practitioners in courts and amongst academics as to the nature of the trust and how to conceptualise the place of trusts within the general scheme of English, Commonwealth and United States private law.<sup>103</sup> There have been, for example, very active debates over the nature of the interest that beneficiaries have in their

101 See, for instance, Jack Beatson "The Role of Statute in the Development of Common Law Doctrine" (2001) 117 LQR 247; Reinhardt Zimmermann "Statuta sunt Stricte Interpretanda? Statutes and the Common Law: a continental perspective" (1997) 56 Cambridge LJ 315; Catherine Skinner "Codification and the Common Law" (2009) 11 Eur JL Reform 225.

102 Law Commission *Evidence Code and Commentary* (NZLC R55, 1999).

103 See discussion in James Edelman "Two Fundamental questions for the Law of Trusts" (2013) 129 LQR 66.

trusts, and whether it is appropriately described in terms of a property interest, or whether the interest is better described as obligations that are owed to beneficiaries by trustees.<sup>104</sup>

- 3.10 While we have tried to take account of these more theoretical debates where they impact on the practical reforms we suggest are implemented, in some senses it is unnecessary to completely resolve those debates in our legislation. Indeed, some of those theoretical debates are probably not capable of final resolution. For instance, we suspect that the current debate over the degree to which a trust confers a property interest on beneficiaries will not be conclusively resolved either in favour of the property interest or the partially competing obligations theory. Rather, the tension between those two conceptions of the trust will continue to be worked through in particular circumstances where the difference may have real world consequences. We have not endorsed one particular theory of what a trust is, but we have tried to articulate what we believe is the fair consensus. In the rare circumstances where there are debates at the edges of that consensus, we have left the resolution of those debates to the courts. For example, our proposed statement of the characteristics of a trust does not commit New Zealand to a particular theory of whether the trust confers a property interest or an interest arising from obligations.

### **The importance of the restricted definition**

- 3.11 While we are recommending a provision that sets out the characteristics of an express trust, that definition will be for the purposes of the new Act.<sup>105</sup> The new Trusts Act will not preclude arguments that arrangements falling outside the definition of an express trust for the purpose of the new Trusts Act are nevertheless trusts. The courts will continue to have the flexibility to recognise arrangements that do not fit within these characteristics as trusts. One of the criticisms of our proposals referred to trusts used in a commercial or banking and finance context that may have partially departed from what we have articulated as being the core elements of the trust. The concern is that these trusts would be considered invalid under the new Act.<sup>106</sup> We anticipate, of course, that recognition of these as trusts would first require an explanation as to why, in the absence of the characteristics specified for an express trust under the new Act, a trust nevertheless exists.
- 3.12 We are confident that recognition by the courts of an arrangement as a trust, despite not fitting within the new Act's characteristics of a trust, will occur only in very rare cases. Rather than preventing the courts from recognising trusts outside this Act, our definition of an express trust will act as a "gatekeeper" for access to the provisions of the Trusts Act. The advantages of falling within the scope of the Trusts Act will be considerable. Those "trusts" that fall outside the Trusts Act will have to negotiate the many difficulties that the Trusts Act resolves, without the benefit of that Act, and the various Trustee Acts that have preceded it.

### **Act not to include constructive or resulting trusts**

- 3.13 The current Trustee Act applies to express trusts, "implied trusts", and constructive trusts. While we intend the new Trusts Act to apply to express trusts, we recommend that it not apply to constructive or resulting trusts. During the course of our considerations, we have debated whether the statute should expressly cover resulting and constructive trusts, which arise by operation of law. On the one hand making such trusts subject to the statute would have the advantage of comprehensiveness. However, while some of our proposals might be clearly applicable or useful in relation to resulting or constructive trustees, it was also clear to us that

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104 Edelman, above n 103.

105 See cl 3 of Appendix A.

106 Helen Dervan "Trustee Indemnity and Trustee Liability" (paper presented to New Zealand Law Society Trust Conference, June 2013) at 241-260.

some aspects of what we are proposing might apply only with difficulty. Indeed, some of the duties that we have formulated with express trusts in mind might have to be altered or excluded in relation to some resulting or constructive trustees. The reality will be that in many resulting or constructive trust cases there is little desire for trustees to hold property for any particular length of time, and that most of the provisions of the Act will simply not be relevant.

- 3.14 While it would have been possible to create a schedule to the statute which expressly modified or made inapplicable particular provisions that did not apply to constructive or resulting trusts, it seemed to us that the sounder approach was to leave them out of the coverage of the statute. Our expectation is that judges, when recognising resulting trusts or imposing constructive trusts, will make use of the relevant provisions in appropriate cases.

## THE NEW TRUSTS ACT AND EQUITY

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- 3.15 The new Trusts Act should give its readers the greatest possible opportunity to understand and apply the rules that it recognises and creates. However, we do not intend for many of the provisions we are proposing for the Trusts Act to represent a new dawn, in the sense that prior case law, learning or doctrine will be irrelevant to the interpretation of the wording of the statute. Just as judges have made use of prior case law in interpreting the code of duties owed by directors in the Companies Act 1993,<sup>107</sup> we would expect the same of those involved in advising trustees and settlors and those involved in litigating aspects of trust law. Ultimately judges must decide whether trust law ought to make reference to pre-existing case law, learning and doctrine. We are not arguing for a wholesale displacement of the common law in the way that the Commission recommended in 1999 that the common law of evidence should be displaced.<sup>108</sup> By setting out the characteristics of trusts and duties of trustees as we have, we are seeking to make them somewhat less mysterious to New Zealanders, but also to preserve the magic that lay behind their development.

### The interaction with existing equitable principles

- 3.16 A more complex question that has been addressed in our issues papers, and also in submissions and discussion with our reference group, is the appropriate relationship between the new Trusts Act and the case law on which it is unquestionably based. While a true code might be said to be “exclusive” in the sense that there is no need to go behind the words that the drafter has used in articulating a code, the reality is that this is not our intention in relation to the Trusts Act.
- 3.17 Our proposed Trusts Act is not intended to supplant the law of equity. As we have explained above, it is not intended as a code that makes earlier cases and commentary irrelevant or of historic or academic interest only. We envisage that the inherent and supervisory jurisdiction of the courts will continue as it does now. Thus, where the statute does not directly cover matters, including matters that are not foreseen by this statute or where we have recommended they are best left to the courts, such as remedies for breach of trust, courts will continue to recognise obligations, and give appropriate remedies. For this reason we have included amongst our draft the following interpretation provision:<sup>109</sup>

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107 *Company Law* (online looseleaf ed, Brookers) at [CA131.01]. In *Benton v Priore* [2003] 1 NZLR 564 at [46], Heath J commented that the duties provisions “should be seen as a restatement of basic duties in an endeavour to promote accessibility to the law”. In *Sojourner v Robb* [2006] 3 NZLR 808 at [100], Fogarty J stated: “A statute such as this does not supplant the common law when it enacts a common law standard which is of its character a principle rather than a rule. As a principle it has to be applied in a wide variety of circumstances and such application is appropriately guided by the common law cases which led to the articulation of the principle in the first place.”

108 *Evidence Code and Commentary*, above n 102. This is discussed also in Law Commission *The 2013 Review of the Evidence Act 2006* (NZLC R127, 2013) at ch 2.

109 See cl 1(2) of Appendix A.



Nothing in this Act prevents a court, in interpreting the provisions of this Act, from having recourse to the general law of trusts and equity where that law is consistent with this Act.

- 3.18 There is no one relationship between the pre-existing law, or equitable principles that might govern the administration of trusts, and our recommendations.
- 3.19 In some instances, the principal examples being the characteristics of express trusts and the articulation of mandatory and default duties, we have endeavoured to essentially incorporate traditional notions of what case law currently requires. The current case law and related commentary will continue to be of primary importance. During consultation, one of the recurring criticisms of our proposal to set out the definition or the duties in statutory language, was that this will somehow fix those duties and meanings, prevent development and focus attention on the words used rather than the principles they represent. This is not our intention and it misperceives the process that courts, lawyers and other readers will take when interpreting the legislation. The proper approach will be to read the words of the statute in light of the understanding of the equitable principles that gave rise to them. We have chosen the wording with care and that wording has been road tested through our consultation, but the focus should not be on interpreting them in isolation, abstracted from their context.
- 3.20 A second way that some recommendations interact with existing case law is to use it as a reference, but to arguably modify the nature and scope of the existing obligations in accordance with our policy decisions. In relation to these provisions, the underlying case law will be important to understand, but will need to be read in light of the way in which the new statute gives effect to the different policy. Our recommendation in relation to the provision of information by trustees, serves as an example. Our recommendation is clearly based in the obligation of trustees as recognised by the Privy Council in *Schmidt v Rosewood*,<sup>110</sup> to provide sufficient information to sufficient beneficiaries. Arguably, our recommendation extends it by requiring the proactive release of certain information to some beneficiaries and by recognising a default presumption that information should be provided to all beneficiaries.
- 3.21 In a third type of provision, we have referred to existing case law but have suggested that it ought to be replaced. In relation to these provisions, the primary focus ought to be the statute, rather than pre-existing case law or statutory provisions. In this category we might put provisions such as the abolition of the law against perpetuities or the abolition of the current rules relating to the categorisation of particular receipts or expenses as capital or income. In the case of these provisions, the old law would remain of historic interest or a way of understanding the mischief which the new provisions are intended to deal with.
- 3.22 In order to aid those who might seek to interpret provisions in the new statute, we have included a consolidated chart of those provisions that fall into each of these three categories at the end of this chapter (see table A). Another table sets out the way in which our other recommendations that currently have a statutory rather than case law character interact with existing statute law (see table B).

## THE NEW TRUSTS ACT AND THE VALIDITY OF TRUSTS

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### The provisions

- 3.23 Our recommendation is that the new Trusts Act should contain a provision that sets out the characteristics of an express trust,<sup>111</sup> as well as providing that all express trusts must

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<sup>110</sup> *Schmidt v Rosewood Trust Ltd* [2003] UKPC 26, 2 AC 709.

<sup>111</sup> See R1.

recognise mandatory duties owed by the trustees. We have provided indicative drafts of these provisions.<sup>112</sup> We have also recommended that there be a provision confirming courts will be able to declare a trust as not having satisfied the characteristics of an express trust. We also provide that nothing in the new statute will preclude the invalidity of an express trust on other grounds. We have suggested the following drafting for that provision:

#### **6 No express trust except under section 5**

- (1) A trust, if it is to be an express trust, must be created in accordance with section 5.
- (2) Nothing in subsection (1) precludes the invalidity of an express trust on any other ground recognised at law.

3.24 However, in a separate recommendation, the effect of excluding a mandatory duty in a trust within the definition of the Act will be that the exclusion is negated, rather than there being no express trust as such.<sup>113</sup> We have made this recommendation to avoid courts having to find, in the face of a clear intention for a trust, that there is not an express trust for the purpose of the Act.

#### **Issues arising out of the interrelationship of these provisions**

3.25 A number of issues follow from these recommendations. First, the degree to which the ability to declare something is not an express trust will interface with current case law relating to “sham” trusts or “illusory” trusts, or to the inherent jurisdiction of the court simply not to recognise the existence of a valid trust. Second, there is a question as to what the effects of a declaration that a particular arrangement is not an express trust will be. Third, there is the issue as to what effect our recommendation that terms of trust cannot exclude the mandatory duties will have on trust deeds that purport to exclude those mandatory duties.

#### *Relationship of the new Act to “sham” or “illusory” doctrines or “no trust” finding*

3.26 It is not possible to say that the law relating to sham trusts or illusory trusts is a particularly settled part of New Zealand or overseas jurisprudence.<sup>114</sup> The phrase “illusory trust” has only been part of the New Zealand discourse since *Clayton v Clayton* in February 2013, which at the time of writing this Report is subject to appeal.<sup>115</sup> Some might argue that while parties and courts have resorted to the language of sham or illusion, the proper approach ought to have always been the consideration of whether there had in fact been a proper trust in the first place. The use of “sham” or “illusory” trust might represent something less than the application of a new doctrine, but rather explain why the courts might have found that a trust existed or did not exist.<sup>116</sup>

112 See cls 9 and 10 of Appendix A.

113 See R2.

114 See the discussion in Thomas Gibbons “Alter Ego trusts” [2007] NZLJ 316; Jessica Palmer “Dealing with the Emerging Popularity of Sham Trusts” [2007] NZ L Rev 81; Jessica Palmer [2008] NZLJ 319 discussing the decision of *Official Assignee v Wilson* [2007] NZCA 122, [2008] 3 NZLR 45; Ross Holmes “All a Sham” [1999] NZLJ 262; Matthew Colaglen “Sham Trusts” (2008) 67 Cambridge L Rev 176.

115 *Clayton v Clayton* [2013] NZHC 301.

116 *Clayton v Clayton*, above n 115. This case was in the context of considering whether the transfer of what would otherwise have been matrimonial property to a husband’s companies was a facade or a sham. See the observations of Lord Sumption in *Prest v Petrodel Ltd* [2013] UKSC 34 at [28]:

The difficulty is to identify what is a relevant wrongdoing. References to a “facade” or “sham” beg too many questions to provide a satisfactory answer. It seems to me that two distinct principles lie behind these protean terms, and that much confusion has been caused by failing to distinguish between them. They can conveniently be called the concealment principle and the evasion principle. The concealment principle is legally banal and does not involve piercing the corporate veil at all. It is that the interposition of a company or perhaps several companies so as to conceal the identity of the real actors will not deter the courts from identifying them, assuming that their identity is legally relevant. In these cases the court is not disregarding the “facade”, but only looking behind it to discover the facts which the corporate structure is concealing. The evasion principle is different. It is that the court may disregard the corporate veil if there is a legal right against the person in control of it which exists independently of the company’s involvement, and a company is interposed so that the separate legal personality of the company will defeat the right or frustrate its enforcement. Many cases will fall into both categories, but in some circumstances the difference between them may be critical.

3.27 Nothing in our recommendations is intended to stand in the way of such a process. It is part of the role of courts to determine whether there is a valid trust and what the effect of that valid trust ultimately is. The effect of a determination under our proposed statute that there is no express trust will essentially be to remove the purported trust from the operation of the new Trusts Act. The courts would still have the ability to determine that there was some other kind of trust or that a trust-like relationship was established. Generally, we think such a determination would be unlikely. The failure to satisfy the essential characteristics of a trust and the three certainties of intention, property and objects in the statute would also fail to satisfy what most would consider to be the requirements for establishing a trust. However, legal developments in particular areas may lead to the variation of some of those elements in particular circumstances, and we think it is important to leave open the opportunity for such developments.

#### *Express trusts that exclude mandatory duties*

3.28 The more difficult question, however, is what the effect will be of requiring courts to read into deficient trust documents the mandatory obligations that we have specified. The case of *Clayton v Clayton* presents an example. That case concerned a series of trusts, the validity of which were challenged in relationship property proceedings. Rodney Hansen J found that in relation to one of the trusts in dispute, the way in which the trustee who was also the settlor and a beneficiary might exercise discretion without reference to the interest of the beneficiaries was so inconsistent with the normal obligations of a trustee that a trust had not been established. This was despite the intention to create a trust.<sup>117</sup>

3.29 Disputes like *Clayton* will unquestionably remain an important pressure point in the law of trusts in New Zealand. Although we make no judgement about the particular facts of *Clayton* itself, the question arises from the result or the reasoning by which the result was reached, as to how this particular kind of dispute might be reasoned under the new Trusts Act. The approach under our recommended statute would be to first start with the provision that confirms the courts' ability to declare that a purported trust not to be an express trust within the meaning of the new Act. Under our new statute, once those core characteristics have been satisfied, the question then becomes one of whether the terms of the trust have purported to exclude one of the mandatory duties that is otherwise provided for in the Trusts Act. If it has purported to exclude such a duty then the provision that we have recommended would have the effect of rendering that exclusion void and would essentially read those duties into the trust deed. It is possible that what might have otherwise been held to be a sham or illusory trust for having purported to have excluded a key mandatory duty will be saved in essence by the voiding of the otherwise offensive clause.

3.30 However, that would not be a necessary result of our new Trusts Act. We would expect a court faced with such a contention to look at whether the existence of such an exclusion in the terms of the trust went directly to the intention of the parties to create a trust in the first place. In many cases the express exclusion of the mandatory duties will indeed indicate lack of intention to create a trust, and hence there will not be a trust. We have taken the view in this Report that it should not be a necessary consequence of the exclusion of one of the core mandatory duties that there was in fact no intention to create a trust. There may well remain cases where it can be appropriately held that there was an overriding intention to create a trust relationship despite poor wording or misapprehension as to what must be contained in a valid express trust deed. Such a determination would necessarily be particularly fact specific, as indeed it is under the current law.

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117 *Clayton v Clayton*, above n 115, at [90].

## THE IMPORTANCE OF THE SETTLOR'S INTENTION

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- 3.31 During the consultation process we often heard the view that since a trust is created by a settlor with property that had previously been the settlor's, priority ought to be given to the settlor's intentions. There have always been active debates over how best to give effect to a settlor's intention once a trust has been formed, even if those wishes subsequently prove to be foolish, nonsensical or against widely accepted public policy, and in some cases against the very nature of the trust itself.<sup>118</sup> Some settlors will always try to keep a degree of control or influence that is compatible with the existence of a trust; others will seek to give discretion to trustees, or seek to immunise their failures in ways that are compatible with the trustees' duties. Debates over what settlors can appropriately control cannot be resolved completely, and this Report does not seek to do that. These debates are fought over at a theoretical level in law journals, and also play out in the very practical advice that solicitors, and other advisers, give to settlors establishing trusts. During our consultation process, the issue of the appropriate place for settlor control featured in our consultation on very practical issues, such as the amount of information that ought to be provided to beneficiaries, and which beneficiaries ought to be provided with that information.<sup>119</sup>
- 3.32 The view that settlors can set up their trusts under whatever conditions they choose is sometimes referred to in literature as "contractarian". The contractarian assumption being that because at the root of the trust is a contractual obligation between the settlor and trustees in terms of how the trustees deal with the property, a settlor ought to be able to impose whatever conditions in that contract the settlor wishes to impose. In the academic literature, the contractarian model of the trust is often associated with John Langbein of Yale University who has written a number of important and influential articles.<sup>120</sup> The law ought to respect the ability to give away property absolutely, or the ability to enter into contracts with others about how those others might use the property. However, the law should also take seriously the proposition that when establishing a trust, the settlor intends something different from a simple gift or the simple establishment of a contractual relationship with the trustee in relation to the property.
- 3.33 We have approached this final Report from the principle that people are entitled to hold and dispose of their property in the way in which they wish, including by settling it on a trust. It is this that informs not only our sense of what ought to be done in the preliminary provisions of a new Trusts Act (setting out the characteristics of express trusts and the duties owed by trustees) but also in the more administrative and mechanical parts of that Act. Both types of provisions, in our view, ought to reflect the central tenet of trust law that, above all, courts ought to strive to give effect to the intentions behind the trust. But it cannot be that settlors can simply choose from a laundry list of benefits that they seek, without also having to take the essential elements of the trust that confer those benefits.
- 3.34 It is for this reason that we have insisted in this Report that there be an articulation of the duties that cannot be waived by a settlor ("mandatory duties"). If the settlor can waive those duties, particularly the duty of good faith, then it is not clear to us how the settlor is intending to create a trust. A far more likely interpretation of such an arrangement is that the settlor was simply intending some kind of gift where the supposed trustee holds the property absolutely for the trustee's own benefit, but perhaps constrained by contractual restriction. Indeed, one way of understanding the rather confusing, and confused New Zealand case law, which considers

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118 See for instance Tusan Hang Tey "Settlor's Reserved Powers" (2009) 23 *Trust Law International* 183, reviewing the ways in which settlors might seek to preserve influence over the conduct of a trust from an international perspective.

119 In an article he published in response to our *Preferred Approach Paper*, Peter Watts suggested that our proposals could be criticised as interfering too much with the importance of settlor intentions (Peter Watts "Yet more expansion of the role of Courts in private lives" *NZ Lawyer* (New Zealand, 25 January 2009)).

120 For example, John Langbein "The Contractarian Basis of the Law of Trusts" (1995) 105 *Yale LJ* 625.

“sham”, “illusory” or “alter ego” trusts, is the sense that just because the word “trust” is used in relation to a particular kind of conveyance or contract does not mean a trust has been created.

- 3.35 This Report is written to be consistent with the proposition of the law giving effect to the settlor’s intention to create a trust, within the common understandings of what a trust is. Moreover, we have attempted to be clear in the statute, in a way that case law and textbooks are sometimes not, as to which duties can be modified or excluded by the settlor when creating the trust. The express recognition of such duties as being “default” is very much intended to emphasise the legitimate role that settlors have in making decisions about how the trust will operate in the future. Similarly our proposals in relation to the variation and revocation of trusts reflect already well understood principles, such as the rule in *Saunders v Vautier*.<sup>121</sup>
- 3.36 Interestingly, Langbein makes a similar point in a number of his more recent articles, that there must be some things settlors cannot provide for in their trust deeds because they would interfere with the role that they are establishing for their trustees to hold property for the benefit of the beneficiaries. Judges and legislators have always been alive to the difficulties created by too much settlor control in terms of how a trust is administered, especially when dealing with the “dead hand” problem where constraints that may have made sense to the settlor at the time the trust was settled no longer make particular sense going into the future. For example, a clause in a trust document that says a Rembrandt painting is to be destroyed by the trustees should not be enforceable because it conflicts with the prime obligation that the trustee holds that property for the beneficiaries. If one is to take the trust model seriously there needs to be some limits at the margins as to what settlors can prescribe or excuse.<sup>122</sup>
- 3.37 An area where we have been conscious of the need to balance the importance of the settlor’s intention with the concern not to allow the “dead hand” of the settlor to have too much enduring control is in relation to the rule against perpetuities. Our approach is to allow newly created trusts to endure for up to 150 years, which extends the potential reach of the settlor’s influence. We have taken care in formulating the approach to existing trusts not to allow the settlor’s intention with regard to the duration of the trust to be too easily ousted, so the duration of existing trusts will only be able to be extended to 150 years in limited circumstances.
- 3.38 Three particular sets of proposals have been raised during consultation as potentially transgressing the primacy of settlor intention. First, those relating to the provision of information to beneficiaries where the settlor may not wish to give information to those beneficiaries.<sup>123</sup> Second, those relating to the review of a trustee’s discretion.<sup>124</sup> Third, those that would prevent settlors from excusing trustees from gross negligence (we used the term “recklessness” in the *Preferred Approach Paper*).<sup>125</sup>
- 3.39 In relation to the provision of information we are still of the firm view that any definition of the trust requires that beneficiaries be able to enforce that trust.<sup>126</sup> To do that, beneficiaries need access to information. However, we have been mindful of those submissions that state that a settlor might be wary of such requirements and may have good reasons why particular beneficiaries are not to receive either general or particular information. For instance, we have often heard of settlors’ concerns that the revelation of the existence of a trust might

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121 *Saunders v Vautier* (1841) Cr & Ph 240, [1841] 41 ER 482. Where courts are asked to use more exceptional powers to vary a trust, the focus will remain on the original design of the trust and the intentions which can be gleaned from the trust’s deed.

122 JH Langbein “Burn the Rembrandt? Trust Law’s Limits on the Settlor’s Power to Direct Investment” (2010) 90 BUL Rev 375.

123 See R6.

124 See R32.

125 See R4.

126 See ch 5.

set a particular beneficiary on the wrong track in life or that some settlors may recognise a particular beneficiary for private reasons that would disrupt families or other relationships if they were revealed. At the same time, there are less convincing reasons for refusing to provide beneficiaries with information, which we do not think should be taken into account. We have taken these concerns about our original proposals seriously and have modified the recommendation regarding the obligation to provide information. While maintaining the prime obligation of trustees to provide sufficient information to sufficient beneficiaries to enable the trust to be properly enforced, modification will be allowed so that trustees can take account of a broad range of factors, including settlor intention, when deciding to reveal particular information to certain beneficiaries, or indeed provide any information to some beneficiaries.

- 3.40 In relation to the review of the exercise of trustee discretion, we have continued with our proposed redrawing of the current section 68 of the Trustee Act, but have sought to emphasise that review ought not to enable courts to substitute their views for those of trustees. Under our proposed new section, review of the exercise of trustee discretion should continue only to occur where the trustee has made a decision that no reasonable trustee could make.
- 3.41 We have continued with our proposal that a settlor should not be able to immunise trustees from liability for deliberate breaches of trust, as such clauses strike at the very nature of the trust itself (something recognised in current case law). We have also recommended that settlors not be able to immunise trustees against liability for gross negligence.<sup>127</sup> However, in deference to those concerned about settlor intentions, we have changed the recommendations so that settlors would be able to exclude liability for a merely negligent breach of a mandatory duty.

### RELATIONSHIP OF THE TRUSTS ACT WITH OTHER STATUTORY TRUSTS

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- 3.42 The new Trusts Act goes further than the current Act by recommending the statutory restatement of the characteristics of a trust and the duties of trustees, aspects of trust law that have previously only existed in case law. The case law status of these characteristics and duties has made it clear that where there are specific standards and features of trusts in particular statutory schemes that differ from general trust law, the specific scheme overrides the general trust law. When the characteristics and duties will have a statutory status under the new Act, it will be important to ensure that the interrelationship between the new Trusts Act and other statutory schemes involving trusts continues to be clear.
- 3.43 Our general principle is that the general trust law presented in the new Act will act as a baseline of the obligations that apply wherever the express trust form is used, but that specific legislation or case law can establish a context-specific approach to particular duties, obligations or procedures. There are several ways that the interaction between a new Trusts Act and other statutory schemes may play out:
- (a) Other statutes involving trusts may set out higher or more specific obligations for trustees or an alternate procedure. There is nothing in our recommendations that will prevent this.
  - (b) The default duties and default positions included in the new Trusts Act may be overridden by alternative approaches in other statutory schemes. In relation to the duties of trustees, this means that while the mandatory duties will apply to every express trust created under any statute, if the trust is to be considered a trust for the purposes of the Trusts Act, the default duties may not apply.

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<sup>127</sup> See R4 and ch 5.

- (c) The trust deeds or trust orders of particular types of trusts may also depart from the default duties and default positions, in the same way that any trust deed of an express trust may differ from the default positions in the new Trusts Act.
- (d) Because of the different policy contexts of the trusts established under other statutes, specific statutory regimes may address matters covered in the new Trusts Act in an alternative way. The particular policy contexts may justify departures from the general law of trusts. Statutory schemes are likely to set up alternative approaches to the retention and disclosure of information to beneficiaries and the appointment and removal of trustees if, for example, there are large numbers of beneficiaries and a democratic process for the appointment of trustees.

3.44 We discuss the two main areas where it is particularly important to note and understand this interaction because of their widespread use: trusts under the Financial Markets Conduct legislation; and Māori land and Treaty settlement trusts. There may be other types of trust where the interaction is similarly important.

### Financial Markets Conduct legislation

3.45 The trust form is used in a variety of circumstances, including commercial and financial investment contexts. The basic point of difference between commercial and non-commercial trusts is that in non-commercial trusts, the assets are usually bestowed gratuitously by the settlor, while in commercial trusts, the assets are held in trust as part of a contractual transaction for the purpose of meeting the contractual objectives.<sup>128</sup> As a point of principle:<sup>129</sup>

[T]he use of rules developed in the context of gratuitous trusts may need to be carefully considered for “fit”. At the same time, however, it should be recalled that often the motivation for use of the trust structure is precisely to obtain the benefit of the efficiency of certain trust rules and principles and the flexibility to split ownership and management – accordingly the use of trusts in a commercial context is often a vote of confidence in those rules.

3.46 One of the reasons identified for using the trust form is the management standards that apply with trustees being bound to act prudently, preserve trust property and act impartially between beneficiaries: “[t]his approach can be attractive for investment vehicles such as unit trusts, superannuation trusts and so on”.<sup>130</sup>

3.47 These types of trust have their foundation in general trust law. However, additional layers of regulation apply through tailored forms of trust deed (invoking contract law), and through the operation of the financial markets legislation. This consists of statutes such as the Securities Act 1978, the Units Trusts Act 1960, the Superannuation Schemes Act 1989 and the KiwiSaver Act 2006. At the time of writing, however, this legislation is subject to major reform under the Financial Markets Conduct Bill. Under the Bill, debt securities, KiwiSaver and retirement schemes must be governed by a trust deed, while other forms of managed investment scheme have the option of adopting a trust form or other legal form such as a partnership or corporate form.

3.48 The Financial Markets Conduct Bill contains provisions that mirror, overlap and in some cases extend the obligations and regulation of those acting in the position of a trustee, for the protection of investors. There are particular supervisor or manager duties that are mandatory. The standard of care imposed is to exercise the degree of care, diligence and skill that a prudent

128 Andrew S Butler “Trusts and Commerce” in Andrew S Butler (ed) *Equity and Trusts in New Zealand* (2nd ed, Thomson Reuters, Wellington, 2009) 1105 at [39.2.1].

129 At [39.2.1].

130 At [39.2.2].

person engaged in the business of acting as a licensed supervisor or professional manager would exercise. There are limits on clauses in governing documents such as trust deeds that exempt or indemnify supervisors and managers. In some respects these are more restrictive than the provisions we recommend for the general trust law context. There are particular limits on the delegation of functions, the contracting out of management functions and the appointment of investment managers that are also stricter in certain respects than our recommendations.

- 3.49 In general, the specific regulation of the financial markets legislation will take precedence over trust law. However, because these provisions do not completely overlap with general trust law, trust law will remain the back-stop for those financial instruments structured as trusts. It will therefore be necessary for specialist trustees to analyse both layers of regulation and their interaction to appreciate the complete regulatory environment.

### Māori land and Treaty settlement trusts

#### *Te Ture Whenua Maori Act 1993*

- 3.50 Te Ture Whenua Maori Act 1993 (TTWMA) provides a specific statutory regime for land owned by Māori, including land held in Māori land trusts. Māori land trusts are generally not created by settlors, but by order of the Māori Land Court. The orders are based on standard Court precedents which tend to be relatively prescriptive.<sup>131</sup> The Court also appoints the responsible trustees for all trusts constituted under Part 12 of TTWMA.
- 3.51 There are a number of provisions under TTWMA that differ from the proposed new Act and general trust law. The Act grants the Court the power to authorise trustees in most types of Māori land trust to apply money for Māori community purposes in general, which means it can be used for purposes beyond the immediate beneficiaries.<sup>132</sup> Trustees of Māori land trusts are, subject to any limitations in a trust order, already given broad powers in a way that is framed differently to the powers of a natural person provision in our recommendations (such powers as “may be necessary for the effective management of the trust and the achievement of its purposes”).<sup>133</sup> The Act requires the Court to make provisions as to the keeping of accounts in trust orders where it considers it necessary or desirable,<sup>134</sup> which means that an alternative to the information retention provisions we recommend for the new Trusts Act will apply. Trustees of Māori land trusts may act by majority as a default position,<sup>135</sup> which is the opposite approach to the one we have taken in this Report. TTWMA includes provisions regarding the use of advisory trustees and custodian trustees in this context, with the key differences being that only the Court may appoint such trustees and that any individual or body corporate may be appointed as a custodian trustee.<sup>136</sup> It also includes provisions on variation and termination of a trust that are expressed more broadly and simply than those under general trusts legislation.<sup>137</sup> The rule against perpetuities does not apply to Māori land trusts (and we recommend the new maximum duration rule ought not to apply also).<sup>138</sup>

131 Submission of Māori Land Court on the *Fourth Issues Paper* at [5.5].

132 Te Ture Whenua Maori Act 1993, s 218.

133 Te Ture Whenua Maori Act 1993, s 226(2).

134 Te Ture Whenua Maori Act 1993, s 230.

135 Te Ture Whenua Maori Act 1993, s 227.

136 Te Ture Whenua Maori Act 1993, ss 224 and 225.

137 Te Ture Whenua Maori Act 1993, ss 241 and 244.

138 Te Ture Whenua Maori Act 1993, s 235.



## Māori Land Court

- 3.52 In addition to its jurisdiction over the Court-made trusts under TTWMA, the Māori Land Court has jurisdiction over any inter vivos express or implied trust over Māori land or General land owned by Māori and in respect of testamentary trusts over Māori land and General land owned by Māori.<sup>139</sup> The Court has the same powers and authorities as the High Court, including its inherent jurisdiction, in relation to trusts, except as expressly provided in TTWMA.<sup>140</sup> The Court first applies the relevant part of TTWMA and, by way of a backstop, relies upon the jurisdiction of the High Court and general trust law. The Māori Land Court's powers in relation to Māori land trusts have been described as “the most extensive supervisory powers” by the Court of Appeal.<sup>141</sup> When the Māori Land Court exercises its discretionary powers, such as the power to vary or terminate trusts, it does so having regard to the Preamble, general interpretation section (section 2) and general objectives (section 17) in TTWMA.<sup>142</sup>
- 3.53 The scheme of TTWMA means that trustees in this context have obligations to the beneficiaries to administer the trust property in accordance with general trust law, the requirements of the Trustee Act and the provisions of TTWMA. In the recent case of *Rameka v Hall*, the Court of Appeal has said that these “trustees are subject to traditional trustee duties with the statutory overlay of particular obligations arising from the context of [Māori land trusts].”<sup>143</sup> The Court of Appeal noted that the duties of trustees in TTWMA are not exhaustive and that general trustee law principles were relevant, before endorsing the settled approach of the Māori Appellate Court to assess the standard trust law duties together with “the broader approach having regard to the special nature of Maori land trusts and the provisions of [TTWMA].”<sup>144</sup>
- 3.54 The deference shown to the special context of Māori land trusts is also evident in decisions relating to the removal of trustees for the failure “to carry out the duties of a trustee satisfactorily”.<sup>145</sup> In *Ellis v Faulkner – Poripori Farm A Block*, the Māori Land Court recognised that powers under TTWMA are to be exercised “in a manner that facilitates and promotes the retention, use, development and control of Māori land as taonga tuku iho by Maori owners, their whanau, their hapū, and their descendants.”<sup>146</sup> In *Hart* the Court stated:<sup>147</sup>
- Given the special nature of a Māori land trust, the Court may take into consideration the views of the owners and the nature of the trust in judging whether there has been satisfactory performance.
- 3.55 Within its particular context, there are unique legal, policy and cultural issues which the Māori Land Court must balance. For instance, a common issue is the perceived tension between resident beneficial owners and absentee beneficial owners.<sup>148</sup> The Court's extensive powers reflect the multiplicity of interests of owners, beneficial owners and beneficiaries and the need for effective ways for these groups to be able to progress issues of land management, ownership, improvement and use.<sup>149</sup> Aspects of general trust law, including the duties of trustees, also reflect cultural values. The Court is able to give appropriate weight to the purpose and context of

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139 Te Ture Whenua Maori Act 1993, ss 111 and 236.

140 Te Ture Whenua Maori Act 1993, s 237.

141 *Proprietors of Mangakino Township v Māori Land Court* CA65/99 [1999] BCL 726; 22 TCL 24/9; Māori LR Jul 1999 2 at [27].

142 Submission of Māori Land Court on the *Fourth Issues Paper* at [4.15].

143 *Rameka v Hall* [2013] NZCA 203 at [19].

144 At [30] citing *Apatu v Trustees of Owahaoko C Trust – Owahaoko C1 and C2* (2010) Māori Appellate Court MB 34 (2010 AP 34) at [14].

145 Te Ture Whenua Maori Act 1993, s 240.

146 *Ellis v Faulkner – Poripori Farm A Block* (1996) 57 Tauranga MB 7(57 T 7) at 7.

147 *Hart – Okoha section 5 block VIII Gore SD* (2012) 12 TWP 286 at [28]. See also *Clark v Trustees of Poukawa 9G and others Trust* (2011) 6 Takitimu MB 285 at [15].

148 Submission of Māori Land Court on the *Fourth Issues Paper* at [5.10].

149 At [5.11].

TTWMA, which adds a distinct “flavour” to how the general trust law is applied. We expect this to continue when there is a new Trusts Act. It is our intention that the new Trusts Act proposed in this Report will not alter the Court’s current jurisdiction in relation to trusts, and would continue to apply general trust law in a way that reflects this particular context, just as the other courts will look to the context of the particular trusts. In order to ensure the Court’s role is preserved we are recommending the inclusion of the following wording:

Nothing in this Act shall detract from or affect any provision of Te Ture Whenua Maori Act 1993 and the jurisdiction of the Māori Land Court over trusts created under that Act.

### *Treaty settlement trusts*

- 3.56 Trusts are also commonly used as the mechanism for holding and managing property following a Treaty settlement, and are in fact one of the only types of “post settlement governance entities” currently accepted. These trusts are established by deed, but the settlements are enabled by legislation. Many of the settlement Acts disapply the rule against perpetuities and the Perpetuities Act 1964, and we are recommending that the maximum duration rule that will replace those also not apply to these settlement trusts. In other respects, these trusts reflect traditional trust law principles and much of the new Act will be applicable to them.
- 3.57 Because these trusts have large numbers of beneficiaries, however, there are some aspects of the new Trusts Act that will not apply because their trust deeds will include an alternative process that is more applicable to the context. For instance, in relation to the provision of information to beneficiaries, the general disclosure of information obligation will apply, while the more specific presumptions may not apply because of the terms of the trust deeds. These deeds normally involve significant information being made available to registered beneficiaries. The Office of Treaty Settlement’s post-settlement governance entity template trust deed includes a registration process through which individuals can apply for membership.<sup>150</sup>
- 3.58 We intend that, as with Māori land trusts, the courts and those involved in the administration of the trusts will continue to be able to apply general trust law to Treaty settlement trusts in a manner that acknowledges and incorporates cultural values and the particular purpose of these types of trusts. We do not intend that the new Trusts Act would cut across this.

## **APPLICATION TO EXISTING TRUSTS**

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- 3.59 New legislation when enacted applies from the date it comes into force. However, consideration must also be given to how it should apply to things done and arrangements made before that date. The general principle or presumption long recognised by the common law and more recently captured in section 7 of the Interpretation Act 1999 is that legislation does not operate retrospectively. However, the presumption against retrospective effect will be overridden where a statute is clearly intended, because of express or implicit wording, to have some retrospective application.
- 3.60 The line between prospective and retrospective is not one that can always be sharply drawn. There are many statutes enacted that are on their face prospective because they apply only to future events. However, they can have an effect on expectations formed before their enactment, so are retrospective in that sense. Retrospective effect of this type is sometimes unavoidable.<sup>151</sup> It is also not inherently objectionable because it is so dependent on the nature of the arrangements

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<sup>150</sup> Office of Treaty Settlements *Deed of Trust Template* (2012) < [www.ots.govt.nz](http://www.ots.govt.nz) > .

<sup>151</sup> JF Burrows and RI Carter *Statute Law in New Zealand* (4th ed, LexisNexis, Wellington, 2009 at 601).

that are made for dealing with those expectations.<sup>152</sup> Problems around this type of retrospectivity are best addressed directly by including transitional provisions in the statute. Transitional provisions deal with how circumstances that arose prior to enactment are affected by the new legislation coming into force.<sup>153</sup> The enactment of a new Trusts Act raises this type of issue in respect of trusts established prior to enactment.

- 3.61 We have approached the important matter of transition from the starting point that there ought to be one law of trusts in New Zealand, not a pre-Trusts Act law and a post-Trusts Act law. Trustees and beneficiaries should be able to determine easily what obligations they are under, or what obligations they are owed, and that would be made too complex if that law depended for too long on the date of the existing trust deed.
- 3.62 In fact, many of the provisions of the proposed Trusts Act do not change the obligations owed, but as we have explained, merely provide explications of the existing law. We see little reason why those explications should not commence with the statute. At the other end of the scale, the more administrative and mechanical provisions that we recommend are designed to be of use for existing trusts as much as future trusts. There seems to us every reason that, except where there are legal proceedings currently on foot, the new law in such areas should advantage all trusts.
- 3.63 However, there are sets of provisions for which we think a transitional period is desirable. When obligations change there ought to be sufficient opportunity for those involved to be able to adapt to the changed obligations. Examples of these provisions might include the expanded obligation of trustees to provide information, which may require trustees to change their administrative practices, or the inability of trustees to rely on an exemption clause that purports to exclude liability, which may require some trustees to consider their own insurance or even whether they wish to continue to be trustees.
- 3.64 Transitional provisions are also required where we are recommending changes to the default powers of trustees, which will give trustees all of the powers of natural persons. This may require trust deeds to be revised to restrict those, now broad, powers when those broader powers would not be appropriate. In one case, that of the allocation of receipts or expenses either to, or against, the categories of capital or income, we are recommending that while the statutory flexibility (which is subject to the duties of the trustees) ought to override constraints in existing trust deeds, constraints might be imposed in future trust deeds.
- 3.65 Although we have indicated the appropriate transitional arrangements in the text as we considered each recommendation, we have also set out a table of recommendations and the suggested transitions for the sake of convenience at the end of this chapter (see table C).

## TABLES

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- 3.66 Table A shows those of our recommendations that are based on existing case law, rather than statute law, and classifies them according to the way in which we intend they will interact with the existing case law.

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152 At 588. In essence retrospective legislation is only inherently objectionable if it takes away existing rights or defences, makes unlawful things that were lawful when they were done, or attaches a tax or other liability to something done in the past.

153 At 601.

**Table A: Interaction of recommendations with case law**

<b>Restate case law principles in statute</b>	
<b>R number</b>	<b>Description of recommendation</b>
R1	Characteristics and creation of a trust
R2	Mandatory duties of a trustee
R3	Default duties of a trustee
R5	Retention of information by trustees
R13	Standard of care for trustees
R24	Power to appoint and remove a trustee
R29	Variation and revocation by beneficiaries
R46	Appointment of a receiver for a trust
R47	Trustees' right to indemnity
<b>Modification to case law in new Act, but case law will remain relevant</b>	
<b>R number</b>	<b>Description of recommendation</b>
R4	Trustees' exemption and indemnity clauses
R6	Provision of information to beneficiaries
R42	Alternative dispute resolution
<b>Significant modification to case law in new Act and current case law will no longer be relevant</b>	
<b>R number</b>	<b>Description of recommendation</b>
R15	Distinction between capital and income
R16	Apportionment of receipts and outgoings
R48	Creditors' claim through trustee's indemnity
R49	Maximum duration of trusts

3.67 Table B shows the recommendations that are based on or adapted from provisions of the current Trustee Act, and classifies them according to the extent that they adapt the existing statutory provisions.

<b>Table B: Interaction of recommendations with statute law</b>	
<b>Modernise and/or clarify existing statutory provision</b>	
<b>R number</b>	<b>Description of recommendation</b>
R14	Investment powers and duties
R18	Acceptance and rejection of trusteeship
R25	Number of trustees
R27	Custodian trustees
R28	Advisory trustees (special trust advisers)
R31	Extension of trustees' powers by the court
R33	Applying for directions of the court
R34	Payment of a commission to a trustee
R35	Beneficiary indemnifying trustee for a breach of trust
R36	Barring of claims
R37	Payments to the Crown
R38	Distribution of shares of missing beneficiaries
R39	Protection against creditors by means of advertising
R44	Application for audit of accounts
<b>Modification of existing statutory provision in new Act</b>	
<b>R number</b>	<b>Description of recommendation</b>
R7	Powers of a natural person
R8	Powers of maintenance and advancement
R9	Age of majority
R10	Power to appoint agents
R12	Power to delegate
R20	Grounds for removal of a trustee
R21	Who may remove a trustee and appoint a replacement
R22	Replacing a trustee who has died
R23	Replacing a trustee who retires
R26	Transfer of trust property
R30	Revocation and variation by the courts
R32	Reviewing decisions of trustees
R40	High Court and District Court jurisdiction
R41	Family Court jurisdiction
R43	Public Trust
<b>Brand new statutory provisions</b>	
<b>R number</b>	<b>Description of recommendation</b>
R11	Power to appoint nominees and custodians
R17	Investment managers
R19	Who may be a trustee

3.68 Table C sets out and categorises the transitional arrangements for each of the recommendations for provisions in the new Trusts Act.

<b>Table C: Transitional arrangements for new Trusts Act for each recommendation</b>		
<b>General rule – Reform applies to existing trusts from the date of enactment</b>		
Applies to all recommendations, other than those included below.		
<b>Reform applies to existing trusts from date of enactment (as with the general rule), but with specific modifications</b>		
<b>R number</b>	<b>Description of recommendation</b>	<b>Description of modification</b>
R12	Power to delegate	New requirements do not apply to existing delegations
R15	Distinction between capital and income for investment purposes	Mandatory for existing trusts; default for new trusts
R16	Apportionment of receipts and outgoings	Mandatory for existing trusts; default for new trusts
R17	Investment managers	Subject to trust terms prohibiting this
R29	Revocation and variation by beneficiaries	With transitional arrangements for proceedings commenced under current variation provisions
R30	Revocation and variation by court	With transitional arrangements for proceedings commenced under current variation provisions
R31	Extension of trustees' powers	With transitional arrangements for proceedings commenced under current variation provisions
R32	Reviewing decisions of trustees	Only to actions or omissions that occur after the new Act in force
R33	Applying to court for directions	With transitional arrangements for proceedings commenced under current provisions
R34	Payment to trustee	With transitional arrangements for proceedings commenced under current provisions
R35	Beneficiary indemnifying trustee	With transitional arrangements for actions by trustees already taken under current provisions
R36	Barring claims	With transitional arrangements for proceedings commenced under current provisions
R37	Payments to the Crown	With transitional arrangements for actions by trustees already taken under current provisions
R38	Advertising for missing beneficiaries	With transitional arrangements for actions by trustees already taken under current provisions
R39	Advertising for creditors	With transitional arrangements for actions by trustees already taken under current provisions
R48	Creditors' claim through trustee's indemnity	Only to transactions entered into after commencement of new Act
R49	Maximum duration of trusts	Applies to all trusts but vesting/termination dates in existing trust deeds will continue to apply
<b>Reform applies to existing trusts after transitional period (2 years)</b>		
<b>R number</b>	<b>Description of recommendation</b>	
R4(1)(a)–(b)	Exemption and indemnity clauses	
R6	Provision of information to beneficiaries	
R7	Administrative powers	
R8	Powers of maintenance and advancement	
<b>Reform does not apply to existing trusts or trust terms</b>		
<b>R number</b>	<b>Description of recommendation</b>	
R4(1)(c)–(d) and (2)	Informing settlor regarding exemption clauses	

**Part 2**  
**CORE TRUST**  
**CONCEPTS IN THE**  
**NEW ACT**



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# Chapter 4

## Characteristics and creation of a trust

### INTRODUCTION

- 4.1 We recommend including sections in the new Trusts Act that outline what a trust is and how a trust is created to provide general guidance on the nature of the trust relationship. The intention of such provisions would not be to override the traditional understanding of a trust based on case law, but to summarise in one place the key features of a trust. It is important that people settling trusts and interacting with trusts understand the trust relationship. The introduction of definition and creation provisions are discussed more extensively in the *Preferred Approach Paper*<sup>154</sup> and the *Introductory Issues Paper*.<sup>155</sup>

### MEANING OF A TRUST

#### RECOMMENDATION

- R1 The new Trusts Act should:
- (1) Provide that the new Act applies only to express trusts, but that the court may apply sections of the Act where appropriate to resulting trusts and constructive trusts.
  - (2) Provide that the characteristics of an express trust are:
    - (a) it is a legal relationship in which the trustee holds or deals with trust property on behalf of another person or persons (the beneficiaries) or for a purpose permitted at law;
    - (b) the trustee is bound by a fiduciary duty to deal with the trust property for the benefit of the beneficiaries or for the purposes of the trust;
    - (c) any beneficiary, or the Attorney-General in the case of a charitable trust, may enforce the trustee's duties against the trustee;
    - (d) the beneficiaries have equitable rights in or in respect of the trust property; and
    - (e) a trust must not have the sole trustee as the sole beneficiary of the trust.
  - (3) Provide that an express trust may be created:
    - (a) by the settlor by words or actions doing the following (collectively known as "the three certainties"):
      - identifying the beneficiaries, or permitted purpose; and
      - identifying the trust property; or
      - indicating an intention to create a trust;

154 Law Commission *Review of the Law of Trusts – Preferred Approach* (NZLC IP31, 2012) at ch 2.

155 Law Commission *Review of Trust Law in New Zealand: Introductory Issues Paper* (NZLC IP19, 2010) at ch 3.



- (b) if a statute provides for the creation of an express trust, in accordance with that statute.
- (4) Define the terms trustee, beneficiary, discretionary beneficiary, settlor and trust property for the purposes of the Act.
- (5) Provide that a trust must satisfy all of the three certainties ((3)(a)) or be created under a statute ((3)(b)) if it is to be an express trust.
- (6) Provide that nothing in the new Act affects any provision of Te Ture Whenua Maori Act 1993 or the jurisdiction of the Māori Land Court over trusts created under that Act.

### The New Zealand context

- 4.2 Trusts are in widespread use in New Zealand and many people with no legal training are involved in trusts as settlors, trustees and beneficiaries. The trust concept is complex, involving relationships that create obligations. The definition of a trust is not readily accessible to many New Zealanders. The Trustee Act 1956 is a collection of administrative and procedural provisions and powers that presumes a certain sort of relationship is in existence. There is no authoritative statement of how that relationship is established or the roles of the parties involved.
- 4.3 We consider that it would be beneficial to include details of the core features of a trust in new legislation because the details would have a significant educative impact on those involved in trusts who do not have legal training. It would also make the legislation clearer on its face because it would explain the type of relationship that is regulated by the Act.

### Objective of the recommendation

- 4.4 The recommendation is that the new Trusts Act include a list of characteristics of a trust and how a trust may be created. These must be present for the Act to apply. This makes it a definition for the purposes of the new Act, rather than a general definition of a trust for all purposes. We have framed the recommendation and indicative draft provisions in a way that covers nearly every type of trust that is used. The provisions do not prevent the use of trusts or trust-like forms that differ from some of the characteristics and that fall outside of the new Act, if these are accepted as valid by the courts. The provisions will be useful as a clear description of the nature and effect of trusts and the way they are created.
- 4.5 The recommendation reforms the existing law by taking core features of a trust from case law and outlining these in statute. It has been argued that the current case law understanding of a trust has the advantage of flexibility.<sup>156</sup> However, there are core, mandatory requirements for a trust to exist. We think it is better to draw these out in statute rather than leave them hidden. Within the bounds of these core characteristics there will continue to be room for different trust structures and purposes, because the nature of the recommended provision is general and inclusive, rather than detailed and prescriptive. We see the benefits of the definition as making it clear to a broader group of people what a trust is and what it does, and conversely providing a clear pathway for finding that something is not a trust.
- 4.6 We recommend a provision, like that in draft clause 1(2) below, that makes it clear the courts can have recourse to the general law of trusts and equity in applying these provisions. Our

<sup>156</sup> Helen Dervan “Trustee indemnity and trustee liability” (paper presented to Continuing Legal Education, New Zealand Law Society Conference “Trusts – best practice in 2013”, Wellington, June 2013).

intention is that these provisions are not a codification of the law as to what a trust is, but a statutory statement that summarises and is filled out by the existing and developing body of equitable case law.

- 4.7 We received mixed views from submitters on whether definition provisions should be included in new legislation. While a number of submitters were supportive of the proposal, others questioned the need for a definition. There has been concern the definition and creation provisions could have the unintentional effect of altering the law or excluding some relationships that previously would have qualified as trusts, and that this could limit the development of case law. However, we believe that these concerns can be alleviated by the broad drafting of the provisions, which takes account of only the widely accepted, core features of a trust. The provision encompasses the full ambit of express trusts.

### Recommended approach

- 4.8 We have chosen to base the recommendation on the widely accepted definition in *Underhill and Hayton Law of Trusts and Trustees*,<sup>157</sup> with some elucidation of key concepts and expansion to include purpose trusts.
- 4.9 Several submitters and consultees raised problems with particular aspects of the definition used in the *Preferred Approach Paper*. We have taken account of these submissions by adjusting wording in the indicative draft to better reflect the wording of the *Underhill and Hayton* definition. It includes references to the fiduciary and proprietary features of trusts. We have also followed submitter suggestions to make it more flexible, expand definitions of beneficiaries and trustees, add a definition of settlor and trust property and remove the problematic requirement included in the *Preferred Approach Paper* proposal that trust property be “identifiably separate” from the trustee’s own property.<sup>158</sup>
- 4.10 We have added R1(6) to ensure that the provisions on the characteristics and creation of a trust and any other provision of the new Act do not affect or limit Te Ture Whenua Māori Act 1993 or the Māori Land Court’s jurisdiction. As discussed in chapter 3, we intend that the Court would continue to exercise its jurisdiction in relation to trusts, and to apply general trust law in a way that reflects this particular context.<sup>159</sup>

### Non-application to constructive and resulting trusts

- 4.11 We have considered whether resulting and constructive trusts should come within the ambit of the new Act. There is general agreement that some but not other parts of the new Act will be relevant to these types of trusts. There are two ways that this could be addressed: either by stating that the Act generally applies to constructive and resulting trusts but specifying which parts do not apply; or by stating that the Act does not generally apply but indicating that the courts may have recourse to the provisions of the Act when making directions about a specific constructive or resulting trust. We recommend the latter approach because much of the Act, particularly the new provisions on trustees’ duties and exemption clauses, are not relevant to constructive and resulting trusts. It is better not to attempt to define constructive and resulting trusts or to set out which parts of the Act apply to them because of the considerable variation in their nature. When finding that a constructive or resulting trust exists and determining how it operates, the courts will be able to consider or rely upon certain parts of the Act.

157 David J Hayton, Paul Matthews and Charles Mitchell *Underhill and Hayton Law of Trusts and Trustees* (18th ed, LexisNexis, London, 2010) at [1.1] [*Underhill and Hayton*].

158 *Preferred Approach Paper*, above n 154, at P1(1)(b).

159 See [3.50]–[3.58].

## Finding that no trust exists

- 4.12 The corollary of having principles of law (whether in statute or not) about what is required for an express trust to be established is that the courts must be able to find that a trust does not exist if those requirements are not satisfied. Consistent with our approach of stating the principles of law in the new Act, we propose that the Act include a provision to remove any doubt that this is an option open to the courts.
- 4.13 There is currently a concern that the law lacks a means of addressing arrangements purporting to be trusts but which lack the fundamental elements of a trust, such as the intention to create a trust, the duties of a trustee, and any separation of beneficial and legal ownership. The law needs to ensure that people who gain the protection and benefits of not being considered the legal owners of property, but who have or will have a beneficial entitlement to the property, are subject to the full legal consequences of the property being in trust; that is, the management by the trustees subject to the duties of trustees for the benefit of the beneficiaries (or purpose of the trust). The property is no longer at the settlor's beck and call, even if the settlor is a beneficiary.
- 4.14 Our recommended approach to this issue retains significant court discretion. It would not constrain the court's ability to assess the situation and make appropriate orders, and to find that a trust does not exist on any other basis.
- 4.15 In this review, the Commission has considered the following alternative legislative interventions: to expand and clarify sham trusts; to restrict the purposes for which trusts can be used; to include a general look-through provision whereby trusts can be set aside or trust property considered to belong to the settlor; and to limit settlor control. We have decided against these approaches. We have concluded that the interface between the principles of trust law and other public policy considerations needs to be addressed on an issue by issue basis within the individual legislative schemes.<sup>160</sup> The purpose of this review is to improve the clarity and functioning of trust law, and to strengthen and uphold the concept of a trust, which has been developed over hundreds of years. The courts will still have the ability to find that doctrine of sham or something similar applies independently of the legislation if they consider this law applicable and necessary.
- 4.16 However, we are cognisant that at a time when trusts as a form of property holding are receiving some bad press because a minority are being used for purposes some consider unethical and because they override policies of other legislation, it is essential that the trust concept is seen to have integrity. In other words, if a trust is validly created then all the legal consequences of a trust must flow from that. If a trust is not validly created then the legal consequences from which a settlor or beneficiary may receive an advantage, including the protection of trust assets from creditors and ostensibly lower levels of personal assets and income, cannot apply. This is the case under the current law. If the three certainties are not present when a purported trust is established, the court must find that there is no trust. The consequences of a finding that any of the certainties are not fulfilled would be those available to the court under the current law. We do not consider it necessary to state the effect of a purported trust found not to have met the three certainties.
- 4.17 While there have been several recent cases in which the validity of a trust has been in question, arguments and judgments have focused on considering whether a trust was a sham or illusory

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160 Submitters were asked whether they agreed with the approach that trusts should continue to be addressed in individual legislative schemes, rather than through a uniform "look-through" provision in trusts legislation (*Preferred Approach Paper*, above n 154, at P57). Most submitters agreed or did not have a concern with this, but a few did highlight issues with particular legislative schemes that they would like to see addressed, such as the relationship between tax trust rules and general trust law, and insolvency.

trust,<sup>161</sup> or whether despite the existence of a trust, a settlor or discretionary beneficiary has property rights in trust property.<sup>162</sup> We consider that it is worthwhile giving more prominence to the power of the courts to find that a purported trust was never properly established in accordance with the core principles of trust law. A legislative provision is the best way to achieve this.

- 4.18 Inland Revenue submitted that the legislation should allow a trustee, beneficiary or any other party, including a creditor, to apply to the court to confirm a trust's existence. We consider that this could result in unwarranted interference in a trust.

### Application of recommendation to existing trusts

- 4.19 The recommendation in this chapter should apply to all trusts, whether new or existing at the time of the enactment of the new Act. The provisions reflect current law so will not alter the position of existing trusts.

## INDICATIVE DRAFT PROVISIONS

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### Part 1

#### *Preliminary provisions*

#### 1 Interpretation

- (1) In this Act, unless the context otherwise requires,—
- beneficiary** means a person who receives, or who will or may receive, a benefit under the terms of a trust; and includes a discretionary beneficiary; and may include a settlor or trustee if the settlor or trustee is included as a beneficiary under the terms of the trust
- discretionary beneficiary** means a person who may benefit under an express trust at the discretion of the trustee or under a power of appointment but who does not have a fixed, vested, or contingent interest in the trust property
- express trust** has the meaning given to it in **section 3**
- permitted purpose** means a charitable purpose and any other purpose for a trust that is permitted in law
- settlor** means a person who settles property on a trust, or transfers value to a trust or for the benefit of a trust on terms of trust; and includes a person who creates an express trust under a will to take effect after his or her death
- terms of the trust**—
- (a) means the terms on which the trust property is settled; and
- (b) includes any valid variations or amendments
- trust property** means any form of property that is settled on the trustees in accordance with the terms of the trust, and includes property derived from or accruing to the trust property (for example, income received)
- trustee** means a person who holds property under a trust.
- (2) In this Act, unless the context otherwise requires, a reference to a trust is a reference to an express trust.

<sup>161</sup> For instance, see *FMA v Hotchin* [2012] NZHC 323; *KA No 4 Trustee Ltd v FMA* [2012] NZCA 370, and *Clayton v Clayton* [2013] NZHC 2013.

<sup>162</sup> The “bundle of rights” doctrine, which argued that the various powers and interests that a discretionary beneficiary has can amount to a property interest for some purposes, see *Walker v Walker* [2007] NZFLR 772; *Harrison v Harrison* [2009] NZFLR 687; *R v R* HC AK FAM-2009-004-1627, FAM-2009-004-1628, 19 November 2009.

- (3) Nothing in this Act prevents a court, in interpreting the provisions of this Act, from having recourse to the general law of trusts and equity where that law is consistent with this Act.

## 2 Act applies to express trusts

- (1) This Act applies to express trusts.
- (2) However, in a particular case relating to a resulting trust or a constructive trust, a court may make orders applying so much of the Act to the trust as it thinks appropriate.

### Subpart 1 — Express trusts

## 3 Meaning of express trust

For the purposes of this Act, an **express trust** means a trust that—

- (a) has the characteristics set out in **section 4**; and
- (b) is created in accordance with **section 5**.

## 4 Essential characteristics of express trust

- (1) The characteristics of an express trust are:
- (a) it is a legal relationship in which a trustee holds or deals with trust property in 1 or both of the following cases:
- (i) trust property held or dealt with on behalf of the beneficiaries (where a trust has beneficiaries);
  - (ii) trust property held or dealt with for the purpose of the trust (where a trust is for a permitted purpose); and
- (b) the trustee is under a fiduciary obligation to deal with the trust property for—
- (i) the benefit of the beneficiaries (where a trust has beneficiaries); or
  - (ii) the purpose of the trust (where a trust is for a permitted purpose); or
  - (iii) the benefit of the beneficiaries and the purpose of the trust; and
- (c) if the trustee's duties are enforceable, they may be enforced against the trustee by—
- (i) any 1 or more of the beneficiaries where a trust has beneficiaries; or
  - (ii) the Attorney-General where the trust is a charitable trust; and
- (d) as a consequence of **paragraphs (a) to (c)**, the beneficiaries have equitable rights in or in respect of the trust property.
- (2) An express trust must not have the sole trustee as the sole beneficiary of the trust.

## 5 Creation of express trust

An express trust is created,—

- (a) subject to any formalities prescribed by a statute, by the settlor who, with reasonable certainty and by words or actions,—
- (i) indicates an intention to create a trust; and
  - (ii) identifies the beneficiaries or the trust purpose; and

- (iii) identifies the trust property; or
- (b) if a statute provides for the creation of an express trust, in accordance with that statute.

## 6 No express trust except under section 5

- (1) A trust, if it is to be an express trust, must be created in accordance with section 5.
- (2) Nothing in subsection (1) precludes the invalidity of an express trust on any other ground recognised at law.

### Commentary

Because the definition of “person” in the Interpretation Act 1999 includes a corporation sole, a body corporate and an unincorporated body, the various definitions in clause 1 that refer to a person are inclusive of these forms of non-natural person. In the definition of “settlor” in clause 1, we understand that there could be multiple settlements made by the same settlor to the same trust, and also multiple settlors to the same trust. In the Financial Markets Conduct legislation context, definitions of “settlor” and “trust property” may differ from those in clause 1.

Clause 4 is intended to bring within the ambit of the Act any express trusts currently recognised by law. It restates general trust law principles and is intended to be broad and inclusive. It emphasises the core characteristics of trusts: the fiduciary nature of the obligation, the trustee’s legal ownership of trust property, the proprietary effect of trusts and the enforceability of trusts. In describing the trust as a “legal” relationship in clause 4(1)(a), “legal” is intended to have a broad meaning, inclusive of equity. Clause 4(1)(a), (b) and (c) are intended to accommodate purpose trusts, but the drafting may need to alter slightly once the Law Commission’s charitable and purpose trust review has been completed. Clause 4(1)(c) is phrased as it is because the limited category of non-charitable purpose trusts that are currently permissible are, although valid, unenforceable.

Clause 5 sets out how a trust is created by referencing “the three certainties”, the well accepted requirements for the creation of a trust, as well as statutes that establish trusts, such as Te Ture Whenua Maori Act 1993. The requirements for the creation of a trust are subject to other statutory requirements, such as those in the Wills Act 2007 and the Property Law Act 2007 where applicable.

Clause 6 confirms the existing law. In making a finding under this provision, the court would determine the legal consequences depending on the circumstances of the case. It is intended that a trust is not created until such time as property is transferred to the trust.

# Chapter 5

## Trustees' duties

### INTRODUCTION

- 5.1 The duties that a trustee owes to beneficiaries are a key facet of the trust relationship. Currently there is little reference to trustees' duties in trusts legislation.<sup>163</sup> It is difficult to understand a trust without understanding trustees' duties. Our intention with these recommendations is to improve the accessibility and clarity of the law. We propose that the new Trusts Act summarise and restate trust law in this area with specific details left to be governed by rules of equity. This chapter discusses our recommendations relating to:
- the mandatory and default duties of trustees;
  - exemption of trustee liability and indemnity clauses;
  - the retention of trust information by trustees; and
  - the provision of trust information to beneficiaries.
- 5.2 The arguments regarding the reform options on these topics are discussed more fully in the *Preferred Approach Paper*<sup>164</sup> and *Fourth Issues Paper*.<sup>165</sup>

### DUTIES OF TRUSTEES

#### RECOMMENDATION

- R2 The new Trusts Act should provide that:
- (1) The following are the mandatory duties of a trustee (which will be implied into every trust and cannot be excluded from the trust relationship):
    - (a) to be familiar with the terms of the trust;
    - (b) to act in accordance with the terms of the trust;
    - (c) to act honestly and in good faith;
    - (d) to act for the benefit of the beneficiaries or to further the purpose of the trust, in accordance with the terms of the trust;
    - (e) to exercise stewardship over the trust property for the beneficiaries or the purpose of the trust; and
    - (f) to exercise powers for a proper purpose.
  - (2) In the exercise of any duty, there is no requirement that beneficiaries are treated equally, as long as they are treated in accordance with the terms of the trust.

163 Sections 13B and 13C of the Trustee Act 1956 address the duty of prudence in relation to investments by trustees.

164 Law Commission *Review of the Law of Trusts – Preferred Approach* (NZLC IP31, 2012) at ch 3.

165 Law Commission *The Duties, Office and Powers of a Trustee: Review of the Law of Trusts – Fourth Issues Paper* (NZLC IP26, 2011) at chs 1–3.

R3 The new Trusts Act should provide that:

- (1) The following are the default duties of a trustee (which apply if and to the extent that they are not excluded or modified, explicitly or implicitly, by the terms of the trust or by statute):
  - (a) not to exercise any power directly or indirectly for the trustee's own benefit;
  - (b) to actively and regularly consider the exercise of the trustee's powers;
  - (c) not to fetter the future exercise of the trustee's powers;
  - (d) to avoid a position of conflict of interest;
  - (e) to maintain accounts of the trust property that adequately identify the assets, liabilities, income and expenses of the trust and are appropriate to the value and complexity of the trust property;
  - (f) not to be unfairly partial to some beneficiaries to the detriment of others;
  - (g) not to make a profit (that has not been permitted by the beneficiaries);
  - (h) to act without reward except where it has been permitted by the beneficiaries or is in accordance with the trustee's right to be reimbursed for legitimate expenses and disbursements;
  - (i) where there is more than one trustee of a trust, to act unanimously;
  - (j) to manage the trust with reasonable care and skill; and
  - (k) to invest prudently.
- (2) These duties may be excluded or modified, explicitly or implicitly, by the terms of the trust but not to the extent that such alterations are inconsistent with the mandatory duties.

### Current law

5.3 The duties of trustees are not set out in the Trustee Act 1956, but are found in centuries of case law. It is generally accepted that there are some fundamental duties which, if excluded, mean that the relationship does not constitute a trust. There are some duties which do not apply to every trust because trust deeds may alter the trustees' obligations by explicitly including some duties and excluding others. The mandatory "irreducible core" of trustees' duties was described in the English Court of Appeal by Millett LJ in the case of *Armitage v Nurse* as being to "perform the trusts honestly and in good faith for the benefit of the beneficiaries".<sup>166</sup> Millett LJ described this as the minimum obligation necessary to give substance to a trust.

### The case for setting out the duties in the new Act

5.4 Trustees' duties are of central importance in a trust and a large number of New Zealanders, including many without legal training, are trustees. We understand that many trustees do not fully understand their obligations. It is worthwhile to include each duty in a simplified form in legislation. This would provide a clear and accessible base from which trustees can gain an understanding of their duties. It would have educative value and may encourage improved standards among trustees because of the greater prominence given to the duties in the law. It

166 *Armitage v Nurse* [1998] Ch 241 at 253. See also Millett LJ in *Bristol and West Building Society v Mothew* [1998] Ch 1 (CA) at 18.



could be argued that the duties are sufficiently clear in the case law and that there would be little practical benefit in expressing the duties in a statute. However, our view is that the significance of the duties to the trust relationship warrants them being given greater attention by being stated in legislation.

- 5.5 Most submitters throughout our consultation have agreed that this is a helpful approach. As a result of feedback we have received following the *Preferred Approach Paper*, we have attempted to reduce repetition and cross-over between different duties, and, where there is overlap, to make it clear what this means. We have clarified the wording of some of the duties to better reflect what was intended.

### Nature of the duties provisions

- 5.6 We intend that these provisions should express, in a distilled form, the principles of law about the duties of trustees that can be gleaned from case law. They would not be a complete code of the law of trustees' duties. The detail of how the law requires the duties to apply in practice would come from case law.

- 5.7 We see this as being similar to the nature of the provisions on company directors' duties in the Companies Act 1993.<sup>167</sup> In its 1989 report upon which the reforms enacted in the Companies Act were based, the Law Commission described the intention of the recommendations relating to directors' duties as to:<sup>168</sup>

... distil the general principles from the cases and express them in the statute, to make them more accessible. Such a statement of general principle was recommended by the Macarthur Committee and has been adopted by the Canadian and Australian Acts. The response to the [Law Commission's] discussion paper indicated overwhelming support for similar reform.

- 5.8 It is generally considered that the case law continues to be relevant in the law of company directors' duties. It acts as an aid to the interpretation of the general principles in the Companies Act and is still relevant to the extent that the Companies Act does not address a particular duty or remedy for breach of a duty.<sup>169</sup>

- 5.9 We recommend that the part of the new Act that includes the duties is subject to the qualification that nothing in the new Act prevents a court from having recourse to the general law of trusts and equity where that law is consistent with the purpose of the Act (see clause 1(3) of the indicative drafting in Appendix A). The intention is to allow the courts to continue to apply the nuances and exceptions to the duties that exist in case law.

### Types of duties

- 5.10 Our recommendations emphasise the distinction between duties that are mandatory and duties that are default. Mandatory duties are part of every trust relationship. They will be implied into every true trust, even where a trust deed attempts to exclude them. In some cases the attempted exclusion of a mandatory duty may be evidence that the settlor did not in fact have the requisite intention to create a trust but intended some other legal relationship.

- 5.11 There are other duties that the courts have found to arise in a trust unless the trust deed states that they do not apply. We classify these as default duties. They are implied in the trust relationship if the trust deed is silent on the matter. We consider it is useful to have a list of

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167 Companies Act 1993, ss 131–138.

168 Law Commission *Company Law: Reform and Restatement* (NZLC R9, 1989) at [186]. The “Macarthur Committee” refers to the New Zealand Special Committee to Review the Companies Act *Final Report of the Special Committee to Review the Companies Act* (Government Printer, Wellington, 1973).

169 *Company Law* (online looseleaf ed, Brookers) at [CA131.01].

duties that apply to a trustee in the absence of any trust term to the contrary. Some of these duties may be excluded outright (such as the duty to act without reward) and some may be modified to alter the extent to which they must be met (such as the duty not to be unfairly partial).

- 5.12 The proposals in the *Preferred Approach Paper* also made a distinction between conduct duties, relating to a trustee's standard of behaviour when carrying out his or her functions as a trustee, and content duties, which prescribe what a trustee must do and not do.<sup>170</sup> We no longer consider that it is helpful to categorise duties this way, as it is not a straightforward distinction. Often duties will have an element of both conduct and content. The three categories that were previously proposed overcomplicated the duties provisions and defeated the intention to make trustees' duties more accessible and comprehensible. Much of our formulation was driven by a desire for the mandatory duties to fit closely with the exemption clause provisions. We now consider that the current formulation is unlikely to create problems in practice. It was also pointed out to us that it makes little sense to talk about a negligent breach of the mandatory duties, because of the nature of these duties.

### The mandatory duties

- 5.13 Some commentators argue that the duty to act in good faith and honestly for the benefit of the beneficiaries (or a permitted purpose) is often considered the only mandatory obligation on trustees. We would argue that all of the mandatory duties we list in our recommendation are as vital to the existence of a trust as the obligation of honesty and good faith. They are necessarily implied by the trust relationship.
- 5.14 The law of trustees' duties has been developed through many cases over hundreds of years. Many of the duties are nuanced and apply differently in different circumstances. Our recommended duties summarise the general principle of each duty, without seeking to set out these nuances and variations. The formulation of the duties provisions in the indicative drafting (and clause 1(3) of the draft in Appendix A) preserves recourse to case law to assist in understanding and applying these duties.
- 5.15 R2(1)(a) (clause 10(a) of the draft) uses the term "be familiar" rather than the previously suggested "understand" as this term recognises that it may not be possible or realistic for a trustee to objectively understand the terms of a particular trust deed. R2(1)(e) (clause 10(e)) uses the term "exercise stewardship" rather than "account to". The latter term caused confusion with the narrower default duty to provide information and confusion as to whether the production of accounts was required. The intention is that trustees in a private trust are accountable to the beneficiaries. Using "stewardship" instead reduces the risk of confusion and better conveys the nature of the relationship.

### The default duties

- 5.16 The default duties in the recommendation are a list of commonly accepted duties from judge-made law. We summarise the existing duties and do not prescribe how they apply in individual circumstances. We acknowledge that there can be some tension between the broadly stated mandatory duties, which cannot be excluded, and the narrower default duties, which can be modified or excluded by the terms of a trust, where these overlap. For instance, there is some overlap between the mandatory duty to exercise stewardship and the default duty to maintain accounts. While it is possible to modify the default duty to suit the requirements of the particular trust, these elements are necessary for the mandatory duty and so they cannot be

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<sup>170</sup> *Preferred Approach Paper*, above n 164, at P5–P7 and [3.16].

- completely excluded. It will ultimately be a contextual question for the courts as to whether a particular attempt to modify or exclude a default duty in fact attempts to oust a mandatory duty or is incompatible with fulfilment of a mandatory duty.
- 5.17 While the default duties are potentially excludable, we note that trust drafters will still need to be cautious when excluding default duties. Deeds have to be drafted in such a way that the arrangement falls within the definition of a trust and the requirements for the creation of a trust. The attempted exclusion of too many default duties may be interpreted as an attempt to exclude a mandatory duty or may lead a court to find that no trust was intended.
- 5.18 During consultation we discovered that many readers perceived the list of default duties in the *Preferred Approach Paper* as prescriptive rules.<sup>171</sup> They were concerned that the various exceptions and nuances in the law were not taken into account. Particular words, such as “evenhandedness” and “accounts”, were identified as problematic. We recognise that some duties are only relevant to certain types of trusts and not others or may be interpreted differently in different contexts, and that it is problematic to attempt to present these as general duties. We therefore intend to present only those duties that are universally applicable to trusts in the list of default duties, and to qualify them with suitable wording that shows that they can be departed from in a particular trust and are subject to case law exceptions.
- 5.19 In order to avoid the confusion and concern exhibited by some submitters about the effect of the duties, we have clarified that none of the duties, mandatory or default, require that beneficiaries are treated equally. Clause 8 of the draft below states: “[t]he exercise of a trustee’s duty does not require that all beneficiaries are treated equally, provided that beneficiaries are treated in accordance with the terms of the trust”. This is particularly important in relation to R2(1)(d) (clause 10(d) of the draft), which requires trustees to act for the benefit of the beneficiaries, and R2(1)(f) (clause 18 of the draft), which requires that trustees are not unfairly partial to some beneficiaries to the detriment of others.

### Standard of care

- 5.20 A major departure from the proposals in chapter 3 of the *Preferred Approach Paper* is that we are no longer recommending that a general duty or standard of care be included alongside the mandatory and default duties. As a result of consultation feedback, we have reconsidered this proposal and are no longer contemplating that a general duty of care applies to every exercise of a duty, power or discretion of a trustee. We do not consider that this accurately represents the law applying to trustees. We no longer propose that a statutory standard of care apply to the determination of whether a breach of a duty has occurred, but leave this for the decision of the courts. Instead, it makes sense that the standard of care applies to the exercise of powers. The standard of care is addressed in paragraphs [6.33] to [6.41] alongside trustees’ powers.

### Application to existing trusts

- 5.21 The mandatory and default duties apply to all trusts, whether settled before or after the enactment of the new Act. The duties provisions represent the existing law and so do not change the basis on which existing trusts were settled. The clauses will be useful to make it clear to all trustees the obligations they are under. We recognise that existing trust deeds will not be written on the basis that there is a clear list of default duties that should be clearly overridden if they are not to apply, and instead may implicitly override the existing duties. If the existing deeds do not do this the trustees are already bound by the duties.

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<sup>171</sup> *Preferred Approach Paper*, above n 164, at P7.

## AVOIDING THE CONSEQUENCES OF A BREACH OF TRUST

### RECOMMENDATION

- R4 (1) The new Trusts Act should provide that:
- (a) the terms of a trust must not limit or exclude a trustee's liability for a breach of trust or grant the trustee an indemnity against the trust property in respect of liability for a breach of trust arising from the trustee's own dishonesty, wilful misconduct or gross negligence;
  - (b) a clause that purports to have the effect stated in (a) is invalid (and is effectively severed from the terms of the trust), provided it is found that the settlor's overall intention was in fact to create a trust as opposed to some other type of relationship;
  - (c) any paid trust adviser or trust drafter who causes a settlor to include a clause in the terms of the trust that has the effect of limiting or excluding liability for negligence, or of granting an indemnity against the trust property in respect of liability for negligence, must before the creation of the trust take such steps as are reasonable to ensure that the settlor is aware of the meaning and effect of the clause; and
  - (d) if a person who is paid to advise on the terms of a trust or the drafting of a trust deed fails to meet the obligation in (c) and is a trustee of the trust, the exemption or indemnity clause will have no effect in respect of that trustee.
- (2) Professional regulatory bodies relevant to trusts should provide guidance for their members as to what steps would be reasonable to ensure that a settlor is made aware of the meaning and effect of any trustee exemption clauses.
- (3) The new Act should re-enact an equivalent of section 73 of the Trustee Act 1956, which gives the court the power to relieve a trustee wholly or in part from personal liability for a breach of trust if the trustee acted honestly and reasonably, and ought fairly to be excused.

### Exemption and indemnity clauses

- 5.22 If legislation is to assist people in clearly understanding the extent of trustees' obligations, it needs to address potential modifications to the consequences of a breach of trust. By limiting or avoiding liability for a breach of trust or being indemnified against such liability, the importance of the duties can be undermined. Exemption clauses are not currently regulated by statute in New Zealand.
- 5.23 We recommend a simpler statement of the law regarding clauses exempting trustees from liability and indemnifying trustees for breach of trust than that proposed earlier in the *Preferred Approach Paper*.<sup>172</sup> Our recommendation is based on the law established by the English Court of Appeal in *Armitage v Nurse* that a trust deed can exclude trustees' liability for a breach of trust arising from conduct that is not fraud.<sup>173</sup>
- 5.24 The recommendation goes further by clarifying that exemption clauses cannot be used to exempt liability for gross negligence. It applies one rule regarding valid exemption and

<sup>172</sup> At P8.

<sup>173</sup> *Armitage v Nurse*, above n 166.

indemnity clauses across every type of breach of trust, instead of attempting to limit their use to a greater degree when they apply to mandatory duties.

- 5.25 We considered including a provision that outlines circumstances in which the trustee can be indemnified or exempted from liability to a greater extent than is allowed by R4(1)(a) and (b), such as where they are directed to by the court or given permission by the beneficiaries. However, we do not think such a provision is necessary as these exceptions will apply regardless.

### The case for reform of exemption and indemnity clauses

- 5.26 Exemption and indemnity clauses enable trustees to manage their risks and provide protection for trustees from litigious beneficiaries. They can make trusteeship more attractive to a trustee and mean that insurance is more likely to be available to trustees. However, beneficiaries are vulnerable to the consequences of such clauses, because they will potentially lose out if the value of trust assets is reduced by trustees not conducting themselves in a way that trustees should. Where an exemption or indemnity clause applies, beneficiaries will probably have no effective means of redress for loss to the trust property. While settlors can be seen as representing the interests of beneficiaries when a trust is settled and the clause is agreed to, it seems that many settlors are not actually aware that beneficiaries might lose out as a result of an exemption clause.
- 5.27 We are also concerned that allowing broad exemption and indemnity clauses may undermine the core trust concept, which requires that a trustee has obligations towards beneficiaries in respect of the trust property. Exemption and indemnity clauses do not remove the obligations from trustees, but they do remove the most significant consequences of a breach and leave beneficiaries without the most effective form of redress. While there are some other possible consequences of a breach of trust, such as the removal of the trustee, it can be argued that the duties of trustees are effectively empty if the trustee is exempted from liability for compensation or the trustee is indemnified from the trust property for the loss.

### The types of conduct for which liability cannot be excluded

- 5.28 We propose that legislation should clarify the types of conduct for which liability cannot be excluded by drawing a line between the type of conduct leading to breach of trust where liability should be able to be excluded and the type of conduct where it should not. We propose that this line should be drawn at gross negligence, so that exemption clauses excluding liability for negligent breaches of trust would be permissible but not those excluding liability for grossly negligent breaches (see draft clauses 27 and 28).
- 5.29 In the *Preferred Approach Paper* we proposed to set this line at recklessness as a way of avoiding potential problems with defining gross negligence.<sup>174</sup> Many submitters were in favour of this, although some submitters did prefer gross negligence. We now consider that there are fewer disadvantages with using a standard of gross negligence. Gross negligence has been used in a growing number of New Zealand statutes over the last 10 years.<sup>175</sup> Countries such as Jersey and Guernsey have enacted statutory provisions to address exemption and indemnity clauses in trusts and have used the gross negligence standard.<sup>176</sup> In February 2013, the Hong Kong Legislative Council introduced the Trust Law (Amendment) Bill, which proposes to regulate

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174 *Preferred Approach Paper*, above n 164, at [3.55]–[3.59].

175 For instance, Corrections Act 2004, s197E; Private Security Personnel and Private Investigators Act 2010, ss 80 and 83; Canterbury Earthquake Recovery Act 2011, s 83; Retirement Villages Act 2003, s 40; and Weathertight Homes Resolution Services Act 2006, s 125F.

176 Trusts (Jersey) Law 1984, s 30(10) and Trusts (Guernsey) Law 2007, s 39(7) and (8).

trustee exemption and indemnity clauses, and uses gross negligence to delineate the conduct for which liability cannot be exempted.<sup>177</sup>

- 5.30 We received significant feedback on the proposal in the *Preferred Approach Paper* that exemption clauses should not be used to exclude liability for a negligent breach of a mandatory duty. There were concerns that this was a considerable restriction on the use of exemption clauses and that it would have the effect of discouraging professionals from acting as trustees. After reconsideration we were convinced that there is little sense in making distinctions and rules based on negligent breaches of mandatory duties as this is unlikely to arise in practice.
- 5.31 It could be argued that any restriction on the types of exemption clauses that may be relied upon is an undue limitation on a settlor's freedom. We would contend that it is a reasonable consequence of the choice of the trust form that the trustee of the trust property be held to certain standards and face consequences for breaching those standards in sufficiently serious ways. The extension of the restriction on exemption clauses to include gross negligence reinforces the fact that trustee obligations are real.

### Greater restrictions for professional trustees

- 5.32 We have considered whether the same limits should apply to non-professional trustees as would apply to professional trustees. The concern that exemption and indemnity clauses unfairly limit trustee responsibility is perhaps more acute in relation to independent trustees who are employed and paid to carry out this role. However, many trustees in New Zealand are not paid professional trustees. Allowing exemption and indemnity clauses to apply more broadly to lay trustees than professional trustees would leave open the concern that the duties of trustees are being undermined by the reduced consequences for a breach of trust. Having one standard for conduct that cannot be excluded, as opposed to the alternative of having differentiated rules, is simpler and easier to understand. The higher standard in what is expected of professional trustees will arise through the court's interpretation of what constitutes fraud or gross negligence for professional trustees as opposed to lay trustees, and through the standard of care in the exercise of powers.

### Requirement for settlors to be informed

- 5.33 Some settlors of trusts are unaware of the practical effect of the broad exemption and indemnity clauses that are included in many trust deeds. These clauses can be a key part of the arrangement negotiated with paid professional trustees for their services as trustees. Settlors may not realise that trustees will not be held liable for breaching the trust.
- 5.34 Requiring a trust drafter or adviser to inform a settlor of the meaning and effect of an exemption clause addresses this issue (see draft clause 31 below). Settlors would be given an informed choice about the effect of including the clause at the time of settlement. This reform would not affect beneficiaries directly, but if settlors are better informed about exemption clauses they may choose not to include such broad clauses in their deeds or at least will have a more accurate understanding of the trust arrangement. It is not intended that settlors would necessarily be required to obtain independent legal advice. It is likely that a practice would develop where settlors would be required to sign a form certifying that they have been advised about the effect of exemption and indemnity clauses, which would constitute evidence that the advice was given. The advice would only be required to be given at the time that the settlor creates the trust.

<sup>177</sup> Trust Law (Amendment) Bill 2013, cl 27. The Hong Kong Financial Services and the Treasury Bureau had earlier proposed that a recklessness standard be used (Hong Kong Financial Services and the Treasury Bureau *Detailed Legislative Proposals on Trust Law Reform* (Consultation Paper, March 2012) at annex H, 41W).

The recommendation may result in some additional time and cost in the creation of a trust, but we consider it should be an essential part of the process.

- 5.35 We recommend that the professional bodies for lawyers, accountants and financial advisers should develop guidance, perhaps in their codes of conduct, to help ensure that their members develop appropriate practices. A breach of the statutory obligation to explain exemption clauses would likely result in disciplinary sanctions by the relevant regulatory body.<sup>178</sup>

### Application to existing trusts

- 5.36 The provisions recommended in R4(1)(a) and (b), restricting certain exemption and indemnity clauses, should apply to all trusts settled after the date of enactment of this Act and all trusts settled before enactment after the lapse of two years. These recommendations are an advancement on the law as it is understood by most people at the moment because of the prohibition on the use of exemption and indemnity clauses for gross negligence. While we do not consider that it is too onerous for these recommendations to apply to all trusts, existing trustees should be given the opportunity to reconsider their position.
- 5.37 The provisions recommended in R4(1)(c) and (d), regarding the obligation to inform a settlor of the effect of an exemption or indemnity clause, should apply only to trusts settled after the enactment of this Act. They should also apply to new terms of existing trusts inserted after the enactment of this Act. These relate to what must occur when a new trust is settled so are not relevant to existing trusts. R4(3) should apply to all trusts regardless of when they were settled as it is a continuation of the existing section 73 of the Trustee Act. Section 73 may well be a useful tool for the courts in managing any difficulties arising from the transition to a new Trusts Act, as the courts will be able to consider relieving liability if the change to the law results in unfairness.

## RETAINING INFORMATION

### RECOMMENDATION

- R5 The new Trusts Act should provide that:
- (1) In exercising the mandatory duties of a trustee, a current trustee is required, so far as is reasonable, to retain the following:
    - (a) the trust deed;
    - (b) any variations made to the trust deed or terms of the trust, including variations made to the beneficiaries of the trust;
    - (c) a list of all of the assets currently held as trust property and liabilities of the trust;
    - (d) any records of trustee resolutions made during that trustee's trusteeship;
    - (e) any written contracts entered into during that trustee's trusteeship;
    - (f) any accounting records and financial statements prepared during that trustee's trusteeship;
    - (g) deeds of appointment and retirement of trustees;

<sup>178</sup> This is similar to the approach taken by the Law Commission for England and Wales in *Trustee Exemption Clauses* (Law Com No 301, 2006) at 69.

- (h) any expression of the intention or wishes of the settlor; and
  - (i) any of the above documents retained by a former trustee during that trustee's trusteeship and passed on to the current trustee.
- (2) Where there is more than one trustee, it is not necessary for every trustee to hold a copy of the documents, except for the documents in R5(1)(a) and (b). One trustee may hold the documents on behalf of the other trustees as long as the documents are available to the other trustees on request.
- (3) A trustee is required, so far as is reasonable, to retain the documents for the duration of his or her trusteeship of the trust and, if the trust continues, to pass on the documents to at least one replacement or continuing trustee when he or she retires or is removed.

### Retention of documents by trustees

- 5.38 The intention of this recommendation is to make it clear to trustees that trusteeship requires the exercise of responsibility for significant records. Including a provision regarding the retention of documents by trustees was well supported by submitters. Several submitters suggested the list of documents that should be retained should expand. The list has been adjusted as a result to include documents not already covered that are of significance to the management of a trust (see draft clauses 33 to 37 below).
- 5.39 It has also been suggested by a few submitters that the provision should place a limit on the period of time that a trustee is required to retain the documents because retention of all documents for the full duration of the trust may be unduly burdensome. Seven years and 20 years were suggested durations. However, both are potentially too short given the duration of trusts and the likely timeframe over which decisions are made. The proposal has been altered to make it clear that documents should be retained for the duration of the trust.
- 5.40 It was noted in submissions that the proposal did not create an obligation for retiring or removed trustees to pass on documents to new trustees or for new trustees to retain them. This gap could lead to an incorrect understanding that when a trustee leaves the office the trust documents may be discarded.
- 5.41 We were also urged to address the issue of whether one trustee can hold documents on behalf of other trustees. We consider that it is reasonable for one trustee to be able to hold the trust documents on behalf of others, although this would not be necessary. However, every trustee should hold a copy of the trust deed and any variations to it.
- 5.42 We want to address the concern that some trustees may see this list as all the documents they will ever need to retain. We want to make the intention clear that this list represents the minimum number and type of documents that may need to be retained depending on the nature of the trust.
- 5.43 Inland Revenue has submitted that it would be useful to include a provision indicating that trustees may have record-keeping requirements under other legislation. We have included this in the indicative draft clauses.

### *Letters or memoranda of wishes*

- 5.44 Letters or memoranda of wishes have been included in the list of documents that a trustee needs to retain because they are relevant documents that a trustee will usually have to consider when making decisions, particularly in relation to distribution. We recognise that the courts



have found different memoranda or letters of wishes can have differing legal status depending on whether they are intended to be binding or not.<sup>179</sup> We want to leave it open to the trustees (and the courts) to determine in the circumstances whether such a statement of the settlor's wishes is a part of the terms of the trust and its legal or moral effect. This recommendation is not intended to alter the law in this regard.

### Application to existing trusts

- 5.45 These provisions should apply to all trusts including those created before the introduction of the new Act. The requirements in this recommendation should represent what trustees are already required to do. Because the retention of documents obligation is subject to a reasonableness requirement we do not envisage that this will create hardship for trustees.

## PROVISION OF INFORMATION

### RECOMMENDATION

- R6 The new Trusts Act should provide that:
- (1) Trustees have a mandatory obligation to provide sufficient information to sufficient beneficiaries to enable the trust to be enforced;
  - (2) There is a presumption that trustees must:
    - (a) notify qualifying beneficiaries (those who the settlor intended to have a realistic possibility of receiving trust property under the terms of the trust) as soon as is practicable of the fact that a person is a beneficiary, names and contact details of trustees and the right of beneficiaries to request a copy of the trust deed or trust information; and
    - (b) provide trust information to a beneficiary who requests it within a reasonable time.
  - (3) The presumptions in (2) do not apply if a trustee reasonably considers that the information should not be provided after taking into account the following factors:
    - (a) the nature of the interests held by the beneficiaries, including the degree and extent of a beneficiary's interests or a beneficiary's likely prospects of receiving trust property in the future;
    - (b) whether there are issues of personal or commercial confidentiality;
    - (c) the expectations and intentions of the settlor at the time of the creation of the trust as to whether beneficiaries would be notified;
    - (d) the age and other circumstances of the beneficiaries;
    - (e) the impact on the trustees, other beneficiaries, and third parties;
    - (f) whether, in the case of a family trust, notification or non-notification may embitter family feelings and the relationship between the trustees and beneficiaries to the detriment of the beneficiaries as a whole;

179 Jeff Kenny and Jared Ormsby "What's so special about a letter of wishes and what documents should a beneficiary be entitled to see?" (paper presented to Cradle to Grave: The Interface between Property and Family Law, Auckland District Law Society, Christchurch, March 2013).

- (g) the practicality of providing information to all beneficiaries or members of a class of beneficiaries in a trust where there are large numbers of beneficiaries or unascertainable beneficiaries;
  - (h) whether some or all of the documents can be disclosed in full or in redacted form; and
  - (i) whether safeguards can be imposed on the use of the documents (for example, undertakings or professional inspection).
- (4) "Trust information" is defined to include any information regarding the terms of the trust, the administration of the trust, or the trust property that it is reasonably necessary for the beneficiary to have in order for the trust to be enforced, but does not include reasons for trustees' decisions.
- (5) A beneficiary may be charged for the reasonable costs of being provided with the trust information.
- (6) Trustees are entitled to apply to the court for an order as to whether they are required to notify a beneficiary or class of beneficiaries under (2)(a), or for an order as to whether they are required to provide a beneficiary with trust information under (2)(b). A beneficiary is entitled to apply to court for an order that the trustees supply trust information. The court is able to review the exercise of the trustees' discretion and merits of the trustees' decision.

### Disclosure of information to beneficiaries

- 5.46 There cannot be any obligation, and hence there cannot be any trust, if the trustee does not owe a duty to account to any beneficiary.<sup>180</sup> To be able to hold a trustee to account, beneficiaries need to know that they are beneficiaries of the trust and need to be able to be provided with trust information on request. While trust deeds can never dispense completely with the requirement to account to beneficiaries and the need to provide some information to some beneficiaries, what is required in each trust is dependent on the trust's circumstances. The decision as to whether a particular beneficiary is entitled to be notified that he or she is a beneficiary or is entitled to receive trust information on request has been found by the Privy Council in *Schmidt v Rosewood Trust* to be something that is within the court's inherent jurisdiction to supervise the administration of trusts.<sup>181</sup> Based on this decision, which was followed in New Zealand in *Foreman v Kingstone*,<sup>182</sup> the courts will apply the principle that a beneficiary should be notified of or provided with the information that is necessary to enable the trust to be enforced. We consider it important to translate this principle into statutory rules and guidance as to how a trustee is to exercise the trustee's discretion.
- 5.47 There appears to be general satisfaction among submitters with the principle in *Schmidt v Rosewood Trust* and no desire to change this. However, there is concern that from a practical perspective it is currently difficult for trustees to determine what their obligation to provide beneficiaries with information entails, because the position relies on the discretion of the court. The current law does not provide clear guidance to trustees in particular circumstances as to

180 David J Hayton, Paul Matthews and Charles Mitchell *Underhill and Hayton Law of Trusts and Trustees* (18th ed, LexisNexis, London, 2010) at [56.14] [*Underhill and Hayton*]; *Armitage v Nurse*, above n 166, at 253.

181 *Schmidt v Rosewood Trust* [2003] UKPC 26, [2003] 2 AC 709 at [66].

182 *Foreman v Kingstone* [2004] 1 NZLR 841 (HC); see also *Rauch v Maguire* [2010] 2 NZLR 845 (HC) at [30].

- how decisions regarding notifying beneficiaries and providing beneficiaries with information should be made. It appears that trustees are commonly required to make decisions about providing information and could do with greater clarification and guidance. The New Zealand Law Society commented that the law is only partially satisfactory because there is uncertainty. It also pointed to several problems in practice: a lack of awareness among trustees of what the disclosure obligations are; inconsistent disclosure practices; uncertainty about the extent to which a settlor can exclude disclosure obligations; and uncertainty about what age beneficiaries must be before information must be disclosed to them.
- 5.48 We do not think it possible or desirable for legislation to introduce fixed rules about which beneficiaries must receive what information because the law is, and needs to continue to be, trust and beneficiary specific. There will always need to be consideration of a number of factors in order to judge whether the trustee's mandatory general obligation to provide sufficient information to sufficient beneficiaries for the trust to be enforced results in a particular beneficiary or class of beneficiaries having a right to be notified of their status and to be provided with trust information. However, we consider that it is helpful for legislation to present the process that applies and the factors that may outweigh the general disclosure obligation (see draft clauses 38 to 44 below).
- 5.49 In response to feedback from submitters and consultees, we have clarified the recommendation from what was presented in the *Preferred Approach Paper*.<sup>183</sup> We have removed the option for the Public Trust to provide advice on whether trustees are required to release information to beneficiaries. This proposal was not supported by submitters. We now consider that trustees are sufficiently able to obtain advice on this issue from a range of sources, including a lawyer, the Public Trust or another adviser.
- 5.50 We are aware that some people would consider the presumption to notify certain beneficiaries (qualifying beneficiaries) to be an advancement on where the law is currently, although for trustees to be accountable it is clearly the case that some beneficiaries have to know about the trust. Trustees are likely to need to be more proactive in notifying beneficiaries. This may alter the way that some settlors choose to structure the beneficiaries of a trust, and may limit the types of beneficiaries included in a trust. We are confident that these recommendations will help trustees carry out their role with respect to beneficiaries in a way that truly reflects the respective rights and obligations of the parties involved in a trust.
- 5.51 In some cases there will be good reasons for settlors desiring to hold back information from some beneficiaries. So long as this can be justified in accordance with the factors proposed, settlors will continue to be able to do this.

### How the recommended provisions will work

- 5.52 We intend that the provision we recommend in R6(1) will confirm the mandatory obligation on trustees to provide sufficient information to sufficient beneficiaries to enable the trust (that is, the terms of the trust and the duties of the trustees) to be enforced. The new Act will set out two presumptions: that the trustee must notify qualifying beneficiaries of certain basic trust information (R6(2)(a)) and that the trustee must provide information to a beneficiary who requests it (R6(2)(b)). Despite these presumptions the trustee may decide that the information should not be provided if the trustee considers it reasonable not to after taking into account a range of factors (R6(3)). These factors are intended to allow the trustee to take into account the particular circumstances of the trust and the beneficiaries, the intentions of the settlor and the type of information. The factors are not determinative of what decision must be made but they

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183 *Preferred Approach Paper*, above n 164, at P9.

provide guidance as to what process and type of consideration a trustee must go through before withholding information.

- 5.53 The provisions we recommend apply to every trust. However, there will be certain types of trusts for which there will be a high likelihood that it will be reasonable for the presumptions not to apply because of the nature of these trusts (for instance, a large number of beneficiaries, presence of commercially sensitive information). Some types of trusts already contain perfectly adequate information provisions schemes within the terms of the trust, such as some Treaty settlement trusts, or within a statute, such as financial markets trusts. Another example is the energy trusts, which have the “Guidelines for access to information by beneficiaries of electricity community and consumer trusts”, a form of self-regulation supported by the Government when energy trusts were developed. They were introduced as an alternative to regulations to address this issue.<sup>184</sup>

### Application to existing trusts

- 5.54 The provisions in this recommendation should apply to all trusts settled after the enactment of this Act and all trusts already in existence after the lapse of two years after the enactment of this Act. We acknowledge that there may be administrative challenges with trustees meeting these obligations and think that there should be sufficient time for these to be worked through. Trustees of existing trusts will need to consider the settlor’s implied intention when balancing the reasons for withholding information against the presumptions to notify and provide information to beneficiaries, as existing trusts may not have an express statement of the settlor’s intention regarding disclosure of information to beneficiaries.

## APPLICATION OF DUTIES TO TRUSTEES OF TRUSTS UNDER DIFFERENT STATUTES

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- 5.55 Our intention is that the recommendations in this chapter create a general floor or baseline as to the obligations on trustees. These will apply generally across all types of trustees, including trustees of trusts created by or in accordance with other statutes that rely on the foundation of general trust law. This approach accords with the way that trust law currently interacts with specific types of statutory trusts, such as financial markets trusts and trusts established under Te Ture Whenua Maori Act 1993.
- 5.56 It should be emphasised that the duties apply contextually in that there may be different emphases placed on them and different nuances that apply in different contexts. For instance, the Māori Land Court, in supervising trusts under Te Ture Whenua Maori Act will have particular approaches to the duties that are appropriate in its context.

## INDICATIVE DRAFT PROVISIONS

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### Subpart 2 — Duties of trustee

#### *General*

#### 7 Types of trustee’s duties

A trustee has—

- (a) mandatory duties (*see sections 9 and 10*); and
- (b) default duties (*see sections 11 to 23*).

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<sup>184</sup> Submission of the Auckland Energy Consumer Trust on the *Fourth Issues Paper* at 1–2.

## 8 No requirement that beneficiaries be treated equally

- (1) The exercise of a trustee's duty does not require that all beneficiaries are treated equally, provided that beneficiaries are treated in accordance with the terms of the trust.
- (2) Nothing in subsection (1) derogates from section 18.

### *Mandatory duties*

## 9 What is trustee's mandatory duty

A trustee's mandatory duty is a duty that—

- (a) the trustee must perform; and
- (b) may not be excluded or diminished; and
- (c) applies regardless of anything that may be contained in the terms of the trust.

## 10 Mandatory duties

The trustee of a trust is under the following mandatory duties:

- (a) a trustee must be familiar with the terms of the trust; and
- (b) a trustee must act in accordance with the terms of the trust; and
- (c) a trustee must act honestly and in good faith; and
- (d) a trustee must, in accordance with the terms of the trust, act for the benefit of the beneficiaries or for the purpose of the trust; and
- (e) a trustee must exercise stewardship over the trust property for the beneficiaries or the purpose of the trust; and
- (f) a trustee must exercise the powers of a trustee for a proper purpose.

### **Commentary**

Clause 8 qualifies all duties, mandatory and default, by making it clear that the duties do not necessarily require equal treatment of beneficiaries. We have attempted to make it clear that although there is a default duty not to be unfairly partial, equal treatment is not required in order to balance competing concerns about the extent of a trustee's discretion. Clause 10 sets out the mandatory duties of a trustee that cannot be excluded and apply in every trust. This statement of the mandatory duties of a trustee is not intended to limit or alter the duties applicable at law, and is intended to restate and summarise the current legal position. Clause 10 does not apply where it is found that the settlor's overall intention was not to create a trust but some other form of relationship, in which case the contract may continue to have effect but the relationship will not be a trust. The purported exclusion of one of these duties in clause 8 may in fact be evidence that the settlor did not intend to create a trust, but some other form of relationship instead, and the certainty of intention, which is necessary for the creation of a trust, is not met (clause 5). The mandatory duties do not match exactly with those in the Financial Markets Conduct legislation, but they are likely to be complementary. Where the trust form is approaching a commercial entity, as is the case under that legislation, there are likely to be nuances in how these obligations apply and interact in practice.

### *Default duties*

## 11 What is trustee's default duty

- (1) A trustee's default duty is a duty that the trustee must perform unless it is modified or excluded by the terms of the trust or the statute under which the trust is created.

- (2) A trustee's default duty may only be modified or excluded to the extent that is consistent with the mandatory duties.
- (3) However, a trustee may depart from the default duties under **sections 19** (duty not to profit) and **20** (duty to act without reward) if all the adult beneficiaries agree.
- (4) In **subsection (3)**, **adult beneficiaries** means the beneficiaries with full legal capacity who are together absolutely entitled to the trust property.

## 12 Default duties

The default duties of a trustee are set out in **sections 13 to 23**.

## 13 Duty not to exercise power for own benefit

A trustee must not exercise a power of a trustee directly or indirectly for the trustee's own benefit.

## 14 Duty to consider exercise of power

A trustee must actively and regularly consider whether the trustee should be exercising 1 or more of the trustee's powers.

## 15 Duty not to fetter future exercise of powers

A trustee must not fetter the future exercise of the trustee's powers.

## 16 Duty to avoid conflict of interest

A trustee must avoid a position where the interests of the trustee and the interests of the beneficiaries conflict.

## 17 Duty to keep proper accounts

A trustee must maintain a statement of the trust property that—

- (a) adequately identifies the assets, liabilities, and income and expenses of the trust; and
- (b) is appropriate to the value and complexity of that property.

## 18 Duty of impartiality

A trustee must not be unfairly partial to 1 beneficiary or group of beneficiaries to the detriment of the others.

## 19 Duty not to profit

A trustee must not make a profit from the trusteeship of the trust.

## 20 Duty to act without reward

A trustee must not take any reward for acting as a trustee, but this does not affect the right of a trustee to be reimbursed for the trustee's legitimate expenses and disbursements in acting as a trustee.

## 21 Duty to act unanimously

If there is more than 1 trustee, the trustees must act unanimously.

## 22 Duty to exercise care and skill in management and administration of trust property

- (1) A trustee who exercises any power of management or administration of the trust property must do so in accordance with the standard of care set out in **section 25**.
- (2) In **subsection (1)**, a power of management or administration of the trust property—

- (a) includes a power, whether created by law or by the terms of the trust, to—
  - (i) hold trust property; and
  - (ii) maintain and develop trust property; and
  - (iii) deal with trust property; and
  - (iv) insure trust property; and
  - (v) carry on a business that is trust property; and
  - (vi) appoint an agent, nominee or custodian; and
  - (vii) appoint a delegate; and
  - (viii) any other power affecting the management or administration of trust property; but
- (b) does not include the exercise of a discretion to distribute trust property to beneficiaries.

### 23 Duty to invest prudently

- (1) When investing trust property, a trustee must invest prudently.
- (2) For the purposes of **subsection (1)**, a trustee invests prudently if the trustee complies with the standard of care set out in **section 26**.

#### Commentary

The list of default duties is intended as a non-exhaustive summary of some of the duties of trustees that apply unless and to the extent that they have not been modified by terms of trust. Further duties, rules and exceptions present in the rules of equity continue to apply. Although the duties in clauses 13 to 23 may be modified or excluded by the terms of a trust, it is not intended that they may do so to the extent that the mandatory duties would be breached. The terms of a trust may allow trustees to exercise discretion to benefit themselves, particularly if they are beneficiaries, or to be in a position where their personal interests conflict with those of other beneficiaries or with their role as a trustee. However, the terms of the trust would not be able to allow trustees to self-benefit without honestly considering the interests of other beneficiaries. Clause 11 allows the default duties to be impliedly modified. This is to account for existing trust deeds, which may not expressly modify these duties.

## Subpart 3 — Trustee's standard of care

### 24 Types of standard of care

This subpart sets out the standard of care—

- (a) for the exercise of a power of management or administration of trust property (*see section 22*); and
- (b) for investment of trust property by a trustee (*see section 23*).

### 25 Standard of care for exercise of power of management or administration of trust property

In the exercise of a power set out in **section 22(2)**, a trustee must exercise the care and skill that are reasonable in the circumstances, having regard in particular—

- (a) to any special knowledge or experience that the trustee has or holds the trustee out as having; and
- (b) if a person acts as a trustee in the course of a business or profession, to any special knowledge or experience that it is reasonable to expect of a person acting in the course of that business or profession.

**26 Standard of care for power of investment**

In the exercise of a power of investment, a trustee must exercise the care and skill that a prudent businessperson would exercise in managing the affairs of others, having regard in particular—

- (a) to any special knowledge or experience that the trustee has or holds the trustee out as having; and
- (b) if a person acts as a trustee in the course of a business or profession, to any special knowledge or experience that it is reasonable to expect of a person acting in the course of that business or profession.

Subpart 4 — Trustee exemption clauses and indemnity clauses

**27 Restriction on trustee exemption clauses**

The terms of a trust must not limit or exclude a trustee's liability for any breach of trust arising from the trustee's own dishonesty, wilful misconduct, or gross negligence.

**28 Restriction on trustee indemnity clauses**

The terms of a trust must not grant the trustee any indemnity against the trust property in respect of liability for any breach of trust arising from the trustee's own dishonesty, wilful misconduct, or gross negligence.

**29 Indemnification with agreement of beneficiaries**

- (1) A trustee may be indemnified from the trust fund for a specific exercise or non-exercise of a trustee duty, power, or function if all the adult beneficiaries agree.
- (2) In subsection (1), **adult beneficiaries** means the beneficiaries with full legal capacity who are together absolutely entitled to the trust property.

**30 Invalidity of restricted exemption clause or indemnity clause**

A clause of the terms of a trust is invalid to the extent that it purports to have the effect stated in section 27 or 28.

**31 Adviser must alert settlor to liability exclusion or indemnity clause**

- (1) This section applies where a person who is paid to advise on the terms of a trust or the drafting of a trust deed (the **adviser**) recommends the inclusion of, or includes, a liability exclusion or indemnity clause in the terms of the trust.
- (2) The adviser must, before the creation of the trust, take reasonable steps to ensure that the effective settlor is aware of the meaning and effect of the clause.
- (3) The liability exclusion or indemnity clause has no effect with respect to an adviser who is a trustee of the trust and who is in breach of subsection (2).
- (4) In this section, **liability exclusion or indemnity clause** means a clause that has the effect of—
  - (a) limiting or excluding the liability of a trustee for negligence; or
  - (b) granting a trustee an indemnity against the trust property in respect of liability for negligence.



*Relief of personal liability*

**32 Court may relieve trustee from personal liability**

- (1) If **subsection (2)** applies, the court may relieve a trustee who is or may be personally liable for any breach of trust from personal liability for the breach.
- (2) The court may relieve the trustee if it appears to the court that—
  - (a) the trustee has acted honestly and reasonably; and
  - (b) the trustee ought fairly to be excused for the breach of trust.
- (3) The court may relieve the trustee in whole or in part.

**Commentary**

Clauses 27 and 28 accept that trust deeds may legitimately seek to exempt liability or indemnify a trustee for acting negligently. These clauses relate to liability to beneficiaries for a breach of trust. The requirement in clause 31 that an adviser must take reasonable steps to ensure the settlor is aware of the meaning and effect of any exemption or indemnity clause is not intended to require that a settlor receive independent legal advice. The use of the term “effective settlor” in clause 31(2) is intended to convey the meaning of a “real” settlor, who is likely to be but not necessarily the original settlor, as opposed to a nominal or later settlor. We intend that each real settlor is advised only the first time that they settle property on to the trust. Clause 32 retains the court’s power, currently in section 73 of the Trustee Act 1956, to relieve trustees of liability for breach of trust in certain cases.

Subpart 5 — Trustees’ obligations in relation to information

*Retention of documents by trustees*

**33 Trustee must retain core documents**

Each trustee of a trust must retain, so far as is reasonable, copies of the following documents relating to the trust:

- (a) the trust deed; and
- (b) any variations made to the trust deed or trust, including variations made to the beneficiaries of the trust; and
- (c) a list of all of the assets currently held as trust property and liabilities of the trust; and
- (d) any records of trustee resolutions made during that trustee’s trusteeship; and
- (e) any written contracts entered into during that trustee’s trusteeship; and
- (f) any accounting records and financial statements prepared during that trustee’s trusteeship; and
- (g) deeds of appointment and retirement of trustees; and
- (h) any letter or memorandum of wishes from the settlor or settlors; and
- (i) any documents referred to in **paragraphs (a) to (h)** that were retained by a former trustee during that person’s trusteeship and passed on to the current trustee.

**34 Retention of documents where there is more than 1 trustee**

If there is more than 1 trustee of a trust, a trustee complies with the obligation in **section 33** if—

- (a) every trustee holds copies of the documents in **section 33(a)** and **(b)**; and
- (b) one of the trustees holds copies of the other documents in **section 33** and makes those documents available to the other trustees on request.

**35 Duration of retention of documents**

A trustee must retain, so far as is reasonable, the documents for the duration of the trustee's trusteeship.

**36 Trustee must pass on documents**

At the time that a trustee ceases to be a trustee of a trust, if the trust continues, the trustee must give at least 1 replacement trustee or continuing trustee the documents that the trustee holds at that time.

**37 Record-keeping requirements under other legislation**

Nothing in this Act affects the obligations of a trustee to keep records under other legislation.

**Commentary**

Clause 33 lists the essential documents that a trustee must retain in fulfilment of the trustee's duties. The provision makes this requirement clear for trustees. Clause 33 is not intended to imply any special status to the documents listed other than that they must be retained. In particular, this provision does not imply that a letter or memorandum of wishes is necessarily a trust document for any other purpose, including disclosure to beneficiaries. The use of the term "so far as is reasonable" is intended to account for situations where it is unduly difficult to retain the documents, for instance where documents are inadvertently lost or destroyed. It is also intended to imply that it may not be necessary for every low-level contract or account to be retained if such contracts and transactions are summarised in other documentation. Clauses 34 to 37 clarify details about the document retention obligation.

*Provision of information to beneficiaries: general obligation***38 Trustee must provide sufficient information**

A trustee must provide sufficient information to sufficient beneficiaries to enable the terms of the trust to be enforced against the trustees.

*Provision of information to beneficiaries: specific obligations***39 Definitions for purposes of sections 40 to 44**

In sections 40 to 44,—

**qualifying beneficiary** means a beneficiary whom the settlor intended to have a realistic possibility of receiving trust property under the terms of the trust

**representative** means the parent, guardian, or property manager of a beneficiary who is a minor or in respect of whom a guardian or property manager has been appointed

**trust information**—

(a) means any information—

(i) regarding the terms of the trust, the administration of the trust, or the trust property; and

(ii) that it is reasonably necessary for the beneficiary to have in order for the trust to be enforced; but

(b) does not include reasons for trustees' decisions.

**40 Presumption that trustee must notify basic trust information**

(1) There is a presumption that a trustee must, as soon as is practicable, provide every qualifying beneficiary or representative of a minor or incapable qualifying beneficiary with the information set out in **subsection (3)**.

- (2) However, the presumption does not apply if the trustee reasonably considers that the information should not be provided (to be determined by consideration of the factors set out in **section 42(2)**).
- (3) The information referred to in **subsection (1)** is—
  - (a) the fact that a person is a beneficiary of the trust in question; and
  - (b) the names and contact details of the trustees; and
  - (c) the right of the beneficiary to request a copy of the trust deed or trust information.

#### **41 Presumption that trustee must provide information on request**

- (1) There is a presumption that a trustee must within a reasonable period of time provide a beneficiary with the trust information that the beneficiary has requested.
- (2) However, the presumption does not apply if the trustee reasonably considers that the information should be withheld (to be determined by consideration of the factors set out in **section 42(2)**).

#### **42 Procedure for deciding against provision of information**

- (1) For the purposes of **sections 40** and **41**, a trustee must not decide against providing information unless the trustee has taken into account—
  - (a) the trustee's obligation under **section 38**; and
  - (b) the factors set out in **subsection (2)**.
- (2) The factors referred to in **subsection (1)(b)** are the following:
  - (a) the nature of the interests held by the beneficiary and the other beneficiaries of the trust, including the degree and extent of the beneficiary's interest in the trust or the beneficiary's likely prospects of receiving trust property in the future;
  - (b) whether the information is subject to personal or commercial confidentiality;
  - (c) the expectations and intentions of the settlor at the time of the creation of the trust as to whether the beneficiaries as a whole and the qualifying beneficiary in particular would be provided with information;
  - (d) the age and other circumstances of the beneficiary;
  - (e) the age and circumstances of the other beneficiaries of the trust;
  - (f) the effect of providing the information on the trustees, other beneficiaries of the trust, and third parties;
  - (g) in the case of a trust that is a family trust, the effect of providing the information on—
    - (i) relationships within the family;
    - (ii) the relationship between the trustees and some or all of the beneficiaries to the detriment of the beneficiaries as a whole;
  - (h) in a trust where there is a large number of beneficiaries or there are unascertainable beneficiaries, the practicality of providing information to all beneficiaries or all members of a class of beneficiaries;
  - (i) the practicality of providing some or all of the information to the beneficiary in redacted form;

- (j) the practicality of imposing restrictions and other safeguards on the use of the information (for example, by way of an undertaking, or restricting who may inspect the documents).

#### 43 Beneficiary may be required to pay cost of providing information

The trustee may require the beneficiary to whom trust information is provided under **section 41** or in accordance with the terms of the trust to pay the reasonable cost of providing that information.

#### 44 Application to court

- (1) The trustee may apply to the court for directions before deciding against providing the information under **section 40** or **41**.
- (2) A beneficiary may apply to the court for an order that the trustee supply the beneficiary with the information the beneficiary has requested.

#### Commentary

Clause 38 provides the general mandatory obligation regarding the provision of information to beneficiaries. This general obligation will not necessarily require that the trustee informs every beneficiary of the trust that they are a beneficiary. Clause 38 is the obligation which underlies the more specific presumptions in clauses 40 and 41. The terms of a trust may provide another process for notifying and informing beneficiaries, which, so long as it meets the general obligation in clause 38, will be valid. It is intended that these provisions leave open the possibility of a secret trust or a trust that directs that certain beneficiaries are not to be given information but in each case the principle that sufficient information must be provided to sufficient beneficiaries such that the trust is able to be enforced must be adhered to. We do not intend that trustees would be required to release insignificant, minor details to beneficiaries.

In deciding which beneficiaries to notify under clause 40, a trustee must determine who are "qualifying beneficiaries". This will require an exercise of discretion by the trustee but ought to be done in a way that gives broad effect to the settlor's intention and does not fetter the trustee's discretions regarding which beneficiaries receive distributions of trust property. A trustee may determine that the presumption to notify a specific beneficiary of the basic trust information does not apply or the presumption to provide the information requested by a beneficiary does not apply, but only after considering the list of factors in clause 42(2). In considering these factors, the trustee must balance the overarching principle that sufficient information must be given to sufficient beneficiaries to enable the trust to be enforced and the obligations to notify and provide information against various considerations arising from the factors listed that may indicate that information should not be given, such as the potential for harm to the trust or beneficiaries. The trustee will also need to consider the trustee's duties in exercising these discretions.

# Part 3

## TRUSTEES



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# Chapter 6

## Trustees' powers

### INTRODUCTION

- 6.1 The recommendations in this chapter remove unnecessary restrictions on powers that are in the current provisions of the Trustee Act 1956 and instead rely on the clear statements of the duties of trustees, as recommended in chapter 5, and the standard of care to guard against inappropriate use of powers by trustees. Our view is that this approach is better at making sure the default powers provisions in the new Act are sufficiently flexible and suitable to the majority of trusts. The interests of beneficiaries or the trust's purpose will be protected by the duties a trustee must adhere to in making any decision or exercising any power as trustee.
- 6.2 The administrative and distributive powers provisions discussed in this chapter are default in that they may be varied or excluded by the terms of a trust. In trust deeds settlors can give the trustees whatever powers they like to manage and distribute the trust property, although these must be exercised subject to the overriding duties on trustees and the standard of care.
- 6.3 This chapter also includes recommendations to make the age of majority for the purposes of trust law 18 years and to clarify the powers of trustees to appoint agents, nominees, custodians and delegates. Included in this chapter is a discussion on the standard of care required of trustees when exercising powers. We recommend including a default provision on the standard of care in the new Act.
- 6.4 The reform of trustees' powers was previously discussed in the *Preferred Approach Paper* and the *Fourth Issues Paper*.<sup>185</sup>

### ADMINISTRATIVE POWERS

#### RECOMMENDATION

R7 The new Trusts Act should:

- (1) Provide that a trustee has the same powers in relation to trust property that the trustee would have if the property were vested in the trustee absolutely and for the trustee's own use, that is, the trustee has the powers of a natural person.
- (2) Provide that in exercising any powers enabled under (1), the trustee is subject to the trustees' duties, the standard of care and the purpose of the trust.
- (3) Include a schedule setting out some commonly used powers of a trustee which are included in the powers enabled under (1) and stating that "for the avoidance of doubt, the powers of a trustee granted under [the general powers provision in (1)] include, but are not limited to, the following: ...". The schedule should include the power to:

185 Law Commission *Review of the Law of Trusts – Preferred Approach* (NZLC IP31, 2012) at ch 4; Law Commission *The Duties, Office and Powers of a Trustee: Review of the Law of Trusts – Fourth Issues Paper* (NZLC IP26, 2011) at ch 5.

- sell or lease trust property;
  - borrow money and create a security interest in the trust property;
  - give a guarantee;
  - seek legal, financial or other advice.
- (4) Provide that this is a default provision capable of being overridden by the terms of the trust.

### Powers of a natural person

- 6.5 The current powers provisions in the Trustee Act are lengthy, complex sections that are difficult to follow and understand. They are overridden in most trust deeds as they do not reflect modern realities and are usually more restrictive than is desired.
- 6.6 We recommend a flexible empowering provision that better allows for the variety of forms and uses of trusts. The recommendation satisfies the original intention of the current powers provisions by giving sufficiently wide powers to trustees to enable them to do all they need to do to manage trust property. While ostensibly broadening trustees' powers, the recommendation will not harm beneficiaries' interests because what trustees may do with trust property is always controlled by their duties to the beneficiaries or the purpose of the trust. Instead, broadening trustees' powers is likely to give them the ability to make better choices in how the trust property is managed.
- 6.7 The recommended provision should replace all sections of the current Trustee Act that address the administrative powers of trustees (sections 14–21, 24, 32–33 and 42A, 42B and 42D).
- 6.8 The recommendation is a change of approach in relation to the business-related powers (sections 32, 32A and 33). In the Trustee Act these provisions intentionally restrict the scope of what a trustee can do with a business by allowing a trustee only to do what is needed to wind up a testator's business and minimise the risk to the trust. In particular, section 32, which provides the default power to carry on business, applies only to testamentary trusts, and generally applies only for two years. The recommendation to give the trustee the same powers as a natural person, including powers in relation to a business, is more likely to accord with modern practice where many trusts are established in order to run businesses and trustees need broad, flexible powers relating to trust businesses.
- 6.9 The introduction of the broad empowering provision was favoured by all submitters commenting on this proposal in the *Preferred Approach Paper* because it simplifies and modernises trust law and accords with common practice in deed drafting. One submitter commented on the need to emphasise that such a provision did not allow trustees to act outside of a proper purpose. We agree that the broad empowerment of trustees as recommended should not imply that trustees have the authority to do whatever they like even if they do have this capacity. The improper use of powers would be open to challenge as a breach of trust.

### Schedule of powers

- 6.10 The Commission's view is that a schedule of powers should be included as it would allay any concern that the new approach is less clear than specific powers provisions. The list of powers to be included in the schedule under R7(3) should be limited to those powers where there could be confusion or uncertainty as to whether a trustee is entitled to act in certain circumstances, rather than attempting to be a complete list. The schedule would make it explicit

to third parties dealing with trustees, for instance banks lending to trustees, that the trustees have the requisite powers. While a significant majority of submitters favoured the inclusion of a schedule of powers included within the general power, a few considered that the schedule was unnecessary and would over-complicate the law in this area. In response to these concerns our recommendation is that the schedule should not attempt to outline every power of a trustee or even all of those currently covered by the Trustee Act, which would make it complex and detailed. Instead it will focus on the powers that are likely to be of particular significance or subject to uncertainty.

## POWERS OF MAINTENANCE OF AND ADVANCEMENT TO BENEFICIARIES

### RECOMMENDATION

R8 The new Trusts Act should:

- (1) Re-enact section 40 of the Trustee Act 1956 in modernised form with the following reforms:
  - (a) defining the phrase "maintenance, education, advancement or benefit" in the legislation in a way that ensures they are interpreted broadly and include the concepts of "comfort" and "wellbeing";
  - (b) removing the current test for the exercise of power in section 40(1)(a): "as may, in all the circumstances, be reasonable"; and
  - (c) removing the requirement in section 40(1)(a)(i) to take into account other trust funds to which a beneficiary may have access.
- (2) Re-enact section 41 of the Trustee Act 1956 in modernised form with the following reforms:
  - (a) defining the phrase "maintenance, education, advancement or benefit" as in (1)(a) above;
  - (b) removing the limits on the amount of the advancement; and
  - (c) clarifying that those who hold contingent interests under a double or multiple contingency are not eligible.
- (3) Provide that this is a default provision capable of being overridden by the terms of the trust.

### Distribution for advancement, education, maintenance or benefit

- 6.11 Current sections 40 and 41 of the Trustee Act, which empower trustees in private trusts to distribute to beneficiaries outside of the explicit distribution requirements in a trust deed for the beneficiary's advancement, education, maintenance or benefit, are overly complex and restrictive. The requirements in section 40 to apply an objective "reasonableness" test and to consider other trust funds that may provide for a beneficiary, and in section 41 to limit the amount that may be advanced to a beneficiary to the greater of \$7,500 or half of the beneficiary's total share, are often overridden in trust deeds.
- 6.12 We are satisfied that the recommendations remove confusion and uncertainty from the current default provision. All submitters commenting on the proposals in the *Preferred Approach Paper*



were supportive of the approach taken.<sup>186</sup> It is desirable to retain the current terms “maintenance, education, advancement or benefit” because their meaning is settled and a change could bring unnecessary uncertainty. The courts have interpreted these terms broadly to encompass payments that enhance a beneficiary’s comfort and wellbeing. One submitter was concerned that defining these terms broadly and explicitly and including the concepts of “comfort” and “wellbeing” would risk abandoning current guidelines when the meaning is certain. We consider that using the same words as the current provision will ensure that courts do rely upon current interpretations. Defining the terms will simply add clarity for those less familiar with the body of current case law.

- 6.13 The New Zealand Law Society commented that the current mix of a subjective test (“at his sole discretion”) and an objective test (“as may, in the circumstances, be reasonable”) in section 40(1)(a) results in confusion and is difficult for trustees to apply. We agree that the objective test unhelpfully limits trustees’ discretion and should be removed. This is in line with our general approach of removing restrictions on trustees’ discretion in the default provisions and relying on clear trustees’ duties and a standard of care to regulate the exercise of trustees’ powers.
- 6.14 The same principle applies to the requirement in the proviso to section 40(1) that where the trustee has notice of another trust fund from which a minor beneficiary may benefit, the trustee should apportion the payment to this beneficiary accordingly. We consider that it should be removed because it is a significant fetter on trustees’ discretion, and is impractical and potentially costly to carry out in practice. It is almost always overridden in trust deeds.
- 6.15 We intend that sections 40 and 41 are rewritten in modernised form and that aspects of the provisions that are not discussed in this chapter are continued in the new Act. For instance, section 41(c) preserves the rights of life and other interest beneficiaries where the application of capital for maintenance may prejudice their interests.

## AGE OF MAJORITY

### RECOMMENDATION

- R9 The new Trusts Act should:
- (1) Set the age of majority for the purposes of the Trusts Act and trust law generally (including wills) at 18 years.
  - (2) Clarify that the Age of Majority Act 1970 does not apply.

### A shift to 18 years

- 6.16 This recommendation brings trust law into line with other legislation, such as the Minors’ Contracts Act 1969, the Care of Children Act 2004 and the Wills Act 2007. Under New Zealand law an 18 year old has the same legal capacity and the same capability as a 20 year old for most purposes. It would be discriminatory to leave the age of majority under the trusts statute at 20 years as there is no objectively assessable reason for distinguishing between 18 and 20 year olds in this context.
- 6.17 Nearly all submitters commenting on this issue supported the proposal. Several were concerned that many 18 year olds may not have sufficient maturity for it to be desirable for them to receive

<sup>186</sup> *Preferred Approach Paper*, above n 185, at P12 and P13.

trust property and have the rights of an adult beneficiary. However, we are not convinced that departing from the now generally accepted age of adulthood can be justified in this context. Settlers will always be free to set terms of trust that provide an alternative age for when beneficiaries receive property.

- 6.18 The recommendation means that for the purposes of trust law the age a child or minor becomes an adult is 18 years. New wording would replace terms such as “full age”, “infant” and “infancy” which imply an age of majority of 20 years.<sup>187</sup> The reform would not alter the ability for a trust deed to set the terms relating to age for that trust.

## POWER TO APPOINT AGENTS, NOMINEES AND CUSTODIANS

### RECOMMENDATION

R10 The new Trusts Act should adopt the approach taken in section 5 of the Select Committee version of the Trustee Amendment Bill 2007, which proposed new sections 29–29E to replace section 29 of the Trustee Act 1956, with amendments. The redrafted provision in the new Act should:

- (1) Allow a trustee to employ an agent to exercise or perform a trustee’s “administrative functions”. “Administrative functions” should be defined as any power, right or function other than a “trustee function”, that is necessary or desirable to exercise or perform in executing the trust, administering any asset of, or property that is subject to, the trust, or both. The provision would define a “trustee function” as any of the following powers, rights or functions vested in the trustee:
  - (a) a function related to a decision regarding the distribution, use, possession, or other beneficial enjoyment of trust property;
  - (b) a power to decide whether any fees should be paid or other payment should be made out of income or capital;
  - (c) a power to decide whether payments received should be appropriated to income or capital;
  - (d) a power to appoint a person to be, or to remove, a trustee of the trust;
  - (e) a power of appointment (including a power to appoint a person to be, or to remove, a beneficiary);
  - (f) a power to appoint or change the distribution date of trust funds;
  - (g) a power to resettle the trust, or to amend, revoke, or revoke and replace terms or provisions of a trust deed;
  - (h) a right conferred by this Act to apply to the court; and
  - (i) the power to authorise an agent to perform any of the functions of the trustees or trustee.
- (2) Require trustees to keep under review the agency arrangements and the way the arrangements are being put into effect, to consider whether to intervene, and to intervene if necessary. In reviewing the agency and actions of the agent, the trustee

<sup>187</sup> Age of Majority Act 1970, s 4.

must consider whether a trustee exercising the standard of care (R13) would intervene and must do so if such a trustee would consider it necessary.

- (3) Provide that trustees are not liable to a beneficiary for the acts or defaults of an agent, unless the trustee failed to meet the duty of good faith and honesty (R2(1)(c)) and standard of care (R13) in making the appointment, or the trustee failed to review the agency and agent's actions, or the trustee's actions to intervene did not comply with the duty of good faith and honesty and standard of care.
- (4) Require that the authorisation of an agent is in writing, is given or delivered to the agent and may be subject to conditions.
- (5) Allow the trustee to pay the agent a reasonable fee for the agent's services.
- (6) Not include the list of example professionals that may be appointed as agents as was proposed for new section 29(1)(a) of the Trustee Act 1956 in the Trustee Amendment Bill 2007.
- (7) Add the following non-exhaustive criteria that a trustee must consider when appointing an agent:
  - whether the intended agent has the appropriate skills, expertise and experience to carry out the task; and
  - the fees the intended agent will charge and whether employing the agent is a cost-effective option.
- (8) Provide that R10 is a default provision capable of being overridden by the terms of the trust.

R11 The new Trusts Act should include a power to appoint nominees and custodians of trust property and apply the same framework as will apply to agents under R10(2)–(5) and (8), including:

- (a) a power for trustees to appoint a person to act as the trustee's nominee in relation to some or all of the trust property and to vest that property in the nominee;
- (b) a power for trustees to appoint a person to act as custodian in relation to some or all of the trust property whereby that person undertakes the safe custody of the property or of any documents or records relating to the property;
- (c) a nominee or custodian must be either:
  - (i) a person who carries on a business that consists of or includes acting as a nominee or custodian;
  - (ii) a body corporate that is controlled by the trustee; or
  - (iii) an incorporated law practice;
- (d) the requirement on trustees to keep the arrangement under review (R10(2)), the provision restricting the trustee's liability (R10(3)), the requirement that the appointment is made in writing (R10(4)) and the power to pay a reasonable fee (R10(5)); and
- (e) that the provision is capable of being overridden by the terms of the trust.

## Power to appoint an agent

6.19 Despite the recommendation that trustees have all of the powers of a natural person in relation to trust property and that this would include power to appoint an agent, we think it necessary to include a provision giving specific power to appoint an agent. These sections empower a trustee to appoint an agent as a default power that is capable of being overridden by the terms of a trust, and clarify that this is not in conflict with the duties of trustees to exercise stewardship and to actively and regularly consider the exercise of trustees' powers.<sup>188</sup>

## Trustee Amendment Bill 2007

6.20 The Trustee Amendment Bill 2007 contained proposed changes to section 29 of the Trustee Act, which authorised trustees to employ agents to transact trust business or do anything required in executing the trust or administering trust property. The reforms proposed in the Bill were intended to:

- clarify the functions that an agent can be employed to carry out;
- require the trustee to keep the arrangement under review, consider whether to intervene and intervene if necessary; and
- clarify that the trustee would not be liable for the agent's actions unless the appointment was not made in good faith or with reasonable care, diligence and skill, or the trustee failed to review the agency or the intervention was not in good faith.

## Our recommendations

6.21 We agree with the policy of the proposed reforms included in the 2007 Bill and recommend only minor adjustments to aid clarity and to tie in to the duties of trustees that will be included elsewhere in the new Act. The only significant alteration from the Bill's approach that we propose is to include a non-exhaustive list of factors for a trustee to take into account in appointing an agent. We consider that this will help trustees to appoint appropriate agents and to better meet their duties under the new Trusts Act. It will provide greater guidance to trustees than the law does currently. Submitters were supportive of the proposal.

6.22 The New Zealand Law Society previously raised the concern that the provisions on the payment of fees and charges in the Bill were too prescriptive. The wording of the 2007 Bill could be considered overly complicated. In our view, a simplified provision allowing the trustee to pay the agent a reasonable fee for the agent's services is sufficient.

## Nominees and custodians

6.23 We have included an additional recommendation to give trustees the power to appoint nominees and custodians. These forms of property holding are already in use in New Zealand, particularly for investment purposes, and are covered in the Trustee Act in relation to some specific uses.<sup>189</sup> Nominees and custodians can be seen as a special category of agents, but because they may hold the legal title to the trust property and so need express authority, we consider that

188 It has been held that if a trustee places trust property in the hands of a third party without the power to do so, the trustee commits a breach of trust: *Browne v Butter* (1857) 24 Beav 159, 53 ER 317.

189 Trustee Act 1956, s 13I (requiring a trustee other than a trustee corporation, to deposit bearer securities with a bank for safe custody), s 26 (allowing a trustee to deposit any documents relating to the trust or trust property with a bank or professional custodian for safe custody), s 29(3)(a) (allowing a trustee to appoint a solicitor as agent and can permit the solicitor to have the custody of transactional documents), s 29(3)(c) (allowing a trustee to appoint a bank or solicitor as agent to receive insurance proceeds and may allow the agent the custody of the insurance policy) and s 14(2B)(b) (providing trustees may appoint a nominee as the party to any occupation arrangement entered into to provide accommodation for a person).

it is helpful to spell out this power.<sup>190</sup> The restrictions and safeguards for these powers regarding reviewing the arrangement, liability of trustees, and fees should mirror those used for the power to appoint agents. Additional safeguards that should apply to nominees and custodians should include: that the appointment must be in writing; and that the custodian and nominee must either carry on business of acting as nominee or custodian, be a body corporate controlled by the trustees, or be an incorporated law practice. The second of these is for the purpose of limiting who can carry out these roles to those who are providing professional services and who would engage the financial services regulation if the trust property held consists of financial instruments.<sup>191</sup> These provisions are based on provisions regarding agents, nominees and custodians in the Trustee Act 2000 (UK),<sup>192</sup> which were introduced after a review by the Law Commission for England and Wales.<sup>193</sup>

## POWER TO DELEGATE

### RECOMMENDATION

- R12 The new Trusts Act should, as a default position, allow a trustee, by power of attorney, to delegate the execution of all or any of the trustee's powers, duties and discretions (that the trustee either holds as a sole trustee or jointly with another person). The provision should:
- (1) Add temporary mental incapacity to absence from New Zealand and temporary physical incapability as the circumstances in which the power of delegation can be exercised.
  - (2) State that the delegation:
    - (a) commences as provided by the instrument creating the power or, if the instrument does not provide for the commencement of the delegation, on the date of the execution of the instrument by the trustee; and
    - (b) continues for 12 months or any shorter period provided by the instrument, with one extension by the delegating trustee of up to an additional 12 months.
  - (3) Require a trustee delegating the powers (or the delegate, where the trustee is incapable of doing so) to, within seven days of the instrument of delegation taking effect, notify any co-trustees and any person with a power to appoint and remove trustees of:
    - (a) the date on which the delegation comes into effect;
    - (b) the duration of the delegation;
    - (c) the identity of the delegate;
    - (d) the reason for the delegation; and
    - (e) which powers, duties and discretions are delegated, where only some are delegated.

190 The Law Commission (England and Wales) and Scottish Law Commission *Trustees' Powers and Duties* (Law Com No 260 Scot Law Com No 172, 1999) at sch 2 notes the following common law issues that may restrict trustees from appointing nominees and custodians:

- a. The trustee is under a duty to take such steps as are reasonable to secure control of trust property and keep control of it;
- b. Title to trust property is to be vested in joint names of trustees so that it can only be transferred with the consent of all the trustees;
- c. It is permissible for trust property documents to be in the custody of just one trustee (but not the property itself).

191 In England and Wales, s 19(2) of the Trustee Act 2000 limits nominees and custodians to these providers and thereby engages the Financial Services Act 1986. In New Zealand, the equivalent of this would be the Financial Services Providers (Registration and Dispute Resolution) Act 2008.

192 Trustee Act 2000 (UK), pt IV.

193 *Fourth Issues Paper*, above n 185.

- (4) Require sole trustees who are delegating to notify any person with the power to appoint and remove beneficiaries, or if none, all competent adult beneficiaries, or where that is unreasonable or impractical in the circumstances, a reasonably representative sample of beneficiaries.
- (5) Require notification, as specified in (3), each time an instrument of delegation takes effect.
- (6) The failure to notify would be considered a breach of trust, but would not, in favour of a person dealing with the delegate, invalidate any act done or instrument executed by the delegate.
- (7) Retain the current position that trustees are only liable to beneficiaries for the actions or default of a delegate if the trustees did not exercise the duty of good faith and honesty (R2(1)(c)) and the standard of care (R13) in the appointment of the delegate.
- (8) Clarify that the default position is that a delegate may exercise the power to resign on behalf of a trustee who has delegated the trustee's powers.
- (9) Retain the current position of allowing delegation to a sole co-trustee only if that co-trustee is a statutory trustee corporation.
- (10) Allow for a co-trustee or a beneficiary to apply to the Public Trust for the Public Trust to consent to become the delegate for a trustee who is unable or unavailable to make a decision, and cannot be contacted for any reason, and there is no delegation in place.

### Delegation under the Trustee Act

- 6.24 A delegation under section 31 of the Trustee Act enables the substitution of a trustee by another person who can take over their duties, powers and discretions where the trustee is leaving or is about to leave New Zealand, or expects to be absent from New Zealand from time to time, or is or may become temporarily incapable of performing his or her duties on account of physical infirmity. Unlike an agent under section 29, who can only fulfil certain powers of the trustee, a delegate can take the trustee's place in exercising all of the trustee's duties, powers and discretions.

### Reforms to power to delegate

- 6.25 We proposed in the *Preferred Approach Paper* to expand the circumstances in which a delegation can apply to include temporary mental incapacity, to limit the duration of a delegation to 12 months with the possibility of a further 12 month extension, to introduce a notification requirement and to allow the Public Trust to become a delegate for a trustee who is unavailable to make a decision.<sup>194</sup> These reforms expand the circumstances when the default power to delegate may be useful, while limiting delegation to temporary situations where it is appropriate. The reforms provide protection for beneficiaries by ensuring that others know about the delegation.
- 6.26 We favoured retaining the current position with regard to a trustee's liability to the beneficiaries for the delegate's actions and defaults. It is fair to the trustee to limit liability to when they have not exercised good faith and reasonable care in the exercise of a delegation as the trustee cannot easily do more than this when they are in the circumstances that allow a delegation.

<sup>194</sup> *Preferred Approach Paper*, above n 185, at P16.

We are unaware of any problems with this approach to the trustee's liability currently. We also proposed a continuation of the current position with regard to delegation to sole co-trustees when they are statutory trustee corporations and delegation by sole trustees because they are both the most practical options.<sup>195</sup>

### Changes from *Preferred Approach* proposals

- 6.27 The proposals in the *Preferred Approach Paper* were generally well received by submitters. However, there was considerable comment from submitters regarding the details of the proposals, which have now been given further consideration.
- 6.28 The comment was made that having a default delegation provision is incongruous with a default duty of trustees to act personally, as had been expressed in the *Preferred Approach Paper*. We have adjusted the wording of the default duty recommendation by stating that the default duties can be altered by statute to address this (R2(1)). There was also concern that beneficiaries could be left in a position of having no redress. However, delegates cannot exclude liabilities to any greater extent than trustees and would have the same responsibility and liability as trustees.
- 6.29 Some submitters were concerned about the effect of the proposals with regard to duration and notification where an instrument of delegation is executed but would only take effect when the circumstances in which delegation is allowed exist. We understand that this is a fairly common way of setting up delegations. It is a sensible way for trustees to protect against unforeseen circumstances that prevent them from carrying out their role. We would not want new legislation to prevent or inhibit this where the instrument of delegation is executed more than 12 months in advance of delegation or because notification did not occur when the instrument was executed. The new legislation should take account of this type of delegation instrument. Our recommendation uses wording similar to that in section 25 of the Trustee Act 1925 (UK). This means that the rules regarding duration and notification take effect only once a delegation takes effect and each time that instrument takes effect.
- 6.30 Several submitters have questioned the current position with regard to whether a trustee may delegate to their only co-trustee. At present such a delegation may only occur where the co-trustee is a statutory trustee corporation. It has been suggested that it should be possible to delegate to a sole co-trustee if that trustee is any corporation. We are not recommending a change to this position at present, but this may be something that will be reconsidered by the Commission in the corporate trustee review.
- 6.31 Submitters favoured the introduction of a notification requirement when the power to delegate is exercised. However, some have suggested that the settlor has a right to be notified. We do not think that it is necessary for a trustee to notify the settlor of a delegation because the purpose of the delegation is to ensure that the trust can continue to be enforced, a role that is carried out by the beneficiaries rather than the settlor. Other submitters questioned the way of determining which beneficiaries should be notified when a sole trustee delegates if there are no persons with the power to appoint and remove trustees. We proposed that competent adult beneficiaries or a reasonably representative sample of beneficiaries should be notified. It was suggested that the former may no longer have an ongoing role with the trust and that the latter was too vague a category to be useful. The purpose of the proposed requirement was to ensure that at least somebody knows when a sole trustee's role has been delegated to another. We do think there is a legitimate concern that the notification requirement could be overly onerous, so we have added the proviso that only what is reasonable in the circumstances is required. It was pointed out that there may be a problem when a trustee is incapacitated and unable to carry out the notification

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195 At P16.

requirement. To address this situation we now recommend that the delegate be required to do the notification.

- 6.32 Some submitters questioned whether the Public Trust should have the role of being the delegate when a trustee is unable or unavailable to make a decision. However, we are comfortable that the Public Trust is an appropriate body to have this role. This type of role is clearly akin to the types of statutory roles that the Public Trust already has under other legislation. We discuss the roles of the Public Trust more generally in chapter 15.

## STANDARD OF CARE

### RECOMMENDATION

R13 The new Trusts Act should:

(1) Provide that, when exercising a power of administration, including a power to:

- hold trust property;
- maintain and develop trust property;
- deal with trust property;
- transfer trust property to any person;
- insure trust property;
- carry on a business;
- appoint an agent, nominee or custodian;
- appoint a delegate; and
- any other power affecting the administration of trust property,

a trustee must exercise such care and skill as is reasonable in the circumstances, having regard in particular –

- (a) to any special knowledge or experience that the trustee has or holds himself or herself out as having; and
  - (b) if a person acts as a trustee in the course of a business or profession, to any special knowledge or experience that it is reasonable to expect of a person acting in the course of that kind of business or profession.
- (2) The standard of care does not apply to the exercise of a discretion to distribute trust property.
- (3) The standard of care does not apply if or in so far as it appears from the terms of the trust that the duty is not meant to apply.

### Standard of care when exercising a power of administration

- 6.33 An important objective of this project has been to rectify the limitations of the default powers that trustees have under the current law where there is no express provision in the terms of the trust. The current default position does not give trustees sufficient powers to administer trusts effectively. Earlier in this chapter we recommended giving trustees the powers of a natural person, unless the terms of a trust state otherwise. Yet, with the much broader empowerment



of trustees in this way, there is a need to impose safeguards and make clear the obligations that ensure trustees act properly in exercising their powers.<sup>196</sup>

- 6.34 The mandatory and default duties provide a degree of balance to guide the exercise of a trustee's powers, but we consider that the standard of care is also an essential element to the framework of obligations on trustees. The standard of care directly addresses how the trustee's powers are exercised. As with the duties of trustees, we recommend a general standard of care provision so that trustees have a clear and accessible statement of the standard of conduct expected of them.
- 6.35 The standard of care provision is not intended to detract from the duties of trustees, which are their primary obligations. The standard of care does not impact upon whether and how a trustee chooses to exercise discretion, but once a trustee chooses to exercise a power, the standard of care directs the manner in which the trustee must exercise it.
- 6.36 The standard of care is already a part of the legal framework for trusts in case law. It is not generally thought to be in itself fiduciary in nature,<sup>197</sup> and is excludable under the terms of a trust. In the specific context of investment, a higher standard of care is already included in the Trustee Act.<sup>198</sup> We propose in chapter 7 that the higher standard of care continues to apply to investment.

### Changes from *Preferred Approach Paper*

- 6.37 We recommend a standard of care based on the wording of the Trustee Act 2000 (UK). We have altered the wording relating to professional trustees from that proposed in the *Preferred Approach Paper* to directly reflect the United Kingdom's wording.<sup>199</sup> This framing of the standard of care accurately represents the existing case law position, so we do not consider that there is a significant risk that this provision will discourage professional trustees from offering their services. Any trustee that has knowledge or expertise will be held to a standard of care that takes into account this knowledge or expertise.
- 6.38 Our previous proposals related the standard of care closely to the duties, but feedback indicated that such an extension was confusing. Applying the standard of care only to the exercise of powers achieves clarity.
- 6.39 In the recommendation, and in clause 25 of the indicative draft, we have attempted to be more specific about when the standard of care is applicable, and when it is not, such as when it does not make sense for the standard to apply in a context (for instance, in relation to the discretion to distribute property to beneficiaries). The point was made that the standard of care should not apply to the exercise of discretions that affect beneficiaries' interests. Trustees are often given broad discretions in the terms of a trust about which decisions they may come to regarding the distribution of trust property to beneficiaries. Applying the standard of care in that context could open those discretions up to scrutiny as to whether the decision itself was reasonable, which is something that the settlors who gave those trustees the broad discretions would never have intended. It is the manner of how trustees carry out their powers, rather than what they decide to do in exercise of their discretions, that is relevant to the standard of care.

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196 The Law Commission for England and Wales addressed the need for this balance when it recommended a general statutory duty of care, which was introduced in the Trustee Act 2000 (UK), s 1: *Trustees' Powers and Duties*, above n 190, at [3.10].

197 *Wilden Pty Ltd v Green* [2005] WASC 83 at [499]; *Spread Trustee Company Ltd v Hutcheson & Ors (Guernsey)* [2011] UKPC 13, [2012] 2 AC 194 at [60]; *Bank of New Zealand v New Zealand Guardian Trust Co Ltd* [1999] 1 NZLR 664 (CA). However some Australian commentators have contended that a trustee's duty of care is a fiduciary duty (Anthony Goldfinch "Trustee's Duty to Exercise Reasonable Care: Fiduciary Duty?" (2004) 78 ALR 678; GE Dal Pont "The Exclusion of Liability for Trustee Fraud" (1998) 6 APLJ 41).

198 Trustee Act 1956, s 13B.

199 *Preferred Approach Paper*, above n 185, at P5(1)(b).

- 6.40 We have also altered the recommendation so that it calls this obligation a “standard of care” rather than a “duty of care”, to avoid confusion with the trustee’s duties, which apply generally to all actions and functions of a trustee.
- 6.41 A submission on behalf of the Auckland Energy Consumer Trust, and supported by Energy Trusts of New Zealand Inc and a number of other energy trusts, expressed concern that the duties proposals in the *Preferred Approach Paper* may override its own standard of care provision in its trust deed. Because the standard of care in our recommendations is a default provision, it will not override specific provisions in those trust deeds.

## APPLICATION TO EXISTING TRUSTS

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- 6.42 The recommendations in R7 and R8 relating to administrative powers and the powers of maintenance and advancement should apply to all new trusts from the date of enactment and to all trusts established before that date two years after the date of enactment. The two year transition period is to allow trust deeds to be varied in order to update the provision of powers to trustees. The alteration to the default position means that all trustees will have the powers of a natural person except where this is modified in the terms of a trust. There may be some trusts that rely on the more restrictive powers of trustees in the current Act and there ought to be opportunity for the terms of trust to be varied where it is considered that trustees’ powers should continue to be restricted.
- 6.43 The remaining recommendations should apply to all trusts from the date of enactment. We considered whether a different approach should apply to the change to the age of majority (R9) as it may alter the age at which beneficiaries in some trusts receive trust property if they rely on a reference to the “age of majority”. We have come to the view that the principled approach is that if reference is made to the age of majority and that age is changed, the new age should apply, as this best meets the settlor’s express intention in choosing that wording in the terms of the trust. The provisions on the powers to appoint agents (R10), nominees and custodians (R11), and delegates (R12) can apply to all trusts but would not apply to arrangements that are already in place, for instance agents, nominees, custodians or delegates currently exercising these roles.
- 6.44 The standard of care (R13) can apply to all trusts from the date of enactment as it represents the existing legal position. It will not alter trustees’ obligations.

## INDICATIVE DRAFT PROVISIONS – STANDARD OF CARE

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### Subpart 2 - Duties of trustee

#### *Default duties*

- 22 Duty to exercise care and skill in management and administration of trust property
- (1) A trustee who exercises any power of management or administration of the trust property must do so in accordance with the standard of care set out in section 25.
- (2) In subsection (1), a power of management or administration of the trust property—
- (a) includes a power, whether created by law or by the terms of the trust, to—
- (i) hold trust property; and
- (ii) maintain and develop trust property; and

- (iii) deal with trust property; and
- (iv) insure trust property; and
- (v) carry on a business that is trust property; and
- (vi) appoint an agent; and
- (vii) appoint a delegate; and
- (viii) any other power affecting the management or administration of trust property; but

(b) does not include the exercise of a discretion to distribute trust property to beneficiaries.

**25 Standard of care for exercise of power of management or administration of trust property**

In the exercise of a power set out in **section 22(2)**, a trustee must exercise the care and skill that are reasonable in the circumstances, having regard in particular—

- (a) to any special knowledge or experience that the trustee has or holds the trustee out as having; and
- (b) if a person acts as a trustee in the course of a business or profession, to any special knowledge or experience that it is reasonable to expect of a person acting in the course of that business or profession.

**Commentary**

The wording of the standard of care in clause 25 is based upon the Trustee Act 2000 (UK), which appears to be a well-accepted framing of the common law duty of care and has been used in draft trusts legislation in other common law jurisdictions. It can be modified or excluded by the terms of the trust. It emphasises that a higher standard of care is expected of professional trustees, which is described as those acting as a trustee in the course of a business or profession. It is intended that trustees will be held to a standard of care that is commensurate with their special knowledge, experience or professional status, and regardless of whether or not they are paid.

# Chapter 7

## Investment

### INTRODUCTION

- 7.1 In this chapter we recommend some minor changes to the current provisions on investment in Part 2 of the Trustee Act 1956. We also recommend more significant reforms to:
- the distinction between capital and income;
  - the apportionment of receipts and outgoings; and
  - the use of investment managers.
- 7.2 These were discussed more extensively in the *Preferred Approach Paper* and the *Fourth Issues Paper*.<sup>200</sup>

### POWERS AND DUTIES

#### RECOMMENDATION

- R14 (1) The new Trusts Act should provide that:
- (a) a trustee should have the power to invest any trust funds in any property;
  - (b) the power of a trustee to invest in any property set out in (a) above should apply only to the extent that it is not overridden or excluded by the terms of the trust or the terms of the trust do not otherwise limit or modify it; and
  - (c) when exercising the power to invest in property a trustee should comply with any relevant requirements contained in the terms of the trust, including any requirement relating to obtaining consent or compliance with any direction with respect to the investment of the trust fund.
- (2) The new Act should provide that:
- (a) when investing a trustee should have a duty to exercise the care, diligence, and skill that a prudent person of business would exercise in managing the affairs of others;
  - (b) where a trustee has any special knowledge or experience or holds him or herself out as having special knowledge or experience, the trustee should have a duty to exercise the level of care, diligence, and skill that it is reasonable to expect of a person with that special knowledge or experience; and
  - (c) the duties in (a) and (b) apply to a trustee to the extent that they are not excluded or modified, explicitly or implicitly, by the terms of the trust.

200 Law Commission *Review of the Law of Trusts – Preferred Approach* (NZLC IP31, 2012) at ch 5; Law Commission *The Duties, Office and Powers of a Trustee: Review of the Law of Trusts – Fourth Issues Paper* (NZLC IP26, 2011) at [5.18]–[5.37].

- (3) The new Act should make it clear that the power to invest in property and the duty to do so prudently do not of themselves preclude trustees from taking account of other relevant matters when determining how to manage trust funds, or from purchasing or retaining property for purposes other than investment, where this is appropriate to give effect to the objectives or purpose of a trust.
- (4) The powers and duties set out in R14(1) and (2) above should replace sections 13A–13D and sections 13F–13H of the Trustee Act 1956.
- (5) Section 13E of the Trustee Act 1956 (which lists the matters trustees may have regard to when investing) should be re-enacted in the new Act. It should be redrafted to provide that trustees may take into account their overall investment strategy when exercising their powers of investment (as well as the other matters currently listed).
- (6) Section 13M of the Trustee Act 1956 (which lists a number of matters the courts may take into account when considering whether a trustee should be liable for breach of trust in respect of an investment) should be re-enacted in the new Act.
- (7) Section 13Q of the Trustee Act 1956 (which provides that in an action for breach of trust the court may set off a loss arising from an investment against a gain from any other investment) should be re-enacted in the new Act. For the avoidance of doubt, the new Act should clarify that the rule of general trust law that requires the assessment of the decisions of a trustee on an investment by investment basis if the decisions are called into question (the anti-netting rule) is abolished.
- (8) Sections 13I, 13J, 13K, 13L, 13N, 13O and 13P of the Trustee Act 1956 should not be re-enacted because these provisions are now unnecessary.

### Maintaining the status quo

- 7.3 The Commission's recommendations in this area do not significantly change the current position in respect of the breadth of the power to invest and the duties governing investment.
- 7.4 Part 2 of the Trustee Act currently provides that a trustee may invest in any property<sup>201</sup> but must exercise the care, diligence, and skill that a prudent person of business would exercise in managing the affairs of others when investing.<sup>202</sup> If the trustee's profession, employment or business involves acting as a trustee or investing money for others, the trustee must exercise the level of care, diligence and skill of a person engaged in that profession, employment or business.<sup>203</sup> A professional trustee thus has to meet a higher standard. The current position is that the duty of a trustee to invest prudently (in section 13B) and the duty of a professional to exercise the level of care and skill of a person engaged in their profession (in section 13C) apply, subject to any contrary intention expressed in the trust instrument (section 13D).
- 7.5 Section 13G imposes a duty on the trustee to comply with any requirement imposed on investment by the terms of the trust, including any requirement relating to obtaining any consents or requiring compliance with any directions with respect to investment of trust funds. Section 13E sets out a non-exhaustive list of factors a trustee may have regard to when investing, including diversification, maintenance of the real value of capital and income, capital appreciation, and inflation. Finally, section 13F preserves the rules and principles of law that

201 Trustee Act 1956, s 13A.

202 Trustee Act 1956, s 13B.

203 Trustee Act 1956, s 13C.

impose duties on trustees, including the duty to act in the best interests of present and future beneficiaries, the duty of impartiality, and the duty to take advice. These apply to the exercise of investment powers subject to any contrary intention expressed in the terms of the trust.

- 7.6 As already noted, the Commission recommends preserving the current position in this area. We do not favour any substantive changes to these provisions (sections 13A–13G). This is the approach we intended in the *Preferred Approach Paper*,<sup>204</sup> but we did not clearly state that the duty to invest was a default duty so was subject to modification by the trust instrument. Some submitters were uncertain as to whether the duty to invest prudently and the higher duty of care and skill imposed on professional trustees would still be able to be modified by the terms of the trust instrument. The recommendations in this Report now make this clear. The duty to invest prudently and the duty of certain trustees to exercise special skill will apply to a trustee if and only so far as a contrary intention is not expressed in the trust instrument. We have also spelt out how the mandatory and default duties discussed in chapter 5 apply to powers of investment.
- 7.7 In response to a concern raised in submissions, the recommendation also now states that when exercising any power of investment, a trustee must comply with any requirements of the trust deed, including any requirement relating to the obtaining of consent or compliance with any direction with respect to investment of trust funds.

### Clarifications and amendments

- 7.8 The Commission recommends a few changes to other provisions currently in Part 2 of the Trustee Act. These changes address existing uncertainty or deal with specific, relatively contained issues. A number of the existing provisions are also largely historic and are no longer necessary.
- 7.9 The current provisions do not make it sufficiently clear that the power to invest does not preclude trustees from purchasing or retaining property for purposes other than investment, where this is appropriate to give effect to the objectives of a trust. In respect of Māori land under Te Ture Whenua Maori Act 1993, the primary role of the trustees may be to retain and protect land assets and taonga Māori for future generations. The purpose of other trusts may include providing a home for a beneficiary. In practice, to ensure that trustees are able to purchase property for the use and enjoyment of beneficiaries without considering the test for prudent investment, many trust deeds already specify this power. It would be helpful if the new Act was clear that trustees may take account of other relevant matters without needing to meet the standard of prudence that applies to investments. We recommend that the new Trusts Act be drafted in a manner that makes it clear that trustees can do this.
- 7.10 Section 13C of the Trustee Act requires professional trustees to meet a higher standard of prudence. Submitters raised questions over who is a professional trustee for the purposes of the section. We have recommended that the higher standard should apply where a trustee has special knowledge or experience or holds him or herself out as having special knowledge or experience. In these circumstances the trustee should be required to exercise the level of care, diligence and skill reasonably expected of a person with that special knowledge or experience. Also, where a person acts as a trustee in the course of a business or profession, it is reasonable to expect a person in that business or profession to have special knowledge or experience. This is the same approach we have taken to the higher standard of the care imposed on professionals who accept office as trustee (see [6.33] to [6.41]).

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<sup>204</sup> *Preferred Approach Paper*, above n 200.

- 7.11 Section 13Q of the Trustee Act provides that in an action for breach of trust, the court may set off a loss arising from one investment against a gain from any other investment. This section does not expressly revoke the anti-netting rule which operated before 1988 to prevent a loss on one investment by a trustee being offset by a gain on another. Allowing the court to take into account profits from one investment and adjust losses from another was arguably an implicit repeal of that rule. However, there has been some uncertainty as to whether the anti-netting rule has been fully abolished. For the avoidance of any doubt we have recommended that it now be expressly abolished in New Zealand.<sup>205</sup>
- 7.12 Section 13M of the Trustee Act lists a number of matters courts may take into account when considering whether a trustee should be liable for breach of trust in respect of an investment. The section provides useful guidance and we recommend that it be retained.
- 7.13 As already noted, we think that section 13E (which lists the matters trustees may have regard to when investing) should also be retained. However, we recommend that it be redrafted to state that trustees may take into account their overall investment strategy when exercising their powers of investment (as well as the matters currently listed in the section).
- 7.14 We recommended in chapter 6 (R7) that new trusts legislation should give trustees the broad powers of a natural person to administer the trust and deal with trust property. Many of the specific powers currently in Part 2 are consequently not needed. We have therefore recommended repealing sections 13I, 13J, 13K, 13L, 13N, 13O and 13P because these provisions are now either historic or unnecessary.

### Application to existing trusts

- 7.15 The reforms discussed here should, when enacted, apply to all existing and new trusts covered by the new Trusts Act.

### INDICATIVE DRAFT PROVISION – INVESTMENT DUTY AND STANDARD OF CARE

- 7.16 We include below an indicative draft of the duty to invest prudently and the standard of care for investment. It is important to note that these two provisions are closely related to the power to invest provision, which would be modelled on the current section 13A, and would give effect to R14(1). That provision would give trustees the power to invest the trust funds in any property. This has not yet been drafted.

#### 23 Duty to invest prudently

- (1) When investing trust property, a trustee must invest prudently.
- (2) For the purposes of **subsection (1)**, a trustee invests prudently if the trustee complies with the standard of care set out in **section 26**.

#### 26 Standard of care for power of investment

In the exercise of a power of investment, a trustee must exercise the care and skill that a prudent businessperson would exercise in managing the affairs of others, having regard in particular—

- (a) to any special knowledge or experience that the trustee has or holds the trustee out as having; and

<sup>205</sup> This is the approach that was taken in cl 30 of the proposed *Trustee Act* in British Columbia Law Institute, Committee on the Modernization of the Trustee Act *A Modern Trustee Act for British Columbia* (BCLI Report No 33, 2004) at 49 [*A Modern Trustee Act for British Columbia*]. The Uniform Law Conference of Canada resolved in 2012 to adopt and recommend for enactment the Uniform Trustee Act based on the 2004 Report of the British Columbia Law Institute. See cl 33 of “Uniform Trustee Act” (Uniform Law Conference of Canada, Whitehorse YK, August 2012) accessible at < www.ulcc.ca > [*Uniform Trustee Act of Uniform Law Conference of Canada*].

- (b) if a person acts as a trustee in the course of a business or profession, to any special knowledge or experience that it is reasonable to expect of a person acting in the course of that business or profession.

### Commentary

Clause 12 of the Bill states that clause 23 is a default duty (see Appendix A). Clause 11 provides that a default duty is one that the trustee must perform unless it is modified or excluded by the terms of the trust. Clause 26 replaces sections 13B and 13C of the Trustee Act 1956. It provides for a situation where trustees may have held themselves out as having special skills or experience or belong to a profession or business that may mean that they could reasonably be expected to make special knowledge or skills above and beyond those of an ordinary but prudent person of business. These two provisions apply when a trustee is exercising a power of investment. The power of investment provision has not been drafted, but like section 13A of the Trustee Act 1956, which it replaces, it will give a trustee a default power to invest in any property. That power could be overridden or modified by the terms of the trust.

## DISTINCTION BETWEEN CAPITAL AND INCOME

### RECOMMENDATION

R15 The new Trusts Act should provide that:

- (1) To facilitate total return investment and allow trustees to invest trust funds without regard to whether the return on investment is technically of an income or capital nature, trustees should have discretion to determine whether a return is to be treated as income or capital for the purposes of distribution.
- (2) Trustees should be required to exercise their discretion on how a return is to be treated in a manner that is consistent with their duties as trustees and fairly and reasonably takes into account the interests of all beneficiaries.
- (3) Trustees should ensure that a reasonable level of income is made available for income beneficiaries in situations where there are defined classes of beneficiaries.

#### Note

The discretion of trustees to decide what is to be treated as income or capital is for the purposes of trust law and does not in any way alter or override the definitions and application of the revenue statutes, for the purposes of taxation.

### The duty of impartiality and modern portfolio investment theory

- 7.17 A key principle of modern day portfolio investment theory is that it is artificial to distinguish between capital and income when investing. Instead modern portfolio management assesses investment options based on their overall total return regardless of whether it is correctly categorised as capital or income.<sup>206</sup> The default provisions in the Trustee Act do not allow trustees to disregard the distinction between capital and income when investing. Trustees have a duty, preserved by section 13F, to act impartially between the interests of different beneficiaries (and classes of beneficiaries where there are classes). This default duty can be, and often is, overridden by the terms of the trust. However, when it is not, it limits the ability

<sup>206</sup> British Columbia Law Institute, Committee on the Moderization of the Trustee Act *Total Return Investing by Trustees* (BCLI Report No 16, 2001) at 5 [*Total Return Investing by Trustees*].



- of trustees to apply principles of modern day portfolio management and invest for the overall maximum total return.
- 7.18 Problems mostly arise where there are beneficiaries with a life interest and others (remainder beneficiaries) with a capital interest in the trust fund. If the duty of impartiality has not been overridden, then the law requires income to go to the life tenants and capital appreciation to go to the remainder beneficiaries.<sup>207</sup> The trustees must consequently ensure that the trust investment policy does not unfairly prejudice either income or capital beneficiaries. Trustees are not permitted to disregard the distinction between capital and income for the purposes of investing so cannot do what non-trustee investors do, which is invest for a maximum return.
- 7.19 Where trustees must invest with a view to balancing the capital and income returns, both categories of beneficiaries are likely to be dissatisfied because neither will benefit from an optimal rate of return.<sup>208</sup> To address this issue we recommend a new default provision which frees trustees from the requirement to select investments with regard to the legal category rather than overall return. The recommended approach will better support trustees adopting a total return investment policy. Within the parameters of their duties, trustees would then be able to maximise the gain to the trust portfolio. The key principle here is that investment decision-making should be separated from distributional issues.
- 7.20 The Commission considered several options, including recommending the percentage trust model, as law reform bodies in some other jurisdictions have done.<sup>209</sup> Under the percentage trust a percentage of the total value of the trust assets is distributed annually in place of income. However, while submitters overwhelmingly supported reform facilitating total return investment, there was little interest in or understanding of the percentage trust approach. Some said that it is not well understood in New Zealand and legislation would be ahead of practice. An important consideration that steered us away from percentage trusts was that it is unsuitable for trusts that give trustees a discretion as to whether and how to make distributions. The New Zealand trust landscape is distinguished by significant numbers of such discretionary trusts so we found the percentage trust model unsuitable as a default provision.
- 7.21 Instead the Commission has recommended that trustees be able to determine what is capital and income for the purposes of distribution. Trustees would be required to make such determinations in a manner that is consistent with their duties as trustees and fairly and reasonably takes into account the interests of all beneficiaries. This approach relies on trustees' mandatory duties rather than on prescribing rules for trustees to follow. Trustees, guided by their duties to beneficiaries, would have discretion to adopt a suitable mechanism to determine how much of the fund should be returned to income beneficiaries (where this is applicable) but would be required to do this in a manner that is in the overall interests of all beneficiaries.
- 7.22 Many recent trust deeds already permit this approach because it allows an investment strategy aimed at the best total return without concern over whether the return is technically income or capital appreciation. The view of most submitters was that trustees could invest more effectively if they were not constrained by distinctions between income and capital growth.

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207 Andrew S Butler "Investment of Trust Funds" in Andrew S Butler (ed) *Equity and Trusts in New Zealand* (2nd ed, Thomson Reuters, Wellington, 2009) 213 at [8.2.11(1)].

208 *Total Return Investing by Trustees*, above n 206, at 5.

209 The British Columbia Law Institute Committee took this approach: Committee on the Modernization of the Trustee Act, above n 205. See also cl 40 of *Uniform Trustee Act of Uniform Law Conference of Canada*, above n 205. Percentage trusts were also considered by the Law Commission for England and Wales to be the model most likely to be successful in facilitating total return investment. However, the Commission felt unable to formally recommend its adoption because of the tax implications involved; see Law Commission (England and Wales) *Capital and Income in Trusts: Classification and Apportionment* (Law Com No 315, 2009) at 72 [*Capital and Income in Trusts*].

- 7.23 The discretion of trustees to decide what is to be treated as income or capital for purposes of trust law does not necessarily alter income tax obligations.

## APPORTIONMENT OF RECEIPTS AND OUTGOINGS

### RECOMMENDATION

R16 The new Trusts Act should provide that:

- (1) A trustee may:
  - (a) apportion any receipt or outgoing in respect of any period of time between the income and capital accounts, or charge any outgoing or credit any receipt exclusively to or from either income or capital as the trustee considers to be fair and reasonable in all the circumstances and in accordance with accepted business practice;
  - (b) transfer funds between capital and income accounts to recover or reimburse an outgoing previously charged to the account that is to receive the funds where such corrections are fair and reasonable in all the circumstances and are undertaken in accordance with accepted business practice;
  - (c) transfer funds between capital and income accounts to recover or deduct any receipt previously credited to the account from which the funds are to be recovered where such corrections are fair and reasonable in all the circumstances and are undertaken in accordance with accepted business practice; and
  - (d) deduct from income an amount that is fair and reasonable in all the circumstances to meet the cost of depreciation, and add the amount to capital, in accordance with accepted business practice.
- (2) Subject to (5) below, the trustee's powers under (1) above should replace the traditional rules concerning apportionment between capital and income, and those traditional rules are abolished.
- (3) The trustee's powers under (1) above should apply to all trusts established before the date on which the new Act comes into force despite anything to the contrary in the terms of the trust.
- (4) In relation to trusts established on or after the date on which the new Act comes into force, (1) above should be a default provision that applies unless it is modified by the terms of the trust.
- (5) The apportionment rules in the Property Law Act 2007 will continue to apply where the trustee is the landlord, tenant, vendor or purchaser of land.

### Complex rules on apportionment

- 7.24 The current default rules on apportionment are complex and difficult to apply. Apportionment under them depends on whether a particular receipt or expense is correctly classified as income or capital. Generally, expenses of an income nature are borne by income beneficiaries while expenses of a capital nature are borne by capital beneficiaries. However, the case law rules

also depend on other factors, such as for whose benefit the expense was incurred, to determine expense apportionment.<sup>210</sup>

- 7.25 Most modern trust deeds now contract out of the traditional rule and simply enable trustees to exercise discretion on apportionment. If the trust deed is silent then trustees must apply the traditional rules. In addition to the case law rules, there are a number of specific provisions in the Trustee Act that deal with apportionment in certain situations. Section 83, for example, contains special rules as to apportionment on purchase, sale or transfer of fixed income assets and shares in certain situations.
- 7.26 Due to their complexity the current rules can result in uncertainty. It may be difficult for a trustee to assess who benefited from a particular expense and apportion it correctly. In some cases apportionment also causes inconvenience and expense because it requires complex calculations of very small sums of money.<sup>211</sup>

### Trustees' discretion

- 7.27 The Commission recommends moving completely away from case law rules and giving trustees the power to exercise discretion to determine how to apportion receipts and expenses. Logically trustees should also be permitted to change their minds subsequently or correct mistakes. The recommendations also address depreciation to ensure that income beneficiaries are not unduly favoured due to a failure to allow for depreciation.
- 7.28 Again, it should be noted that the recommendations do not in any way alter the tax status or liability that attaches to any receipt or outgoing. The reforms give trustees discretion as to how they apportion outgoings and receipts for the purposes of trust law without breaching their obligations as trustees. That would not affect the treatment of those receipts and outgoings for tax purposes.
- 7.29 The recommendation requires that the allocation of receipts and outgoings is undertaken in accordance with accepted business practice. The New Zealand Law Society and some other submitters considered that some guidance on what constitutes accepted business practice in this context could be helpful. Some submitters proposed that trustees should have to comply with “generally accepted accounting practice” reporting standards promulgated by the External Reporting Board under the Financial Reporting Act 1993. However, we were not persuaded that prescriptive financial reporting standards should necessarily be trustees’ only guide.
- 7.30 Our recommended reforms also replace section 83 and other provisions containing special rules relating to the apportionment of receipts and outgoings between income and capital. Sections 83, 84 and 85 of the Trustee Act need not be carried forward into a new statute. They are obscure, difficult to apply and can result in impractical outcomes. Instead, we propose that trustees should be able to allocate or apportion receipts and outgoings justly and equitably in these circumstances.
- 7.31 While we have recommended that the traditional rules concerning apportionment between capital and income be abolished in this context, we have clarified, in response to points raised by submitters, that the apportionment rules in the Property Law Act 2007 should continue to apply where the trustee is the landlord, tenant, vendor or purchaser of land.

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210 *A Modern Trustee Act for British Columbia*, above n 205, at 53.

211 *Capital and Income in Trusts*, above n 209, at 9.

### Application to existing trusts

- 7.32 In the *Preferred Approach Paper* we proposed that our approach to apportionment should apply to existing as well as new trusts regardless of whether any contrary provisions have been included in the trust instrument.<sup>212</sup> While one submission questioned why the proposed reform should be a mandatory position, most submitters who commented expressed support for a simple new rule giving trustees discretion.
- 7.33 We continue to favour an approach that gives all trustees discretion over apportionment. We recommend that the traditional rules governing apportionment should be abolished and that the reforms should apply to all existing trusts. Instructions on apportionment included in existing trust deeds would guide rather than overrule the new provision giving trustees discretion. Trustees would always need to exercise discretion and apportion receipts and outgoings fairly and reasonably in the circumstances ensuring that their actions accord with accepted business practice.
- 7.34 However, going forward we think the new provision should be a default one. Against the backdrop of the new default provision, which gives trustees discretion over apportionment, settlors should be free to modify the new rule. We think it unlikely that settlors would wish to do this, but the principle of settlor autonomy means that the option should be available.
- 7.35 Given the important links between R15 in respect of the distinction between capital and income and R16 in respect of apportionment, the new provisions giving effect to R15 should also apply to existing trusts and to new trusts in the way discussed here also.

## INVESTMENT MANAGERS

### RECOMMENDATION

R17 The new Trusts Act should provide that:

- (1) Trustees are authorised to appoint investment managers and give them authority to make investment decisions.
- (2) The appointment of investment managers should be subject to the following legislative safeguards:
  - (a) trustees must act honestly and in good faith (R2(1)(c)) and exercise the reasonable care, diligence and skill of a prudent person of business (R14(2)) when appointing an investment manager, and must review the investment manager's performance periodically;
  - (b) trustees must create a written policy statement that gives guidance as to how investment functions are to be exercised by an investment manager setting out the general investment objectives, and require investment managers to agree to comply with the policy statement; and
  - (c) trustees are liable for any default of their investment manager where the trustees have failed to act honestly and in good faith (R2(1)(c)) and exercise the reasonable care, diligence and skill of a prudent person of business (R14(2)) when making the appointment of a manager or monitoring the investment manager's performance.

212 *Preferred Approach Paper*, above n 200, at [5.41]–[5.44].

### **New default position**

- 7.36 Currently trustees can, and normally should, get advice on potential investments. However, they must personally assess such advice and decide whether to accept or reject it. Under the current default provisions trustees are not able to appoint investment managers and give them authority to make investment decisions, although our research indicated that many modern trust deeds enable trustees to do this.
- 7.37 The Commission recommends that trustees should be able to appoint investment managers with authority to make investment decisions as the new default position. Most submitters favoured trustees having the power to delegate to investment managers. Submitters commented on the complexity of the investment task, preferring that it be handled by specialised professionals, as it is not reasonable to expect trustees to possess this degree of expertise or engage in complex financial analysis when highly trained specialists can undertake such tasks for a fee. The use of investment managers recognises that making sound investment decisions in today's world requires considerable skill and judgement. The range of potential investment products and combinations is now immense and investment has become far more complex as a result. It is simply not realistic to require trustees to undertake this function personally.
- 7.38 A suitably qualified and competent professional investment manager is likely to do a better job than many lay trustees. With appropriate safeguards there may also be less risk in allowing for the appointment of experts than in leaving investment in the hands of trustees. The recommended power to appoint investment managers is constrained by important safeguards designed to ensure that trustees set the investment policy and exercise appropriate care in choosing and monitoring their appointed manager. The Commission considers that periodic review of the investment manager's decisions and having a written policy statement are necessary to ensure trustees remain accountable for their actions.
- 7.39 As already noted, the new provisions will be default provisions. It would therefore be possible for a settlor to exclude or alter the power of appointment, or exclude or modify any of the safeguards in the trust deed.

### **Application to existing trusts**

- 7.40 Trustees of existing trusts should have the power to appoint investment managers, subject to anything in the terms of the trust precluding this.

# Chapter 8

## Appointment and removal of trustees

### INTRODUCTION

- 8.1 This chapter addresses topics relating to the appointment and removal of trustees. The following specific issues are covered:
- acceptance or rejection of trusteeship;
  - who may be appointed as a trustee;
  - the discharge and replacement of a trustee, including grounds for removal, who may remove a trustee and appoint a replacement trustee, appointment of a replacement trustee when a trustee dies while in office, and the retirement of trustees;
  - whether persons removing and appointing trustees should be subject to duties;
  - whether trustees who are removed should always be replaced and whether the new Act should provide for a minimum number of trustees; and
  - the transfer of trust property when a trustee is removed.
- 8.2 There are issues with the current law in these areas due to a lack of clarity in the existing statutory provisions or processes, or an outdated approach that no longer meets the needs of contemporary trust practice. Our recommendations seek to modernise the statutory provisions in these areas of trust administration, and to provide guiding principles and mechanisms for appointment and removal that are more robust. The new Act should also include the requirement that trustees be over the age of 18 years. The suite of recommendations has been designed to work together as an overall package. The reform options are discussed in detail in the *Preferred Approach Paper* and *Fourth Issues Paper*.<sup>213</sup>

### ACCEPTANCE AND REJECTION OF TRUSTEESHIP

#### RECOMMENDATION

R18 The new Trusts Act should provide that:

- (1) A person who is appointed as a trustee of an express trust may accept or reject the trusteeship.
- (2) Acceptance of a trusteeship must be either express (in writing or oral) or clearly implied through conduct, unless otherwise specified in the terms of the trust.
- (3) Rejection of trusteeship need not be in writing (unless the terms of the trust specify otherwise), but must be communicated to the person specified under the terms of the trust (such as the settlor or appointer) in clear and unambiguous terms.

<sup>213</sup> Law Commission *Review of the Law of Trusts – Preferred Approach* (NZLC IP31, 2012) at ch 6; Law Commission *The Duties, Office and Powers of a Trustee: Review of the Law of Trusts – Fourth Issues Paper* (NZLC IP26, 2011) at ch 4.

- (4) If a trustee does nothing to accept or reject a trusteeship within three months of receiving notice of the appointment, the trustee will be deemed to have rejected the trusteeship.
- (5) If a trustee rejects the trusteeship, the property vests in the remaining trustees.

### Accepting or rejecting the role of a trustee

- 8.3 The recommendations in this area reflect and clarify the current case law. Currently, no one can be compelled to be a trustee of an express trust.<sup>214</sup> To give effect to this principle, trusteeship does not commence until the appointment is accepted. Acceptance may be express or implied by conduct such as dealing with the trust property.<sup>215</sup> An appointed trustee who does not want to accept the trusteeship may reject the office. If this happens, the trust property will either vest in the remaining trustees, or, if there are no other trustees, revert to the settlor.<sup>216</sup> There is no time limit for rejection, but once the trusteeship has been accepted it cannot later be rejected, but must be resigned.
- 8.4 The law is ambiguous and in need of clarification regarding the effect of inaction. There is case law that supports the proposition that inaction for a long period will be presumed to constitute rejection.<sup>217</sup> There is also case law for the proposition that a long period of inaction will be presumed to constitute acceptance (because there has been no express rejection).<sup>218</sup> Whether the court finds there has been an implied acceptance or an implied rejection is assessed on the facts.<sup>219</sup>
- 8.5 Our recommendation retains the settled position under case law that a trustee does not assume trusteeship until the office is accepted, while clarifying that inactivity is considered to be rejection. Acceptance will continue to be able to be implied through conduct. A trust deed could provide an alternative approach with respect to whether acceptance or disclaimer needs to be in writing.
- 8.6 It is useful to stipulate a defined period of time after which inaction will be treated as rejection, to ensure that a named trustee has clear warning of the date by which trusteeship must be accepted. Three months provides the appointed trustee with a sufficient opportunity to accept the appointment and is consistent with the period in section 19 of the Administration Act 1969 for the proof of a will by an executor.
- 8.7 Submitters did not take issue with this proposal. A few considered it to be unnecessary, but we prefer that the law be more certain in this area. As a result of submitter feedback, we have altered the order of the proposal so that it follows a more logical progression. We have decided not to include the previous example draft provision because it was unduly prescriptive. The provision, when drafted, should not be too prescriptive of the types of conduct that may imply acceptance as the case law should continue to apply.

214 The Trustee Act 1956, s 43 provides that the Public Trust can be compelled to be a trustee in some circumstances, but does not otherwise alter case law.

215 See *Lord Montford v Lord Cadogan* (1816) 19 Ves 635, 35 ER 841 (Ch) and *James v Frearson* (1842) 1 Y & C Ch Cas 370, 62 ER 929.

216 *Lord Montford v Lord Cadogan*, above n 215; *Robinson v Pett* (1734) 3 P Wms 249; 24 ER 1049.

217 *Re Clout and Frewer's Contract* [1924] 2 Ch 230; *Re Gordon* (1877) 6 Ch D 531; *Re Birchall* (1889) 40 Ch D 436.

218 See *Re Uniacke* (1844) 1 Jo & Lat 1, however, the approach in this case was criticised and not followed in *Re Clout and Frewer's Contract*, above n 217.

219 *Lady Naas v Westminster Bank Ltd* [1940] AC 366 (HL).

## WHO MAY BE A TRUSTEE?

## RECOMMENDATION

- R19 The new Trusts Act should provide that any natural person or body corporate may be appointed as trustee of a trust, except:
- (a) a natural person under 18 years of age;
  - (b) an undischarged bankrupt (an undischarged bankrupt may be appointed with the consent of the court);
  - (c) a person who is subject to a property order made under section 31 of the Protection of Personal and Property Rights Act 1988 or a person for whom a trustee corporation is acting as manager under sections 32 or 33 of that Act; and
  - (d) a corporation that is in receivership, liquidation or voluntary administration (or any similar status).

## Restricting who may be a trustee based on capacity

- 8.8 Currently under case law any person with legal capacity to hold property, including a settlor and any of the beneficiaries, may be appointed as a trustee.<sup>220</sup> We have considered whether there should be any restrictions on who may be a trustee, and if so, the content of these restrictions. In particular we drew a distinction between restrictions based on capacity and restrictions based on suitability. Some persons have limited capacity to deal with property or enter into contracts, for example persons under the age of 18 years, undischarged bankrupts (as their existing and acquired property rights vest in the Official Assignee),<sup>221</sup> companies which are in liquidation, and persons subject to a property order under the Protection of Personal and Property Rights Act 1988. Irrespective of their suitability for office, such persons are not able to function effectively as trustees because of their limited capacity to deal with property. In contrast, other factors, such as a history of dishonesty offences, do not affect a person's capacity to deal with property, but may raise doubts about the person's suitability.
- 8.9 We recommend imposing restrictions based on capacity but not suitability. Persons who lack full capacity should not be able to be appointed as trustee. Any purported appointment should be invalid. While settlor autonomy is an important principle, it should not extend to empowering those who lack legal capacity to act as trustee.
- 8.10 Although the argument can be made that the office of trustee requires good judgement and honesty, and that those who lack these characteristics should be restricted from appointment, it is difficult to draw principled grounds for excluding someone from acting as a trustee based on past behaviour. For example, a category such as "dishonesty offences" includes even relatively minor instances of theft, which a settlor may not consider to be sufficiently serious to preclude appointing a person as trustee. A person who is "mentally disordered" under the Mental Health (Compulsory Assessment and Treatment) Act 1992 might include persons who are entirely capable of managing trust property, depending on the nature of mental disorder.<sup>222</sup> A mandatory

220 The only restriction is that there will not be a valid trust if the sole trustee is also the sole beneficiary, because legal and beneficial ownership will exist in the same person. *Re Heberley (deceased)* [1971] NZLR 325 (CA) at 333 and 346; *Re Cook, Beck v Grant* [1948] 1 All ER 231 (Ch) at 215.

221 Insolvency Act 2006, ss 7 and 102.

222 The inclusion of this category in the Eden Park Trusts Amendment Bill 2009 was subject to a report by the Attorney-General under s 7 of the Bill of Rights Act 1990, which held that this constituted unjustifiable discrimination on the basis of disability and was not rationally linked to capacity to be a trustee.



prohibition would also preclude such people from acting as trustees of trusts they settle for the benefit of their own families. There is an element of subjectivity in judgements about suitability. We consider that these are best left to the settlor rather than imposed through legislation.

- 8.11 We have accepted submitter suggestions to extend the restrictions on corporate trustees to those in voluntary administration because they also lack sufficient capacity to carry out the role of trustee. We are recommending a continuation of the current general position that any corporation may be trustees at present. However, further restrictions on corporate trustees, such as a company that is under statutory management, has entered into a compromise with creditors or does not satisfy the solvency test, along with other issues relating to the appropriateness of corporate trustees, may be considered further in the corporate trustee review. There is a risk that these companies will be unable to meet financial liabilities to beneficiaries and creditors.

## DISCHARGE AND REPLACEMENT OF A TRUSTEE

### RECOMMENDATION

#### R20 **Mandatory and discretionary grounds for removal**

The new Trusts Act should:

- (1) Require the removal of certain trustees by imposing an obligation on persons with the power to appoint and remove trustees under R21(1) to remove a trustee when the following mandatory grounds are met:
  - (a) the trustee is incapacitated; and
  - (b) the trustee is subject to either an enduring power of attorney in relation to property or a property order, or has a trustee corporation appointed to act as a manager under the Protection of Personal and Property Rights Act 1988; and
  - (c) the trustee's powers have not been delegated by a delegation authorised by statute or by the terms of the trust.
- (2) Empower (but not require) persons with the power to appoint and remove trustees under R21(1) to remove a trustee and appoint a replacement, if it is desirable for the proper functioning of the trust, when one or more of the following discretionary grounds are met:
  - (a) the trustee refuses or fails to act as a trustee;
  - (b) the trustee, being a corporate trustee, enters into receivership or liquidation, ceases to carry out business, is dissolved, enters into a compromise with creditors or voluntary administration under Parts 14 or 15A of the Companies Act 1993, or does not satisfy the solvency test in section 4 of that Act;
  - (c) the trustee is no longer considered suitable to continue to hold office as a trustee because of circumstance or conduct, for instance, this may be the case when:
    - (i) the whereabouts of the trustee is unknown and the trustee cannot be contacted;
    - (ii) the trustee is not capable of fulfilling the role because of sickness or injury;
    - (iii) the trustee is adjudged bankrupt;
    - (iv) the trustee is convicted of a dishonesty offence;

- (v) the trustee becomes precluded from serving as a director under the Companies Act 1993 because of a breach of that Act or the Securities Act 1978, or is the subject of a current banning order under the Financial Markets Conduct legislation;
  - (vi) the court finds the trustee has committed serious misconduct in the administration of the trust; or
  - (vii) the trustee, being a lawyer, chartered accountant or financial adviser, is found to have seriously breached the applicable ethical standards of that profession, resulting in the trustee being struck off, losing a license or being disqualified.
- (3) Retain the court's general discretion to remove trustees if expedient, including the discretion to remove a trustee without appointing a replacement in accordance with R25.
- (4) Provide that nothing in (1) or (2) is to be read as limiting the grounds on which a person nominated under the terms of the trust with a power to remove and appoint trustees is entitled to exercise that power.

#### R21 **Who may remove a trustee and appoint a replacement**

The new Trusts Act should provide that:

- (1) In absence of any contrary intention in the terms of the trust, the following persons have the power to remove and appoint trustees by deed when the grounds in R20 are met:
- (a) the person nominated under the terms of the trust with a power to remove and appoint trustees; or
  - (b) if there is no person in (a) or if that person is unavailable or unwilling to make a decision, the remaining trustees; or
  - (c) if there is no person in (a) or (b) or if that person is unavailable or unwilling to make a decision, whichever of these representatives of the trustee being removed is relevant:
    - (i) a property manager appointed over the trustee under the Protection of Personal and Property Rights Act 1988;
    - (ii) the holder of an enduring power of attorney over property of an incapacitated trustee; or
    - (iii) the liquidator of a corporate trustee that enters into liquidation.
- (2) Where a representative of the trustee listed in (1)(c) acts to remove and replace, the following process applies:
- (a) the representative should provide notification of the intended discharge of the trustee and of the person selected as replacement, and a statement of the trust accounts to all competent adult beneficiaries, or where it is unreasonable or impractical to do so, to a reasonably representative sample of beneficiaries;

- (b) the beneficiaries should be given 20 working days from the date that notification is received to object to the intended replacement trustee or to anything in the statement of trust accounts;
- (c) at the end of the notice period, if no one has objected the representative should apply to the Public Trust to confirm the discharge and replacement of the trustee;
- (d) the Public Trust, if it is satisfied that due notice and information was given to the beneficiaries and that no objections have been made, may confirm the discharge and replacement of the trustee by deed;
- (e) if a beneficiary objects, an application will need to be made to the court for the trustee to be removed and replaced;
- (f) if the Public Trust:
  - (i) is not satisfied regarding the notice and information given to the beneficiaries; or
  - (ii) has concerns because of issues raised by the beneficiaries, disagreement between the parties, or any other reason,

it may decline to confirm the discharge and replacement of the trustee. An application will need to be made to court for the discharge and replacement of the trustee and the court will be able to make any other necessary directions about the management of the trust.

#### **R22 Appointment of replacement when trustee dies while in office**

- (1) The new Trusts Act should provide that, in absence of any contrary intention in the terms of the trust:
  - (a) if a trustee dies while in office and it is necessary, either because the trustee was a sole trustee or because the terms of the trust require it, or desirable for the trustee to be replaced, the replacement may be appointed by deed by:
    - (i) the person nominated under the terms of the trust with a power to remove and appoint trustees; or
    - (ii) if there is no person in (i) or if that person is unavailable or unwilling to make a decision, the remaining trustees; or
    - (iii) if there is no person in (i) or (ii) or if that person is unavailable or unwilling to make a decision, the executor or administrator of the trustee; and
  - (b) if the deed of replacement is to be made by the executor or administrator, the process of notification of beneficiaries and confirmation by the Public Trust in R21(2) should apply.

#### **R23 Retirement and replacement of trustee**

The new Trusts Act should provide that, in absence of any contrary intention in the terms of the trust:

- (a) if a trustee wishes to retire, the trustee may be discharged by deed by:

- (i) the person nominated under the terms of the trust with a power to remove and appoint trustees; or
  - (ii) if there is no person in (i) or if that person is unavailable or unwilling to make a decision, the remaining trustees; or
  - (iii) if there is no person in (i) or (ii) or if that person is unavailable or unwilling to make a decision, the retiring trustee and a replacement trustee, selected by the retiring trustee, together; and
- (b) if (a)(iii) applies, which will be the case if the retiring trustee is a sole trustee or if the persons in (a)(i) and (ii) are unavailable or unwilling, the process of notification of beneficiaries and confirmation by the Public Trust in R21(2) applies (with necessary amendments).

### Current law

- 8.12 Currently, the Trustee Act sets out aspects of the law regarding the discharge and replacement of a trustee in sections 51 and 43. Section 51 of the Trustee Act provides a list of specific circumstances in which the court may replace an existing trustee, including committing misconduct, being convicted of a crime, being mentally disordered, being bankrupt, and being a corporation in liquidation. Section 43 states that the person nominated in the trust deed as appointer of trustees, the surviving or continuing trustees, or the personal representative of the last surviving or continuing trustee, may appoint a replacement trustee in limited circumstances (in addition to any power contained in the trust deed). These circumstances include where the trustee has died, is out of the country for more than 12 months, desires to be discharged, refuses to act, is unfit or incapable of acting or is a corporation in liquidation.
- 8.13 The court has the jurisdiction to remove trustees and appoint new trustees. This is a general discretion to be exercised when the removal of an existing trustee and appointment of a new trustee is expedient, for instance when there is a conflict of interest or an irreconcilable disagreement between the trustee and the beneficiaries.<sup>223</sup>
- 8.14 There are a number of issues with the way that sections 51 and 43 operate. These sections are neither aligned nor clearly differentiated, which causes confusion and a lack of clarity about the circumstances in which a trustee may be removed without recourse to the court. Some of the court's specific powers of removal, for example the power to remove a bankrupt trustee, have been held to come within the broad power under section 43 to remove a trustee who is "unfit to act".<sup>224</sup> There is some case law on the meaning of the terms "unfit to act" and "incapable of acting". However, there remains ambiguity and these terms may not provide sufficient guidance to persons wishing to exercise a power under section 43.<sup>225</sup>
- 8.15 The law on the retirement of a trustee is unclear and does not operate as an effective statutory default. In addition to a trustee being able to retire if discharged under sections 43 and 51, a trustee may retire by deed with the consent of co-trustees or those with the power to appoint trustees under section 45. Also, in a seldom-used and unclear process under section 46, a trustee may retire by "passing his accounts before the Registrar" of the High Court where there are no

223 *Re Roberts* (1983) 70 FLR 158, 20 NTR 13 (SC); *Mendelsohn v Centrepont Community Growth Trust* [1999] 2 NZLR 88 (CA); *Kain v Hutton* CA23/01, 25 July 2002.

224 Andrew S Butler "Trustees and Beneficiaries" in Andrew S Butler (ed) *Equity and Trusts in New Zealand* (2nd ed, Thomson Reuters, Wellington, 2009) 105 at 114, citing *Re Wheeler and De Rochow* [1896] 1 Ch 315 and *In re Hopkins* (1881) 19 Ch D 61 (Ch).

225 For a discussion of the case law, refer to the *Fourth Issues Paper*, above n 213, at [4.14]–[4.15].

co-trustees or they do not consent, and, if no one is able or willing to appoint new trustees, the retiring trustee may apply to the court for the appointment of a new trustee. However, there are situations that fall outside all of these sections, where there is no effective mechanism for a trustee to retire without recourse to the court, for instance where there is a sole trustee and no one with the power to remove and appoint trustees.

## **R20: Mandatory and discretionary grounds for removal of a trustee**

- 8.16 We consider that it is useful for legislation to address the removal of a trustee in a more comprehensive, coherent way. We propose replacing the vague and problematic terms “unfit” and “incapable” under section 43 with a list of circumstances that meet the broad criteria to guide the exercise of discretion.<sup>226</sup> The statutory grounds for removal would not be able to be overridden, but the trust deed would be able to include further grounds or detail to guide the exercise of discretion. We do not intend that the court’s inherent jurisdiction to remove and replace trustees would be altered by the provision.
- 8.17 We propose that persons with the power to remove and replace trustees should have an obligation to remove a trustee who loses capacity to deal fully with property because of a personal property order or the appointment of a property manager. This would not apply where a delegation is in place for temporary incapacity. However, once the delegation expires and if the incapacity continues, the trustee should be removed. The legislation would also provide a list of grounds for removal on a discretionary basis under an updated and modernised form of section 43. Factors relating to the trustee’s capacity, like bankruptcy, liquidation, and receivership, should be included among these grounds, as well as other factors that call into question the trustee’s suitability.
- 8.18 We have considered the option of mandatory removal when the grounds are made out but consider that this is not appropriate because it would impose additional duties on the person with the power to remove and replace trustees. Also, there may be situations where one of the grounds is made out but it is not in the interests of the trust for the trustee to be removed.
- 8.19 Submitters have generally approved of this approach and have provided specific suggestions to refine the wording of the proposed provision. As a result, we have adjusted the structure of the proposal to make the circumstances that require mandatory removal clearer. We have also made sure the provision aligns with other aspects of our recommendations, such as delegation of trustee powers and the minimum number of trustees.
- 8.20 Several submitters suggested that the threshold for considering that a trustee should be removed on the basis of one of the discretionary factors (“desirable for the proper functioning of the trust”)<sup>227</sup> was too easily satisfied and that a more objective, higher standard, such as “necessary”, would be better. They were concerned that a trustee could be too readily removed when any of the list of circumstances was present, although not necessarily serious or instrumental to the trustee’s capacity to carry out the role. We consider that “desirable” is the more appropriate standard as it gives those with the power to appoint and remove trustees’ discretion to consider whether removal of a trustee is the best course of action in the circumstances. We have made changes to address submitters’ concerns that trustees should not be removed for minor breaches of trust or professional ethical standards. More serious misconduct is now required.

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226 The power of removal would apply to established situations that currently fall under the headings “unfit” (such as dishonesty offence convictions and misconduct in trust administration), and “incapable” (trustees not capable of fulfilling their duties, for instance, because of sickness or injury).

227 See *Preferred Approach Paper*, above n 213, at P23(2).

- 8.21 We have not followed the Inland Revenue's related suggestion that creditors should be given standing to apply to the court for the removal of a trustee.

### **R21: Who may remove a trustee and appoint a replacement**

- 8.22 Under the existing law, the continuing trustees or someone with the power to appoint or remove trustees under the trust deed, are able to remove a trustee where necessary in most cases.<sup>228</sup> However, issues may arise where there is no such person, or where that person is unavailable, for instance, if there is a sole trustee or a corporate trustee enters into liquidation.
- 8.23 Our intention with the recommendation is to continue to empower persons who have the power to remove and appoint trustees to do so when the grounds for removal are met, so that application to court can be avoided in most cases. We have expanded the categories of representatives who may remove and appoint a trustee to include a liquidator of a corporate trustee, and the holder of an enduring power of attorney or property manager under the Protection of Personal and Property Rights Act. We have included a process to provide validation and confirmation when trustees are being removed by a representative, to prevent this power being misused.
- 8.24 We are aware that there are some concerns with the proposal to give the power to holders of an enduring power of attorney and property managers. The Ministry of Social Development was not in favour because it considers the role of the property manager or attorney is to look after the incapacitated person's personal affairs. The property manager or attorney owes specific duties to persons unable to manage their own property. The Ministry does not consider it appropriate to extend the role by imposing duties in respect of a trust.
- 8.25 In our view, the practical advantages of this option outweigh the concern. We consider that a representative of a trustee who loses capacity would be in a good position to remove and replace the trustee because the representative is already familiar with the trustee's affairs. The power to remove the trustee is consistent with the existing role. The power to appoint new trustees is an extension of the role, but is consistent with the current approach of allowing the personal representative of a deceased trustee to appoint a replacement. Given that these issues only arise if there is a sole trustee in office and no one with the power to appoint and remove trustees, the personal representative of the trustee is likely to have some level of involvement, and may be the only person aware of the situation and competent to act. If the property manager fails to remove the trustee, it will put the incapacitated trustee at risk of liability, something from which a property manager is required to protect the trustee. We recognise that it is not ideal for the personal representative to fill this role but that there is no one else who is in a position to effect the change of trustee so that in these relatively rare cases a court proceeding can be avoided.
- 8.26 The recommendation includes supervision by the Public Trust when there is a sole trustee and no one with the power to appoint and remove trustees. If the Public Trust is not satisfied that the beneficiaries were notified of the discharge and replacement of the trustee and given a statement of the trust accounts, or if the beneficiaries object to the proposed appointment or anything in the statement of accounts, the personal representative will need to apply to the court to approve the appointment and provide direction on the administration of the trust. The statement of trust accounts is intended, in line with the duty to keep proper accounts, to be a statement that adequately identifies the assets, liabilities, income and expenses of the trust. This is a change from the proposal in the *Preferred Approach Paper*, which would have required the Public Trust to certify that the accounts were in order.<sup>229</sup> Following feedback from the Public

228 Trustee Act 1956, s 43.

229 *Preferred Approach Paper*, above n 213, at P23.

Trust and others, we now realise that this would have placed a potentially onerous obligation on the Public Trust to check over the trust accounts. We do not think this is necessary so long as a statement of the trust accounts is brought to the attention of the beneficiaries who are being notified of the replacement of the trustee so that the beneficiaries are given the opportunity to raise any concerns.

- 8.27 It should be emphasised that if for any reason the process in this recommendation or the recommendations in R22 or R23 cannot occur, or those involved do not want to proceed with this process, an application can be made to the court for the discharge and replacement of the trustee. Further, it should be noted that the provisions recommended in this chapter are default provisions, and would not apply if an alternative process were set out in the terms of a trust. For instance, the Auckland Energy Trust deed contains rules governing the appointment, retirement and proceedings of trustees. These would continue to apply under the new Act.

### **R22: Appointment of a replacement when trustee dies while in office**

- 8.28 Section 43 of the Trustee Act mingles death with other reasons for discharging a trustee, meaning that it is less than straightforward to work out the procedure that applies in that situation. Our proposals in the *Preferred Approach Paper* did not directly address what happens when a trustee dies.<sup>230</sup>
- 8.29 We now consider that clarity is improved by separating out the case of a trustee that dies while in office. The recommended process echoes that in R21 but applies to an executor or administrator of the trustee who has died rather than a personal representative. It may not always be necessary or desirable for a deceased trustee to be replaced. This provision will only be needed when the deceased trustee was the only trustee of the trust, the terms of the trust require that the trustee is replaced, or those with the power to appoint a new trustee consider that it is desirable to do so.

### **R23: Retirement and replacement of a trustee**

- 8.30 Many modern trust deeds do not rely on the Trustee Act provisions for the retirement of a trustee; instead they include a process for retirement and replacement of trustees.
- 8.31 The current law means that a court application is necessary where the retiring trustee is a sole trustee and the trust deed does not grant anyone the power to remove and appoint trustees. This causes unnecessary expense and takes up the court's time for an essentially administrative matter.
- 8.32 A trustee could currently be discharged without consent by applying to the Registrar of the High Court, even when this is not in the best interests of the trust. However, there may be valid reasons for those with a power to appoint and remove trustees not to discharge a trustee who wishes to retire, for instance, when a trustee seeks to retire because the trust has been poorly managed and the trustee wishes to avoid potential liability. However, there is no reasonableness requirement for withholding consent, which may pose an obstacle to efficient removal and replacement.
- 8.33 In the *Preferred Approach Paper*, we proposed a simpler process for retirement that aligned more closely with general provisions for removal by including "wishes to be discharged from office" in the list of possible grounds for removal.<sup>231</sup> When a trustee retired, the co-trustees, or those with a power to appoint, would make sure that the trust was in order before carefully selecting a

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230 At [6.31]–[6.39].

231 At [6.45].

new appointment. We considered the option of allowing a trustee to retire unilaterally because this would remove the need for a complex and expensive court process. However, while this would continue to be possible if authorised by the trust deed, we did not think the statutory default should allow this. The recommendation, involving certification by the Public Trust, is designed to allow removal without court supervision unless there is disagreement.

- 8.34 As a result of submitter feedback, our recommendation is now to have provisions addressing retirement of a trustee that are separate from the grounds and process for removal of a trustee. We have tried to clearly distinguish retirement and removal so that they are recognised as different concepts.
- 8.35 We have also modified the proposal by allowing a trustee who wishes to retire but who any co-trustees and the person with the power to appoint and remove trustees under the deed refuse to discharge, to use the process of notifying beneficiaries and seeking confirmation from the Public Trust. This resulted from submitter concern that it would be too difficult for a trustee to retire.
- 8.36 Notifying beneficiaries of the intended appointment and enabling beneficiaries to challenge a proposed new appointment would provide a safeguard to ensure that contentious cases receive court supervision.

## EXERCISE OF POWER TO REMOVE AND APPOINT TRUSTEES

### RECOMMENDATION

R24 The new Trusts Act should provide that:

- (1) Those who exercise a power to discharge and/or appoint trustees under the new Act (under R20, R22 and R23) rather than because they are appointed by the terms of the trust are subject to a mandatory duty to exercise the power in good faith, honestly and for a proper purpose (R2).
- (2) The court may remove and replace someone with the power to discharge and appoint trustees under the terms of the trust if that person has exercised the power unlawfully, or if that person has been removed as a trustee, or if otherwise expedient.
- (3) A person with the power to appoint trustees would be entitled to apply to the court for directions in the exercise of that power.

### Power of removal and appointment of trustees

- 8.37 In the *Preferred Approach Paper* we proposed that a general duty of good faith and honesty be imposed on any person exercising a power to discharge and appoint trustees, whether the power was exercised under statute or under the trust deed.<sup>232</sup> We had considered that this could be valuable because the duties of those with such a power to appoint and remove trustees are currently not set out in statute, and those exercising the power may not be aware of the case law, which has imposed duties on those exercising such powers.

<sup>232</sup> At P26.



- 8.38 Currently, the law is not entirely clear. It has been argued that all persons with the power to appoint and remove trustees are subject to a duty of good faith, but this has not been settled by the courts.<sup>233</sup> In some cases, the court has held that a person with the power to appoint trustees is subject to more extensive fiduciary duties,<sup>234</sup> and on this basis removed and replaced such a person. It seems that whether fiduciary duties arise in the case of a particular person with the power to appoint and remove trustees is a matter of interpretation based on the terms of the trust.
- 8.39 The power to appoint and remove trustees is of increasing importance. Sometimes the settlor retains this power in order to keep a final level of control over the trust. There are questions regarding the appropriate bounds of this role, in particular, whether those exercising a power to appoint trustees (either under the trust deed or legislation) should be subject to any duties and whether the court should be able to remove and appoint someone with the power to remove and appoint trustees under the trust deed.
- 8.40 Feedback received on the proposal reflected differing understandings of the current law and therefore differing perceptions about the extent to which we were suggesting changes to the law. We had intended that the proposed duty would simply set out the standard the courts currently expect from those with the power to appoint and remove trustees. A number of submitters considered that the proposed duty extended the law by making persons with the power to appoint and remove trustees subject to the court's oversight. Some considered that these powers could currently be exercised with unfettered discretion, for instance where a settlor may have reserved the powers for him or herself. Other submitters favoured the duties on those with powers to appoint and remove trustees being more extensive, and including a requirement that the powers be exercised for a proper purpose.
- 8.41 It would seem that the law in this area is still unsettled. The extent of the duties applying to a person with the power to appoint and remove trustees is dependent on the circumstances of the particular trust. We now consider that it is not helpful to set down general duties for anyone exercising these powers. We think it is still necessary to settle the duties in relation to those who will be empowered by the new Act to discharge and appoint trustees. Consequently, we recommend that these people be subject to the duty to exercise the powers in good faith, honestly and for a proper purpose. Those who are also trustees will be subject to more extensive duties.
- 8.42 The recommendation leaves open to the courts the question of what duties, if any, apply in respect of persons given the power to appoint and remove trustees by a trust deed, and whether honesty and good faith, and more rigorous fiduciary duties apply in the circumstances of a particular trust.
- 8.43 The recommendation does clarify that the court exercises supervision by having the power to remove and replace a person with the power to appoint and remove trustees if that power is exercised unlawfully, or that person has been removed as a trustee, or it is otherwise expedient. A person with the power to appoint trustees would also be entitled to apply to the court for directions in the exercise of that power.

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<sup>233</sup> Butler, above n 224, at 112–113.

<sup>234</sup> *Carmine v Ritchie* [2012] NZHC 1514 at [66]; David Hayton, Paul Mathews and Charles Mitchell (eds) *Underhill and Hayton: Law of Trusts and Trustees* (18th ed, LexisNexis, London, 2010) at [70.20] and [71.11].

## NUMBERS OF TRUSTEES

## RECOMMENDATION

- R25 The new Trusts Act should provide, in absence of any contrary intention in the terms of the trust, that:
- (a) trustees can be removed without being replaced, provided that this will not result in there being fewer trustees than the minimum number prescribed in the terms of the trust; and
  - (b) if a sole trustee is removed or dies in office, the trustee may be replaced with more than one replacement trustee, unless the terms of the trust provide otherwise.

## Altering the number of trustees

- 8.44 The Trustee Act does not impose a minimum number of trustees. This is left to the trust deed. However, a trustee must not be removed without being replaced under the statutory power of removal unless two trustees or a statutory trustee corporation remains in office. A retiring trustee will not be discharged from duties unless two trustees or a trustee corporation remains in office.<sup>235</sup> In effect this means that there is a default minimum requirement of two trustees on an on-going basis unless the initial appointment was a single trustee, or unless one of the statutory trustee corporations is appointed.
- 8.45 The minimum number rules are not explicit and the provisions are not well understood. There is a widespread misconception that the trustee corporation exception in section 43(2)(c) applies to any corporate trustee as opposed to a statutory trustee corporation.
- 8.46 Our recommendation would enable the replacement of trustees where necessary but will not require a removed trustee to be replaced in every instance. This decision would be subject to the overall duty of good faith and honesty where the appointer is subject to such a duty, and, where it is a trustee exercising the power to remove and appoint another trustee, the trustee is subject to the mandatory duties of trustees and any other duties that apply under the particular trust. This is simplified from what we had proposed in the *Preferred Approach Paper* as a result of submitters' comments that the considerations we had previously proposed to guide how the decision is to be exercised made the provision overly complex.
- 8.47 The recommended provision could be overridden by a contrary intention expressed in the trust deed. New legislation should not contain a statutory default minimum number of trustees for the initial appointment or subsequent appointments. A statutory minimum number of trustees is unnecessary and would complicate existing arrangements that have only one trustee. It should continue to be possible for a settlor to appoint a sole trustee. If a sole trustee is removed it should be possible to appoint more than one trustee in replacement.
- 8.48 We have not pursued that part of the original proposal that attempted to clarify that if a settlor provided in the trust deed that there must always be two or more trustees, this would be interpreted as requiring two persons who are able to exercise independent judgement. We accepted submitter feedback that this is not necessary if the statutory default position is that there can be a sole trustee. Where the trust deed prescribes its own rules for the number of

<sup>235</sup> Trustee Act 1956, s 43(2)(c).

trustees it is not helpful for legislation to provide an interpretation that goes beyond what the legislation permits when the trust deed is silent.

## TRANSFER OF TRUST PROPERTY

### RECOMMENDATION

R26 The new Trusts Act should:

- (1) Impose a duty on a departing trustee to transfer property to the continuing trustees, including to complete formalities for the transfer of registered property interests.
- (2) Provide that a trustee shall be divested of all trust property if validly removed from office (including through death or voluntary discharge), and provide that the trust property shall vest in the continuing trustees, subject to liabilities attaching to the trust property.
- (3) Provide, as a default provision, that where a trustee has been removed but has not transferred the trust property to a continuing trustee:
  - (a) the continuing trustee must give the departing trustee notice that the departing trustee will be divested of the trust property after 20 working days;
  - (b) if the departing trustee objects within 20 working days, the continuing trustee must apply to court for a transfer order;
  - (c) if the departing trustee does not object within 20 working days, the Public Trust may, upon request of the continuing trustee, issue a statutory certificate of vesting confirming that the deeds which remove the departing trustee and appoint the continuing trustees have been validly executed (a vesting certificate issued by the Public Trust will not be ineffective for failure of the notice provisions);
  - (d) the Public Trust may refuse to grant a vesting certificate when it considers that the property arrangement is complex or it is not clear whether the trustee was properly removed or for any other reason, and the continuing trustee must apply to the court for a transfer order;
  - (e) the continuing trustee may submit the vesting certificate to registries of property interests, in which case the statutory certificate of vesting shall be sufficient and complete proof of change of ownership of property, and:
    - (i) must be accepted as complete documentation under section 99A of the Land Transfer Act 1952; and
    - (ii) must be accepted as proof of transfer of any other registered interest recorded in a register under New Zealand law;
  - (f) the departing trustee must be given the documents demonstrating that the property is no longer in the departing trustee's name once transfer and registration are complete; and
  - (g) a registry that transfers property in reliance on a statutory vesting certificate is not liable for any loss caused as a result of the transfer of property.

### Transferring trust property when there is a change of trustee

- 8.49 The transfer of property when a trustee is removed is addressed in several sections of the Trustee Act.<sup>236</sup> These work well for non-registered property interests, but there are issues in relation to the transfer of registered interests. It is unclear what documentation is required to transfer a registered interest where the departing trustee either cannot or will not be involved. Registries are properly concerned to protect against wrongful transfer. However, different requirements for different registries can cause administrative problems for trusts and difficulties for the registries in question, such as potential liability for a wrongfully executed transfer, in the absence of a clear statutory process on which to rely.
- 8.50 A court order addresses these issues, but has its own problems due to cost, delays, and a perceived inaccessibility for lay trustees. It is also questionable whether it is appropriate to use the court's time for what is essentially an administrative matter.
- 8.51 In the ordinary course of events, the departing trustee should transfer the property to the continuing trustee. However, there are a variety of reasons why this might not occur, such as incapacity, refusal or omission. If there is delay before the continuing trustees realise that they do not have legal title, the departing trustee may no longer be available.<sup>237</sup> A process is required to transfer trust property in these cases, but it is important to protect against wrongful transfer.
- 8.52 We recommend combining a statutory vesting provision with a duty on the departing trustee to transfer property, and a process for the Public Trust to issue a certificate of vesting. It would facilitate the transfer of trust property through providing an alternative to a court process for non-contentious cases. The court's supervision would be retained for contentious cases. We could not go as far as recommending a stand-alone statutory vesting provision as this would be inconsistent with the land transfer system's principle that the register can be relied on to accurately reflect ownership.
- 8.53 In most circumstances, the simplest way for trust property to be transferred will be for the departing trustee to transfer the property and register the change of ownership. Making this a statutory duty may assist remaining trustees in dealing with a removed trustee who refuses to transfer ownership. This is not a complete solution, however, as it could not be used when the trustee being removed lacks capacity or where it is discovered after removal that the property was not validly transferred.
- 8.54 We address these difficulties by recommending the Public Trust be authorised to issue a certificate of vesting on application by the continuing trustees. This would not supplant the role of the courts where there is a dispute and would only be available for non-contentious transfers. The Public Trust would check the deeds removing and replacing trustees and seek a statutory declaration from the person with the power to appoint and remove trustees affirming that the former trustee was removed for a valid reason under the legislation. If there are objections from the departing trustee, the property arrangement is complex or it is not clear that the trustee was properly removed, the Public Trust should refuse to grant a certificate and the continuing trustees should apply to court for a transfer order instead. If there are no objections or concerns, the Public Trust can issue the certificate.

236 Section 47 provides that a deed of appointment or discharge operates to vest trust property. It does not apply to some property, including land, or shares or stocks that are transferable only in books kept by a company or other body. The Act allows the court to make an order vesting land (s 52) and stocks and other intangible property (s 59) in limited circumstances. Under s 57, a vesting order takes effect as if the previous trustee had transferred the property but land interests must still be registered.

237 The recent case of *Re Wilson* [2013] NZHC 1365 illustrates this point. This was a straightforward application for the High Court to vest land currently in the name of the former trustee of a testamentary trust in the new trustees as the former trustee was now 90 years old and no longer had the mental capacity to effect the transfer. The Court was satisfied the order to vest the land should be made and the costs of the application were met by the estate.

- 8.55 The certificate could be lodged with Land Information New Zealand, share registries or a similar entity as evidence of change of ownership and would constitute sufficient proof of change of ownership for their purposes. Because the certificate would require a statutory declaration, there would be personal remedies against continuing trustees who dishonestly used a certificate of vesting to transfer property. The new Act would provide that no registry would be liable for relying on a statutory vesting certificate.
- 8.56 This option is preferred to that of giving the continuing trustees or those with the ability to appoint and remove trustees the power to unilaterally transfer assets. While this latter approach would have the advantage of simplicity, there are risks in foregoing any form of independent supervision. Combined with the power to remove trustees, this could freeze out a dissenting trustee and facilitate breaches of trust.

### **APPLICATION TO EXISTING TRUSTS**

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- 8.57 All recommendations in this chapter should apply to existing as well as new trusts. The recommendations provide increased clarity and improved procedures for the discharge and replacement of trustees.

# Chapter 9

## Custodian and advisory trustees

### INTRODUCTION

- 9.1 This chapter addresses reforms to the provisions relating to advisory and custodian trusteeship. These two mechanisms each allow for an arrangement in which there is another party with a role in the trust relationship. These reforms were discussed more extensively in the *Preferred Approach Paper* and the *Fourth Issues Paper*.<sup>238</sup>

### CUSTODIAN TRUSTEES

#### RECOMMENDATION

R27 The new Trusts Act should re-enact section 50 of the Trustee Act 1956 in modernised form with the following clarifications, additions and reforms:

- (a) continue to provide for the appointment of a corporation as a custodian trustee;
- (b) provide that, subject to the terms of the trust:
  - (i) the role of the custodian trustee is to hold the trust property, invest funds and dispose of the assets as the managing trustee directs in writing;
  - (ii) the trust property vests in the custodian trustee as if the custodian trustee were the sole trustee;
  - (iii) the management of the trust property and exercise of all powers and discretions exercisable by the trustee under the trust remain vested in the managing trustees as if there were no custodian trustee;
  - (iv) the custodian trustee has all the administrative powers of a trustee but none of the discretionary powers;
  - (v) the custodian trustee has the power to execute any documents or perform any administrative action directed by the managing trustee; and
  - (vi) the custodian trustee may be appointed over part of the trust fund.
- (c) provide that the custodian trustee must act on the instructions of the managing trustee and is liable for loss caused by:
  - (i) failing to execute the instructions of the managing trustee; or
  - (ii) acting without the authority of the managing trustee;
- (d) provide that the custodian trustee is not liable for executing instructions of the managing trustee where the managing trustee is in breach of trust;

<sup>238</sup> Law Commission *Review of the Law of Trusts – Preferred Approach* (NZLC IP31, 2012) at ch 7; Law Commission *The Duties, Office and Powers of a Trustee: Review of the Law of Trusts – Fourth Issues Paper* (NZLC IP26, 2011).

- (e) provide that the custodian trustee may apply to the court for directions if it receives instructions from the managing trustee that it suspects are in breach of trust, but shall not be liable for a failure to do so;
- (f) provide that, in addition to any remuneration or commission payable to the custodian trustee, the custodian trustee has the benefit of the right of indemnity in respect of costs incurred by the custodian trustee; and
- (g) provide that the appointment of a custodian trustee must be in writing.

### What are custodian trustees?

9.2 Custodian trusteeship is a mechanism that allows for the appointment of a corporation as an ongoing bare trustee to hold assets on behalf of managing trustees.<sup>239</sup> If a custodian trustee is appointed, the custodian trustee's role is to hold and administer trust property on the instructions of the managing trustees.<sup>240</sup> The custodian trustee must accept the instructions of a majority of the managing trustees as if they were given by all the managing trustees. If the managing trustees change, there is no need to change the legal ownership of the trust assets. This mechanism allows for a separation between legal ownership, management, and beneficial interest. We understand that it is widely used in Māori land trusts, and trusts with overseas assets or an overseas managing trustee. Section 225 of Te Ture Whenua Maori Act 1993 applies when a custodian trustee of a Māori land trust is appointed.

### Reforms

9.3 We recommend that the role of custodian trusteeship is spelt out to a greater extent than it is in the current Act. This includes clarifying that custodian trusteeship is essentially an administrative role, and imposing duties and restrictions on liability. We do not propose changing the nature of the custodian trustee's role. The duties and liabilities included are consistent with the current conception of the role. Submitters on the *Preferred Approach Paper* did not have any issues with what was proposed.

9.4 We recommend clarification in relation to when a custodian trustee receives unlawful instructions from the managing trustees. The role of the custodian trustee is to act on the instructions of the managing trustees. It is not to check whether these instructions are valid. An injured beneficiary can recover from the managing trustees directly. We consider that the custodian trustee should only be liable where:

- the custodian trustee, on its own initiative, perpetrates a fraud against the trust;
- the custodian trustee fails to execute the instructions of the managing trustees, and thereby causes loss to the trust; and
- the custodian trustee acts independently of instructions from the managing trustees (but not fraudulently), and thereby causes loss to the trust.

9.5 These situations would arise only where the custodian trustee acted without the authority of the managing trustees. The new Act should provide that the custodian trustee is liable for failing to execute the instructions of the managing trustees and acting without their authority. These should be mandatory provisions for which liability cannot be excluded. The legislation should

<sup>239</sup> Noel C Kelly, Chris Kelly and Greg Kelly *Garrow and Kelly Law of Trusts and Trustees* (6th ed, LexisNexis, Wellington, 2005) at 445. In this context the term "bare trustee" is used to describe a trustee having minimal duties, and no role in exercising discretion to distribute trust assets.

<sup>240</sup> Trustee Act 1956, s 50(2)(c).

also provide that the custodian trustee has the duty to act on the instructions of the managing trustees and has all the administrative powers of a trustee, although is not able to exercise discretion.

- 9.6 In order for custodian trustees to efficiently deal with property and to improve clarity, we recommend that the new Act provide that a custodian trustee is entitled to indemnity from the trust fund. We also recommend that a custodian trustee be able to be appointed over part of the trust property as the default position, as this may be useful in some circumstances and is consistent with the purpose of custodian trusteeship.
- 9.7 The recommendation differs from the original proposal in the *Preferred Approach Paper* by not extending the role of custodian trustee to natural persons.<sup>241</sup> We now consider that it is better to retain the current scope of the custodian trustee role. The appropriateness of retaining this role for corporations may be reconsidered in the context of the Law Commission's corporate trustee review. We also are no longer proposing to allow multiple custodian trustees, because of the need to be cautious about altering this role when we are not aware that there are any problems with the current approach.
- 9.8 These changes mean that the new Act, like the Trustee Act, will differ from Te Ture Whenua Maori Act in the nature of custodian trusteeship. In the Māori land trust context it is appropriate to allow multiple custodian trustees and natural person custodian trustees because the custodian mechanism is relied upon to enable those trusts to be managed effectively and efficiently where there are large numbers of trustees. Our recommendations are not intended to affect the application of section 225 of Te Ture Whenua Maori Act.

## ADVISORY TRUSTEES (SPECIAL TRUST ADVISERS)

### RECOMMENDATION

R28 The new Trusts Act should re-enact section 49 of the Trustee Act 1956 in modernised form with the "advisory trustee" renamed the "special trust adviser" and with the following clarifications and reforms:

- (a) a special trust adviser may advise the trustee on any matter relating to the trust;
- (b) a special trust adviser is not a trustee, and does not have the powers and duties of a trustee;
- (c) the trustee is not liable for anything done or omitted by the trustee by reason of following the special trust adviser's advice unless the trustee is acting dishonestly, in wilful breach of trust or grossly negligent in following the advice (replacing proviso (c) to section 49(3) of the Trustee Act 1956); and
- (d) the trustee is not liable for a breach of trust merely because the trustee elects not to follow the special trust adviser's advice.

### Role of the special trust adviser

- 9.9 Section 49 of the Trustee Act is a default provision that provides for the appointment of advisory trustees by the settlor, the court, a trustee or a person with a power to appoint a trustee. An advisory trustee is not a real trustee, as he or she does not have legal ownership

<sup>241</sup> *Preferred Approach Paper*, above n 238, at P29.



of the property or the powers or duties of a trustee. The advisory trustee is an adviser to the real trustee. The trust property remains vested in the trustee who retains sole management and administration of the trust. The trustee may consult the advisory trustee on any matter relating to the trust or trust property.

- 9.10 This statute-created adviser (which we recommend should be called a special trust adviser) is still considered a useful part of the New Zealand's trusts framework. Trustee corporations, including the Māori Trustee, commonly use advisory trustees as they enable family members or advisers to be involved and oversee the administration of the trust while allowing the trustee corporation to do the day to day administration. Submissions also indicated that advisory trustees may be settlors, particularly those with special skills that can help the trustees, and experts, such as financial advisers.

### Liability of trustees

- 9.11 The area where there is a need for statutory reform relates to the trustee's liability when following the adviser's advice. Currently the trustee is not required to follow advisory trustees' advice, but the trustee's liability is limited when following it. There is a lack of clarity about the extent of the protection from liability in proviso (c) to subsection (3) of section 49. The wording is confusing as it could be interpreted as a blanket protection for the trustee from liability when following an adviser's advice. However, this seems unlikely in the context of the section as proviso (d) implies that the trustee is not entitled to rely on the advisory trustee's advice if the trustee considers it would breach the trust or the law.
- 9.12 There was some concern from submitters regarding our original proposal to clarify that the trustee is liable if he or she "knew or ought to have known" that the advice of an adviser was unlawful, contrary to the terms of the trust or trustee's duties, or was advice that no reasonable adviser would have given. Several submitters considered that trustees should be able to rely on the advice of an adviser without fear of liability. A number were concerned about making trustees liable where they "ought to have known" that a course of action was unlawful or would breach the trust because this would impose an unreasonable burden on trustees. Conversely, some submitters were concerned about the gap in accountability that exists where a trustee is absolved of any liability when he or she relies on a special trust adviser's advice.
- 9.13 The intention with section 49 seems to be to create an adviser with a formal status within the trust arrangement in whom trustees are entitled to have some confidence. The person appointing an adviser is generally the settlor, the court or a person with the power to appoint trustees, although it may be the trustee. It seems appropriate that there is some protection from liability for a trustee relying upon an adviser because of the statutory status of this adviser, but that this should not be a blanket protection or too extensive in order not to dilute the trustee's responsibility too far. A trustee should still be required to understand the terms of the trust and recognise potential breaches of trust.
- 9.14 We accept that it is overly onerous to remove the protection from liability when a trustee ought to have known that an adviser's advice was in breach of trust or unlawful. Instead we recommend that the language used in relation to the restriction on trustee exemption clauses is used here: the trustee will not be liable when relying on the adviser's advice unless in following the advice the trustee is dishonest or is grossly negligent. We think that trustees should be afforded the same degree of protection from liability as they can have under an exemption clause but it should not go as far as a blanket protection from liability.

- 9.15 We recommend that it should not be mandatory for trustees to apply to the court for direction when the adviser's advice is unlawful, objectionable or exposes the trustee to liability.<sup>242</sup>

#### **APPLICATION TO EXISTING TRUSTS**

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- 9.16 The recommendations regarding custodian trustees and special trust advisers should apply to all trusts, including existing trusts. The recommendations are based upon current provisions and do not shift away from or narrow these in a way that would be detrimental to existing trusts. We do not see any difficulty with this recommendation applying to existing appointments.

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<sup>242</sup> This is consistent with the Select Committee's version of the Trustee Amendment Bill 2007 ((144-2) (select committee report)), but differs from what was proposed in the Law Commission's 2002 Report *Some Problems in the Law of Trusts* (NZLC R79, 2002) at 24.

# Part 4

## COURT POWERS AND JURISDICTION



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# Chapter 10

## Revocation and variation

### INTRODUCTION

- 10.1 While the general rule is that trusts, once established, cannot be varied, changes in law, taxation rules and family circumstances can mean that trust deeds need to be modified to enable the trust property to be dealt with or the trust administered in a different way. The law has long recognised that there are circumstances where trusts should be able to be varied, brought to an end (revoked) or resettled onto new trusts. In this chapter we make recommendations relating to the revocation and variation of trusts. These issues were discussed more extensively in the *Preferred Approach Paper* and *Third Issues Paper*.<sup>243</sup>

### REVOCAION AND VARIATION BY BENEFICIARIES

#### RECOMMENDATION

R29 The new Trusts Act should:

- (1) State the common law rule (known as the rule in *Saunders v Vautier*) which provides that:
  - (a) where they are in agreement, legally capable adult beneficiaries who hold the entire beneficial interest in the trust property may act together to revoke a trust and require the trustees to distribute the trust property as they direct; and
  - (b) a legally capable adult beneficiary of a fixed share of trust property may, where the beneficiary has an absolute vested interest in that share, request the trustees to transfer that share to him or her. The trustees may only refuse to do so where the property is not in a form, or cannot be changed into such a form, that allows the beneficiary's share to be transferred to the beneficiary without detrimentally affecting the interests of other beneficiaries.
- (2) Clarify that where they are in agreement, and with the agreement of the trustees, legally capable adult beneficiaries who hold the entire beneficial interest in the trust property may act together to confer new powers upon trustees or deviate from, or vary, the terms of the trust.
- (3) Clarify that legally capable adult beneficiaries who hold the entire beneficial interest in the trust property may consent to a resettlement of a trust, as well as a variation or revocation.

<sup>243</sup> Law Commission *Review of the Law of Trusts – Preferred Approach* (NZLC IP31, 2012) at ch 9; Law Commission *Perpetuities and the Revocation and Variation of Trusts: Review of the Law of Trusts – Third Issues Paper* (NZLC IP22, 2011) at pt 2.

## Legislation to clarify the extended rule in *Saunders v Vautier*

- 10.2 The Trustee Act 1956 does not address the circumstances under which beneficiaries are able to revoke, vary or resettlement a trust by agreement. Currently the rules that apply are a matter for case law as developed by the courts. The original rule in *Saunders v Vautier* provided that where the beneficiaries of a trust are all adults with full legal competence and are in agreement, they can act together to require the trustees to terminate the trust and transfer the trust property to them to distribute as they see fit.<sup>244</sup> The rule in *Saunders v Vautier* may also be used to transfer to a legally capable adult beneficiary of a fixed share of the trust property his or her share, provided the trust property is in a form that will allow the transfer of that share to him or her.<sup>245</sup> However, this aspect of the rule does not apply if the beneficiary's interest is not an absolute vested one.<sup>246</sup> A beneficiary cannot request the revocation of a trust where their interest is contingent unless all beneficiaries agree (including those who would benefit if the contingency were not met).
- 10.3 The scope of the rule in *Saunders v Vautier* has broadened over time and the courts have allowed beneficiaries to use the rule to confer new powers upon trustees or deviate from, or vary, the terms of the trust where the trustees are in agreement with the change.<sup>247</sup> It is likely that the rule also applies to allow beneficiaries to consent to a resettlement of a trust as this would be consistent with the policy that those with the beneficial interest in property should be able to determine what happens to that property. In all cases where the original trusts are not simply being revoked, the agreement of the trustees is required, because the trustees are responsible for managing the trust in the interests of the trust's beneficiaries.
- 10.4 While the case law rules are reasonably clear in many respects, they are not necessarily known or understood by lay people involved with trusts. A majority of submitters (including the New Zealand Law Society) favoured codifying on the basis it would make the law more accessible for lay people and that it would also help place the court's powers to approve variations into context. Some submitters expressed concern over the potential for unintended consequences to arise if established trust law principles in this area were encapsulated in statute.
- 10.5 We consider that a clear statement of the law in this area would have significant educative value and recommend codifying the case law rule. We consider that concerns over inadvertent modification of the law when codifying can be addressed by carefully wording the statutory provision (see clauses 51 to 53 of the indicative draft at the end of this chapter). These clauses give effect to and illustrate our recommendation (R29).
- 10.6 By legislating it is also possible to address the uncertainty at the edges of the rule. The new Act should clarify that legally capable adult beneficiaries may consent to a resettlement of a trust, as well as a variation or revocation. The agreement of the trustee will always be required in cases where the original trusts continue, to avoid the trustees being burdened by obligations to which they may not have agreed.

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244 *Saunders v Vautier* (1841) Cr & Ph 240, 41 ER 482 (Ch).

245 Andrew S Butler "Trustees and Beneficiaries" in Andrew S Butler (ed) *Equity and Trusts in New Zealand* (2nd ed, Thomson Reuters, Wellington, 2009) 105 at 147; *Quinton v Proctor* [1998] 4 VR 469.

246 *Burns v Steel* [2006] 1 NZLR 559 (HC) at [36]; Noel C Kelly, Chris Kelly and Greg Kelly *Garrow and Kelly Law of Trusts and Trustees* (6th ed, LexisNexis, Wellington, 2005), at [25.5.2].

247 *Re Philips New Zealand Ltd* [1997] 1 NZLR 93 (HC) at 101. This is also the position in the United Kingdom; see *Neville v Wilson* [1996] 3 All ER 171 (CA).

## REVOCAION AND VARIATION BY THE COURT

### RECOMMENDATION

R30 The new Trusts Act should provide that:

- (1) The court may:
  - (a) approve any revocation, variation or resettlement of a trust or any change to the scope or nature of the powers of the trustees to manage or administer the trusts on behalf of the following beneficiaries:
    - (i) persons under the age of 18 years;
    - (ii) incapacitated persons;
    - (iii) persons who may become entitled at a future date or on the happening of a future event or once they become a member of a certain class; and
    - (iv) future persons; and
  - (b) waive the requirement for the consent of any other person and approve any revocation, variation or resettlement of a trust or any change to the scope or nature of the powers of the trustees to manage or administer the trusts.
- (2) When considering whether to approve or waive the requirement for consent to a revocation, variation or resettlement of a trust or any change to the scope or nature of the powers of the trustees under (1) the court must take into account the following factors:
  - (a) the nature of any person's interest and the effect any proposed varying arrangement may have on that interest;
  - (b) the benefit or detriment to any person that may result from the court approving any proposed varying arrangement;
  - (c) the benefit or detriment to any person that may result from the court declining to approve any proposed varying arrangement; and
  - (d) the intentions of the settlor to the extent these can be ascertained.
- (3) The court must not make an order under (1) of the proposed provision if its effect would be to reduce or remove any fixed indefeasible interest or interest that has vested absolutely in a beneficiary.
- (4) Any order of approval or waiver that is made by the court under (1) should be binding on all persons on whose behalf it is made (including any person who is the subject of an order of waiver) and the trusts should take effect as rearranged.

### Current position and issues

- 10.7 Where a trust has minor, incapacitated or unborn beneficiaries, the rule in *Saunders v Vautier* cannot be used and the trust can only be revoked, varied or resettled by the court unless specific provisions addressing this situation have been included in the trust deed.
- 10.8 Under section 64A of the Trustee Act the High Court has a discretionary power to approve on behalf of a minor, and certain incapacitated or unascertained beneficiaries, an arrangement

that varies or revokes a trust or enlarges the powers of the trustees in respect of property subject to a trust.<sup>248</sup> The court may only approve an arrangement if it is not to the “detriment” of the beneficiary on whose behalf it is consenting. Under its inherent jurisdiction the High Court can also authorise variations of trusts on behalf of incapable beneficiaries in other limited circumstances.<sup>249</sup>

- 10.9 The main problems the Commission identified with the current provision, which we discussed in detail in the *Preferred Approach Paper*,<sup>250</sup> are briefly that:
- (a) There is uncertainty over the range of varying arrangements the courts can approve on behalf of beneficiaries.
  - (b) The classes of beneficiaries for whom the court can approve varying arrangements are somewhat unclear and are also too limited. We consider that it is clear that the current provision does not adequately cater for the range of situations where the consent of beneficiaries cannot be reasonably obtained.
  - (c) The requirement in section 64A that any varying arrangement must not be to the “detriment” of those beneficiaries on behalf of whom the court provides consent is restrictive and arguably does not give the court sufficient discretion to consider the broader consequences of any proposed variation and its potential effect on all the beneficiaries of the trust.

### Recommended reform

- 10.10 We recommend replacing section 64A with a new provision that addresses these issues (see clauses 55 and 56 of the indicative draft below).

#### *Range of varying arrangements the court may approve*

- 10.11 In relation to the issue concerning the range of varying arrangements the courts should be able to approve on behalf of beneficiaries (issue (a) above), we recommend that the court have the power to approve any revocation, variation or resettlement of a trust or any change to the scope or nature of the powers of the trustees to manage or administer trusts. This clarifies that the court in its protective role is able to approve any variation or resettlement that a competent adult could approve. In our view it is logical that the court should be able to agree to any variation that an adult beneficiary might agree to under the extended rule in *Saunders v Vautier* because the purpose of the provision is for the court to make a protective decision for those beneficiaries who are not adults of full capacity, and are unable to reach their own view on proposed changes to the trust.
- 10.12 Some submitters were concerned that this approach would allow far-reaching revisions of trusts, extending beyond what the settlor would have wished. While we acknowledge their concern, we consider that it is preferable to leave it to the court to determine whether it should in all the circumstances approve an arrangement that extends beyond or differs from what the settlor may have wished. As discussed further below, the intention of the settlor and the primary purpose of the trust must be considered by the court as one of a number of relevant matters that the court weighs up when deciding whether to approve a revision of the trust.

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248 *Re Clifford (deceased)* HC Christchurch A30/82, 22 July 1993 at 11.

249 *Chapman v Chapman* [1954] AC 429 (HL); *Re Ebbett* [1974] 1 NZLR 392 (SC) at 396; *Re Gray (deceased)* [1956] NZLR 764 (SC).

250 *Preferred Approach Paper*, above n 243, at [9.14]–[9.45].

*Classes of persons*

- 10.13 On the issue of the classes of beneficiaries for whom the court should be able to approve varying arrangements (issue (b) above), we recommend broadening the current classes because we consider that the classes of person for whom the court can currently approve an arrangement under section 64A are too limited.
- 10.14 We also recommend giving the court discretion, subject to some important safeguards, to waive the requirement for the consent of any other person. This is to prevent desirable variations being thwarted in situations where one or more ascertainable beneficiaries cannot be traced or contacted despite reasonable efforts, or to deal with situations where there are numerous beneficiaries with a remote or negligible interest in a trust. In such situations it is impractical and costly to require the personal consent of each of them. We consider that it is unreasonable to allow people with interests of a remote or negligible nature to have power of veto over variations that are desired by beneficiaries with far more significant interests.
- 10.15 However, it is equally important to protect the position of a recalcitrant adult beneficiary with a fixed or indefeasible interest where he or she refuses to consent to a variation. Overriding the views of a beneficiary in this situation would not be consistent with the underlying principle in *Saunders v Vautier*. Those with the right of enjoyment in the property should be able to dictate the manner of enjoyment. Where a beneficiary with a fixed or indefeasible interest refuses to agree to a variation, overriding his or her refusal in a manner that removes or reduces that interest arguably amounts to an expropriation of property.
- 10.16 Our recommended approach addresses this issue by requiring that the court, when considering whether to waive the requirement for the consent of any beneficiary, take into account the nature of the interests of everyone affected by the proposed arrangement, and the benefits or detriments to those affected if the court approved that arrangement or if the court declined to approve the arrangement. In addition, the provision should include the important protection that the court must not use its discretionary power to reduce or remove any vested or indefeasible interest held by a beneficiary.

*The requirement for no detriment*

- 10.17 On the issue of whether the current detriment test should be retained (issue (c)), we recommend changing to a broader test under which the court must consider the nature of the person's interests and the effect the proposed variation will have on that interest, as well as the benefits or detriments that approving or not approving the change will have on all those beneficiaries who would be affected by the proposed arrangement. In addition, we recommend that the intentions of the settlor, to the extent that these can be ascertained, should also be considered by the court when determining whether to approve a variation.
- 10.18 We think that the intention of the settlor and the primary purpose of the trust should be considered as one of a number of relevant matters that the court weighs up when deciding whether approval should be given. We favour this approach because it strikes a balance between the competing interests. It does not limit the court's ability to approve varying arrangements that conflict with the settlor's primary intention or the trust's substratum where other relevant factors argue compellingly for such change. Equally, this approach does not allow the court or others to simply ignore the settlor's intention or wishes either.



### RECOMMENDATION

R31 The new Trusts Act should provide that:

- (1) The court may make amendments to the non-distributive administrative provisions of the terms of any trust where it considers this necessary to enable the trustees to efficiently manage trust property.
- (2) Under (1) the court may amend the terms of a trust to enlarge or extend the scope of the powers available to the trustees for administering or managing trust property.
- (3) The court may not make amendments to the terms of a trust that alter or otherwise change the beneficial interests under the trust under this recommendation.

### Section 64 of the Trustee Act

- 10.19 Section 64 of the Trustee Act is essentially administrative in nature. It empowers the court to sanction specific transactions that would be in the best interests of beneficiaries but would otherwise be difficult to effect. Before any transaction can be approved under section 64 the court must be satisfied that it would be inexpedient, difficult or impractical for the trustees to undertake the transaction without the court's assistance. The court must also be satisfied that the transaction in question is expedient for the trust as a whole, rather than just expedient for one or more of its beneficiaries. The provision does not permit the court to make changes to the beneficial interests under the trust. Beneficial interests can only be varied under section 64A.
- 10.20 Our review identified two main issues with section 64:<sup>251</sup>
- (a) The provision makes an unnecessary and confusing distinction between the court making an order conferring on the trustees the necessary powers to undertake a class of transactions and an order that simply amends the administrative provisions of the trust deed; and
  - (b) The threshold for court intervention is currently set too high. The court must be satisfied that it would be inexpedient, difficult or impractical to effect the transaction in question without the court's assistance.

### Recommended reform

- 10.21 Traditionally, section 64 has mainly been applied to authorise dealings with trust assets in a way that was not contemplated (or authorised) by the trust deed. As noted already, section 64 can be distinguished from the type of intervention undertaken under section 64A (which allows more substantive amendments to trusts including changes to provisions about beneficiaries). We recommend retaining this type of distinction and recommend a new provision to replace the current section 64.
- 10.22 We recommend that the scope of the current provision be broadened to permit the court to make orders amending the non-distributive administrative provisions of the trust deed where this is necessary to enable the trustees to efficiently manage trust property. We also recommend modifying the criteria for court intervention. Trustees should simply be required to show that the change is necessary for the efficient management of the trust assets.

<sup>251</sup> These are discussed more fully in *Preferred Approach Paper*, above n 243, at [9.46]–[9.61].

- 10.23 Submitters generally favoured this type of approach. However, some submitters expressed a clear desire to restrict a new provision (replacing section 64) to amendments that are for the administration and management of the trust assets rather than more substantive changes. Submitters were concerned that the law should not lightly override a settlor's decisions as to what restriction should be placed on trustees' powers by allowing *carte blanche* modification of the terms of the trust.
- 10.24 The counter-argument, which other submitters also raised, is that over time the circumstances and business practices surrounding trusts change. It is sensible, if not essential, to provide some avenue for trustees to apply to the court for amendments to ensure the non-distributive administrative provisions of a trust are adequate to enable them to efficiently manage trust property when circumstances change in this way.
- 10.25 We consider that our recommended approach strikes an appropriate balance between the competing concerns of administrative expediency and respecting the settlor's wishes. Clause 57 of the indicative draft illustrates the recommendation.

## VARIATION PURSUANT TO A TRUST DEED

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### Current position

- 10.26 Variation and resettlement powers are commonly included in trust deeds. Variation powers usually lie with the trustees, but may be reserved to the settlor or some other person. It is also possible to include a revocation power in a trust deed, although we understand that such provisions are uncommon these days.
- 10.27 The extent of any such variation or resettlement power will depend on the interpretation of the clause and the trust deed itself. The principles applying to the interpretation of contracts are also applied to the interpretation of trusts. The nature of a trust, for example, whether it is a family trust, a superannuation trust, debenture trust, or energy trust, also influences how its provisions are interpreted.<sup>252</sup> It is therefore difficult to identify definitive rules from case law that could guide the use of variation clauses. Clauses need to be construed in the context of the type of trust involved and the particular wording employed.
- 10.28 Generally "clear words" giving a power of variation are required. When interpreting a clause the court will "construe each provision according to its natural meaning, and in such a way to give it its most ample operation".<sup>253</sup> A general broad power giving the trustees the fullest possible powers or the powers of a natural person cannot be used by trustees to change or add to their own powers and duties created by the trust deed. These types of general powers are normally interpreted as supplementing the other specific powers given by the deed, but not as intending to convey a power of variation. There is a rebuttable presumption that a variation power cannot be used to extend its own scope or amend its own terms.<sup>254</sup> Trustees cannot use variation powers to remove a specific restriction to which they were subject from the very foundation of the trust.<sup>255</sup>

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252 Kelly, Kelly and Kelly, above n 246, at ch 11.

253 *Kearns v Hill* (1990) 21 NSWLR 107 (SC) at 109.

254 David Hayton, Paul Matthews and Charles Mitchell (eds) *Underhill and Hayton: Law of Trusts and Trustees* (18th ed, LexisNexis, London, 2010) at [43.19].

255 *Re UEB Pension Plan* [1992] 1 NZLR 294 (CA) at 301.

## Recommend no change

- 10.29 As part of our review we considered whether the case law should be stated in legislation and whether legislation should provide guidance on how such clauses should be interpreted. There was no support for either of these possible approaches from submitters over the course of our review.
- 10.30 Given the need for a contextual approach to be taken to the interpretation of variation and resettlement powers, we also see little benefit in trying to include guidance in new legislation. Our view is that variation clauses should continue to be construed on a case by case basis according to the existing principles of interpretation. The existing principles of interpretation are well understood and flexible. We recommend no change in this area. There is also a concern that enacting statutory guidance in this area risks stifling further development of the principles of interpretation. There is merit in allowing a consistent approach to the interpretation of legal documents to be developed by the courts in all areas of law.

## APPLICATION TO EXISTING TRUSTS

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- 10.31 We see no difficulty with the new revocation and variation provisions recommended in this chapter applying to all trusts, whether settled before or after the enactment of the new Act.
- 10.32 Where proceedings have been commenced under the current variation provisions of the Trustee Act (section 64 or section 64A) there are two workable options for dealing with the transition. First, existing proceedings could simply be completed under the existing provisions of the Trustee Act. Where proceedings are part heard they may need to be completed under the Trustee Act anyway. The second option would be for the provisions replacing sections 64 and 64A to apply, and for the court to make orders under those provisions. We think that any final decision about how existing proceedings under the current Act should be treated is probably best made during the preparation of a draft Bill.

## INDICATIVE DRAFT PROVISIONS

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### Part 4 Administration of trusts

#### Subpart 1—Revocation and variation of trusts

##### 51 Revocation by unanimous consent of beneficiaries

- (1) The trustees of a trust must terminate the trust and distribute the trust property on being required to do so by the beneficiaries if the conditions set out in subsection (2) are satisfied.
- (2) The conditions for the termination of the trust under subsection (1) are as follows:
  - (a) the trustees have received a written notice requiring the trustees to terminate the trust; and
  - (b) the notice is signed by each beneficiary or by the duly authorised agent of that beneficiary; and
  - (c) each beneficiary is, at the date of receipt of the notice, 18 years of age or older and otherwise a person of full legal capacity.

- (3) The conditions in **subsection (2)** are treated as satisfied in respect of a person on whose behalf the court has made an order of approval under **section 54** or an order of waiver of consent under **section 55**.

## 52 Other actions with unanimous consent of beneficiaries

- (1) The beneficiaries of a trust acting unanimously may do any of the following things, if the conditions set out in **subsection (2)** are satisfied:
- (a) confer new powers upon the trustees:
  - (b) vary the terms of the trust:
  - (c) deviate from the terms of the trust:
  - (d) consent to the resettlement of the trust.
- (2) The conditions for an action by the beneficiaries under **subsection (1)** are:
- (a) the trustees have received a written notice of the proposed new powers, variation, deviation, or resettlement, as the case may be; and
  - (b) the notice is signed by each beneficiary or by the duly authorised agent of that beneficiary; and
  - (c) each beneficiary is 18 years of age or older and otherwise a person of full legal capacity; and
  - (d) the trustees have agreed to the proposal.
- (3) The conditions in **subsection (2)** are treated as satisfied in respect of a person on whose behalf the court has made an order of approval under **section 54** or an order of waiver of consent under **section 55**.

## 53 Beneficiary's right to share of trust property

A beneficiary of a fixed share of the trust property may require the trustees to transfer that share to the beneficiary (and the trustees must do so) if—

- (a) the beneficiary is absolutely entitled to that share (for example, any condition relating to the vesting of that share set by the terms of the trust has been met); and
- (b) the property is in a form, or can be changed into a form, that can be transferred to the beneficiary; and
- (c) the transfer is not detrimental to the interests of the other beneficiaries; and
- (d) the beneficiary is 18 years of age or older and otherwise a person of full legal capacity.

## 54 Power of court to approve revocation, variation, or resettlement of trust

- (1) The court may, on behalf of any of the persons set out in **subsection (2)** who has an interest in property held under a trust, approve the revocation, variation, or resettlement of the trust.
- (2) The persons referred to in **subsection (1)** are as follows:
- (a) a person under the age of 18 years:
  - (b) a person who lacks full legal capacity:
  - (c) a person who may acquire an interest at a future date or on the happening of a future event or on becoming a member of a certain class of persons:
  - (d) a future person.

- (3) On an application for an order of approval under **subsection (1)**, the court—
  - (a) must take into account the following factors:
    - (i) the nature of any person’s interest in the trust property and the effect of the proposed order on that interest; and
    - (ii) the benefit or detriment that may result from the proposed order to any person having an interest in the trust property; and
    - (iii) the benefit or detriment that may result to any person having an interest in the trust property if the court refuses to make the proposed order; and
    - (iv) the intentions of the settlor of the trust in settling the trust property, if it is practicable to ascertain those intentions; and
  - (b) must not make an order of approval if its effect would be to reduce or remove any vested interest in the trust property or other property right held by a beneficiary.
- (4) An order of approval under **subsection (1)** binds the person on whose behalf it is made and takes effect without any further step.
- (5) In this section, **interest** includes—
  - (a) a direct or an indirect interest:
  - (b) a contingent interest.

**55 Power of court to waive requirement of consent to revocation, variation, or resettlement of trust**

- (1) The court may waive the requirement that the consent of a person be obtained for the revocation, variation, or resettlement of a trust.
- (2) On an application for an order of waiver of consent under **subsection (1)**, the court—
  - (a) must take into account the following factors:
    - (i) the nature of any person’s interest in the trust property and the effect of the proposed order on that interest; and
    - (ii) the benefit or detriment that may result from the proposed order to any person having an interest in the trust property; and
    - (iii) the benefit or detriment that may result to any person having an interest in the trust property if the court refuses to make the proposed order; and
    - (iv) the intentions of the settlor of the trust in settling the trust property, if it is practicable to ascertain those intentions; and
  - (b) must not make an order of waiver of consent if its effect would be to reduce or remove any vested interest in the trust property or other property right held by a beneficiary.
- (3) An order of waiver of consent under **subsection (1)** binds the person on whose behalf it is made and takes effect without any further step.
- (4) In this section, **interest** includes—
  - (a) a direct or an indirect interest:
  - (b) a contingent interest.

**56 Power of court to vary or extend trustees' powers in relation to property**

- (1) The court may vary or extend the powers of the trustees of a trust in relation to property transactions if—
  - (a) the court considers that the variation or extension is necessary for the proper management of the trust property; and
  - (b) the variation or extension does not alter or otherwise affect a beneficiary's interest under the trust.
- (2) An application for an order under **subsection (1)** may be made by—
  - (a) the trustees or any 1 of them;
  - (b) any person beneficially interested under the trust.
- (3) In this section, **property transaction**, in relation to trust property, means the acquisition of, disposition of, or other dealing with trust property and includes sale, lease, mortgage, surrender, release, purchase, investment, retention, and expenditure.

**Commentary**

The definition of beneficiary in clause 1 (Interpretation) of the Bill will apply. A beneficiary means a person who receives, or who will or may receive, a benefit under the terms of the trust; and includes a discretionary beneficiary; and may include the settlor or trustee.

# Chapter 11

## Reviewing the actions of trustees

### INTRODUCTION

- 11.1 This chapter considers the procedure under section 68 of the Trustee Act 1956 for reviewing the acts and decisions of trustees. The Commission recommends retaining and reforming that procedure as well as confirming that judges can review decisions made by trustees under both the new Trusts Act and under the trust deed. However, the grounds of review should be limited as to whether trustees have made a decision that was not reasonably open to them. It should not be the substitution of the judge's view of what was an appropriate decision for that of the trustee.
- 11.2 These issues were discussed more extensively in the *Preferred Approach Paper* and the *Fifth Issues Paper*.<sup>256</sup>

### REVIEWING ACTS AND DECISIONS OF TRUSTEES

#### RECOMMENDATION

- R32 The new Trusts Act should include a review provision to replace section 68 of the Trustee Act 1956 with the following features:
- (1) The court should be able to review the act, omission or decision (including a proposed act, omission or decision) of a trustee on the grounds that the act, omission or decision was not reasonably open to the trustee in the circumstances.
  - (2) The procedure for review should be a two stage process:
    - (a) an applicant for review should be required to put forward evidence that raises a genuine and substantial dispute as to whether the act, omission or decision in question was reasonably open to the trustee in the circumstances (first stage); and
    - (b) if the court is satisfied that the applicant has established a genuine and substantial dispute, the court must allow the trustee the opportunity to appear before the court and put forward evidence establishing that the act, omission or decision was reasonably open to the trustee in the circumstances (second stage).
  - (3) Where the court finds, on a balance of probabilities, that the trustee's act, omission or decision was not reasonably open to the trustee in the circumstances, the court may set aside the act or decision, restrain the trustee from acting or deciding the case, or in the case of an omission direct the trustee to act.

256 Law Commission *Review of the Law of Trusts – Preferred Approach* (NZLC IP31, 2012) at ch 10; Law Commission *Court Jurisdiction, Trading Trusts and Other Issues: Review of the Law of Trusts – Fifth Issues Paper* (NZLC IP28, 2011) at ch 1.

- (4) The court must not make any order under the provision that affects:
  - (a) a distribution of the trust property that has been made not in breach of trust and before the trustee had notice of the application; or
  - (b) any right or title acquired by a person in good faith and for value.
- (5) A trustee's act, omission or decision under a power either in the new Act or the terms of the trust would be subject to review under the new provision.
- (6) An application for review may only be made by:
  - (a) a beneficiary; or
  - (b) any personal representative of a beneficiary who lacks capacity (such as a parent or guardian of a minor beneficiary, or a property manager or holder of an enduring power of attorney for an incapacitated beneficiary).

### Current law and issues

- 11.3 Section 68 permits a beneficiary aggrieved by an act, omission or decision of a trustee to apply to the High Court to review that act, omission or decision. A beneficiary may also apply if he or she has reasonable grounds to anticipate that he or she will be aggrieved by an act, omission or decision of a trustee. The court may require the trustee to appear before it and substantiate the trustee's decision. The court may make any orders as are necessary in the circumstances, except that the court may not disturb any distribution of trust property that has been made without a breach of trust before the trustee was aware of the application to the court. The court also may not affect any right acquired by any person in good faith and for value.
- 11.4 Jurisdiction under section 68 can only be invoked by a person who is beneficially interested in the trust property. In addition, it is limited to acts, omissions or decisions of a trustee in the exercise of a power conferred by the Act. Trustees' powers conferred by trust deed or by another statute fall beyond the jurisdiction of section 68, as do powers conferred by court order.<sup>257</sup>
- 11.5 One significant issue is whether section 68 gives the court a greater ability to interfere with a trustee's decision than does the court's inherent jurisdiction to supervise the exercise of discretionary powers by trustees.<sup>258</sup> Section 68 is silent on this issue and does not prescribe the circumstances in which the court may interfere with a trustee's decision or action. This may give the court a wide power to interpose its guiding, or restraining, hand on the exercise by trustees of their powers and discretions. This was the approach taken by the court in the early case of *Rossiter v Wrigley*.<sup>259</sup> Here the Court seemed to consider that the standard for review was

<sup>257</sup> *Jaspers v Greenwood* [2012] NZHC 2433 at [19].

<sup>258</sup> The most comprehensive outline of the grounds for intervention under the court's inherent jurisdiction is in the decision of Fisher J in *Wrightson Ltd v Fletcher Challenge Nominees Ltd* (1998) 1 NZSC 40,388 (HC) at 40,413. In summary, the court will set aside the trustee's decision only where the trustee has:

- acted in bad faith or for an improper motive;
- failed to exercise the discretion by considering the wrong question or misinterpreting the trust deed;
- considered irrelevant considerations;
- failed to consider relevant considerations; or
- reached a decision that is perverse or capricious.

A further ground for intervention discussed in *Wrightson Ltd* and an earlier case is that the trustee must not have acted unreasonably in the exercise of the power or discretion. See *Craddock v Crowhen* (1995) 1 NZSC 40,331 (HC) at 40,331.

<sup>259</sup> *Rossiter v Wrigley* HC Hamilton A105/80, 3 July 1989.



whether the trustees acted reasonably or not in the steps that they took. More recently, in obiter comments in *Jaspers v Greenwood*, Kós J construed the provision more narrowly. He said:<sup>260</sup>

Section 68 does not confer upon the High Court the role of general court of appeal from trustees' decisions. The relevant beneficiary grievance must involve the exercise (or intended exercise) of a trustee power in a manner that is ultra vires, vitiable on the basis of relevance of considerations or bad faith, or unreasonable in a *Wednesbury* sense. In other words, the ordinary means of review of the exercise of a statutory power.

- 11.6 In *Wendt v Orr* the Supreme Court of Western Australia, when considering the Western Australian equivalent of section 68, was not prepared to limit itself in that way.<sup>261</sup> It considered that while the established grounds for intervention would allow the court to intervene, there may be other grounds as well.<sup>262</sup>
- 11.7 Another significant issue with the current section is whether the ordinary incidence of the onus lying on the applicant for review is altered in section 68. In *Rossiter v Wrigley* the Court required the applicant to do no more than satisfy the standing requirement before requiring the trustee to show that he had not breached a duty or standard.<sup>263</sup> More recently in *Jaspers v Greenwood*, the Court disagreed with this approach, finding that the onus was on the applicant.<sup>264</sup> In Queensland, where there have been a number of cases under a similarly worded provision,<sup>265</sup> the courts have considered that the onus is on the applicant beneficiary to show that the trustee has breached the appropriate standard of conduct required of trustees before they require a trustee to appear to defend his or her actions.<sup>266</sup>

### When should the court interfere with a trustee's decision or action?

- 11.8 A new provision should specify the standard against which the court will review trustees' decisions. If the new provision is silent there will be continued uncertainty about the standard expected of trustees when exercising their powers.
- 11.9 Some submitters argued that review by the courts under the provision should be limited to the grounds already developed by the court under its supervisory equitable jurisdiction because this reflects the court's role as a corrector of fundamentally flawed decisions and not a de facto trustee. There was little support from submitters for the court being invited simply to consider whether trustees have acted unreasonably. The New Zealand Law Society, for example, considered the word "unreasonably" to be imprecise and that various forms of noncompliance by a trustee could fall within the meaning of "unreasonable". It can also give the impression that the merits of a trustee's decision can be examined for reasonableness. The New Zealand Law Society considered that the term "irrational" (in the sense that no reasonable trustee could make the decision) was more precise and should be used instead.
- 11.10 In the *Preferred Approach Paper* we proposed making the standard one of whether the action or decision of the trustee "was one that was not reasonably open to the trustee in the circumstances".<sup>267</sup> This formulation was intended to capture existing grounds of review as developed by the High Court under its supervisory jurisdiction, including the ground of

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260 *Jaspers v Greenwood*, above n 257, at [22] (comments in obiter).

261 *Wendt v Orr* [2004] WASC 28.

262 At [56].

263 *Rossiter v Wrigley*, above n 259.

264 *Jaspers v Greenwood*, above n 257, at [23] (comments in obiter).

265 Trusts Act 1973 (Qld), s 8.

266 See the discussion on the Queensland cases in CEF Rickett "Reviewing a trustee's act, omission or decision under s 68 of the Trustee Act 1956" [1990] NZ Recent Law Review 69 at 80.

267 *Preferred Approach Paper*, above n 256, at P42(2).

“irrationality” in the sense of being a decision that no reasonable trustee could have made. Although the majority of submissions raised no concerns over the “not reasonably open” formulation, a few submitters thought it was too broad and there was a risk that it would be applied by the courts as a test of whether the trustee had acted reasonably. Conversely a few submitters also questioned whether that test captured all the current grounds for intervention, including unlawfulness, developed by the courts.

- 11.11 We have not considered it necessary to modify the wording to expressly include a reference to whether the act or decision was “unlawful”. We consider that this is not necessary and that an unlawful decision (because it is unlawful) would not be a decision that is reasonably open to the trustee. The test of “not reasonably open” we have recommended is one of whether or not the trustee’s action or decision was one of a range of options that was properly open to the trustee in the circumstances. It is our intention to capture, with this formulation, the established grounds for intervention developed by the court under its supervisory equitable jurisdiction, while also leaving open the possibility that the courts may need to further develop those grounds in the future.
- 11.12 It is important that the test in the statute broadly aligns with the approach taken under the court’s inherent jurisdiction to supervise trustees and review their actions. As has been noted in many cases and commentaries, the settlor has given the trustees, and not the courts, discretion to take action and make decisions in respect of the trust. The role of the court under the proposed review provision should continue to be a supervisory one, ensuring that actions and decisions entrusted to trustees are properly exercised by them. The court should not be invited to review the merits of the trustee’s decision or impose its own view as to what was reasonable in the circumstances.

### **What should an applicant be required to prove?**

- 11.13 We consider that the usual standard, which requires an applicant to show on the balance of probabilities that a trustee has acted improperly in the exercise of his or her powers sets too high a threshold for a beneficiary to overcome given the information asymmetry between trustees and beneficiaries. A trustee is not required to give reasons for the exercise of his or her discretions or decisions, and will not be required to do so under the changes we are recommending elsewhere in this Report. Without knowing the trustee’s reasons, it will be difficult for a beneficiary to challenge the exercise of a trustee’s powers as improper.
- 11.14 We consider that this rather defeats the purpose of a review provision, which is to provide a mechanism to allow beneficiaries to hold trustees to account. This concern was shared by a number of submitters. However, many submitters were also concerned that the bar not be set too low either. All submitters considered that there should be some obligation on an applicant to raise at least a tenable issue. Most also expressed concern that trustees should not end up having to respond to frivolous time and resource wasting nuisance claims by beneficiaries who merely disliked his or her decision or have a general sense of grievance.
- 11.15 In response, and to balance the interests of trustees and beneficiaries, we recommend a two stage process under which the applicant is first required to put some evidence before the court that raises a genuine and substantial dispute as to whether the trustees have acted properly in the exercise of their powers (first stage). Only then, if the court is satisfied that the applicant has raised a genuine and substantial dispute, should the trustee be required to appear before the court and put forward evidence that their action or decision was a proper one in the circumstances (second stage). By the term substantial we mean that the matter genuinely in dispute is not trivial. It should be a matter of genuine dispute that is of some importance for the trust’s beneficiaries.

## Actions and decisions under trust deeds should be within scope

11.16 We recommend that the review provision should apply to a trustee's actions and decisions whether they are made under a power in the new Act or the trust deed. This has the advantage of introducing a consistent standard across all actions. It also addresses current uncertainty over whether review is available where the same powers are contained in both the statute and the trust deed. Most submitters were in favour of this approach and argued that it is something of an anomaly to allow the court to review trustees when they exercise some powers but not when they exercise powers set out in the trust deed. It is also confusing and leads to inconsistencies in the law.

## Who should have standing to apply for a review?

- 11.17 At present the court has jurisdiction to review a decision of a trustee under section 68 only where an applicant has a beneficial interest in the trust property. The specific wording in the section is “any person who is beneficially interested in any trust property”. Some commentators and judges have suggested that it is arguable that discretionary beneficiaries cannot apply under the section,<sup>268</sup> while others have considered that it is likely that a person with contingent or vested interests, whether indefeasible or subject to divestment, would be considered “beneficially interested”.<sup>269</sup>
- 11.18 We consider that the same definition of beneficiary contained in draft clause 1 and discussed in chapter 4 should apply here.<sup>270</sup> This includes a discretionary beneficiary; and may include a settlor or trustee where they may receive a benefit under the trust.
- 11.19 Many submitters, including the New Zealand Law Society, argued that the new provision should not distinguish between beneficiaries of a trust and the objects of a power of appointment, and that both should be entitled to make an application. However, some submitters, responding to the *Preferred Approach Paper*,<sup>271</sup> were concerned that our definition of beneficiary was too broad and that it could allow trustees to be held to account by institutions or members of a class whose chances of receiving property in reality are remote. These submitters suggested that potential applicants should be limited to those beneficiaries who have or may have, sometime in the future, real prospects of receiving trust property.
- 11.20 While we acknowledge these concerns, we believe the risk is more theoretical than real. Although any beneficiary, no matter what their prospects of benefiting may be, would be free to bring an application for review, we consider the requirement that the applicant adduce evidence raising a genuine and substantial dispute is sufficient to address concerns over spurious nuisance claims. Our view is that the evidential threshold included as the first stage of the procedure for review will ensure that any applicant must have a genuine issue with the trustee's conduct before the court will properly consider an application.
- 11.21 In the *Preferred Approach Paper* we proposed that the guardians of minor beneficiaries and representatives of incapacitated beneficiaries should have standing to apply under the new provision.<sup>272</sup> This proposal raised no concern among submitters and we recommend the inclusion of these potential applicants. The *Preferred Approach Paper* also included a proposal that settlors should also be able to apply under the new provision. This proposal did however

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268 Rickett, above n 266, at 80; *Jaspers v Greenwood*, above n 257, at [21]–[24].

269 The authors of *Garrow and Kelly Law of Trusts and Trustees* express this view and cite *Johns v Johns* [2004] 3 NZLR 202 (CA) at [49] in support of their view of what beneficially interested might include; see Noel C Kelly, Chris Kelly and Greg Kelly *Garrow and Kelly Law of Trusts and Trustees* (6th ed, LexisNexis, Wellington, 2005) at [25.3.10].

270 See cl 1 of Appendix A.

271 *Preferred Approach Paper*, above n 256, at P42.

272 At P42(5).

raise concern among a few submitters. Having reconsidered that issue, we have decided not to recommend the inclusion of settlors who do not already fall within our definition of beneficiary. We consider that to give settlors review rights would be a significant change to the law in New Zealand and would alter the existing relationship between settlors and trustees.

- 11.22 The review provision we have recommended is not intended to remove the courts' inherent supervisory jurisdiction in respect of trusts. We consider that the courts' supervisory jurisdiction should remain. It would therefore be possible for a beneficiary to apply to the court under the inherent jurisdiction or the new provision. The preservation of the courts' supervisory jurisdiction would enable New Zealand to benefit from decisions in other common law countries where actions of trustees are reviewed.

## APPLICATION TO EXISTING TRUSTS

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- 11.23 The new review provision we recommend should apply to trustees in respect of all trusts, whether settled before or after the enactment of the new Act. However, only actions, omissions or decisions of trustees that occur after the date the new provision comes into force should be reviewable under the new provision. Section 68 of the Trustee Act would continue to apply (to the extent it is applicable) to anything done before the new provision takes effect.

## INDICATIVE DRAFT PROVISIONS

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### Part 3 Supervision of trustees

#### *Court's review power*

#### 49 Court may review trustee's act, omission, or decision

- (1) The court may review an act, omission, or decision (including a proposed act, omission, or decision) of a trustee of an express trust on the ground that the act, omission, or decision was or is not reasonably open to the trustee in the circumstances.
- (2) The court may review an act, omission, or decision under **subsection (1)** on the application only of—
  - (a) a beneficiary; or
  - (b) if a beneficiary does not have full legal capacity, his or her personal representative.
- (3) The review must be conducted in accordance with **section 50**.

#### 50 Procedure for trustee review

- (1) An applicant for review under **section 49** must adduce evidence that raises a genuine and substantial dispute as to whether the act, omission, or decision in question was or is reasonably open to the trustee in the circumstances.
- (2) If the court is satisfied that the applicant has established a genuine and substantial dispute, the court must allow the trustee the opportunity, and may require the trustee, to appear before it to adduce evidence establishing that the act, omission, or decision was or is reasonably open to the trustee in the circumstances.

- (3) If the court, after hearing the trustee, is satisfied on a balance of probabilities that the act, omission, or decision was or is not reasonably open to the trustee in the circumstances, the court may (but subject to subsection (4))—
  - (a) set aside the act or decision or direct the trustee to act in the case of an omission:
  - (b) restrain the trustee from acting or deciding in the case of a proposed act or decision, and direct the trustee to act in the case of a proposed omission:
  - (c) make such other orders as the court considers necessary.
- (4) The court must not make an order that affects—
  - (a) a distribution of the trust property that has been made not in breach of trust and before the trustee had notice of the application; or
  - (b) any right or title acquired by a person in good faith and for value.

### **Commentary**

The terminology “a genuine and substantial dispute” is intended to signal that the decision or action under review is not a trivial or unimportant matter. The word “substantial” is used in its broadest sense to exclude trivial issues and to signal that the matter under review is one of importance for the trust’s beneficiaries. The intention is to exclude nuisance claims, but not to set the bar so high that any genuine matter of dispute that is important to a beneficiary cannot be reviewed.

The definition of beneficiary in clause 1 (Interpretation) of the Bill will apply. A beneficiary means a person who receives, or who will or may receive, a benefit under the terms of the trust; and includes a discretionary beneficiary; and may include the settlor or trustee.

# Chapter 12

## Other powers of the court

### INTRODUCTION

- 12.1 A wide variety of unrelated powers are conferred on the court by various sections of the Trustee Act 1956. This chapter considers and makes recommendations in relation to the following sections of the Trustee Act:
- section 66 – applying to court for directions;
  - section 72 – authorising payment of commission;
  - section 74 – a power to make a beneficiary indemnify for breach of trust;
  - section 75 – barring claims and future claims;
  - sections 77 to 79 – payment of trust money to the Crown;
  - section 76 – distribution of shares of missing beneficiaries; and
  - section 35 – protection against creditors by means of advertising.
- 12.2 In broad terms, we recommend that each of these provisions be retained with some reform. These issues were discussed more extensively in the *Preferred Approach Paper* and the *Fifth Issues Paper*.<sup>273</sup>

### SECTION 66 – POWER OF COURT TO GIVE DIRECTIONS

#### RECOMMENDATION

R33 The new Trusts Act should provide:

- (1) That any trustee may apply to the court for directions concerning any property subject to a trust, or respecting the management or administration of any such property, or respecting the exercise of any power or discretion vested in the trustee (replacing section 66 of the Trustee Act 1956).
- (2) Whenever possible, a trustee should present to the court a proposed course of action or possible course of action regarding the matter on which the trustee seeks directions.
- (3) Every application for directions should be served upon, and the hearing attended by, any person interested in the application or such interested persons as the court otherwise determines.
- (4) For the avoidance of doubt:
  - (a) a court may refuse to provide directions if it would be more expedient for the issues to be addressed through a different form of proceedings;

<sup>273</sup> Law Commission *Review of the Law of Trusts – Preferred Approach* (NZLC IP31, 2012) at ch 11; Law Commission *Court Jurisdiction, Trading Trusts and Other Issues: Review of the Law of Trusts – Fifth Issues Paper* (NZLC IP28, 2011) at ch 2.

- (b) an application for directions under the section can only be made by a trustee for the time being of the trust in question; and
- (c) the court's power to give directions under (1) does not restrict the ability of the trustee to apply to the court for a declaration as to the interpretation of the trust instrument.

- 12.3 Section 66 of the Trustee Act provides that a trustee may apply to the court for directions concerning the trust property, the management or administration of trust property or the exercise of a power of discretion of the trustee. The section gives no further guidance.
- 12.4 However, case law has established some parameters as to when the section should or should not be used. The section is intended to assist trustees facing a choice between two or more courses of action, either of which might expose the trust to risk. Further, section 66 should only be used in the following circumstances: when the facts are clear, agreed upon and fully disclosed to the court; when no breach of trust is alleged or questions of law or interpretation are at issue; and when the issue cannot be simply resolved through legal advice or the independent exercise of discretion.<sup>274</sup> It is also established that the court should not go further than answering the questions posed. The courts have developed such parameters to prevent section 66 being used by overly-cautious trustees who should be exercising their discretion or seeking legal advice, or where alternative proceedings, such as breach of trust, would be more appropriate.
- 12.5 The new Trusts Act will need to retain the power to apply to the court for directions. In the interests of ensuring that the replacement section's meaning is clear on its face, we consider that the provision should include more detail about the types of circumstances for which directions may be sought and clarification about the availability of alternative proceedings. We do not think the revised section should go as far as detailing the case law principles that have been developed because it is desirable to have a relatively broad power of direction and for the courts to retain some discretion as to whether section 66 applies to the circumstances.
- 12.6 Submitters who commented on section 66 generally considered that it would be beneficial to incorporate case law principles into legislation so that the purpose of the section is more readily apparent, although most warned that the legislation should not be too prescriptive and that the court should retain discretion. Our recommended revision balances these competing concerns.
- 12.7 We also recommend the new provision clarify that only trustees can apply under the section, and should make it clear that this is only current trustees. We consider that this is unmistakably the intention of the current section despite some inconsistency in the case law that has suggested that beneficiaries may apply for directions under section 66.
- 12.8 Finally, we consider that it would also be helpful for the new provision to note the court's ability under its supervisory jurisdiction over trusts to make a declaration on the interpretation of a trust deed. It should also state that the court may refuse to provide directions if alternative proceedings would be better.

<sup>274</sup> Noel C Kelly, Chris Kelly and Greg Kelly *Garrow and Kelly Law of Trusts and Trustees* (6th ed, LexisNexis, Wellington, 2005) at 711–715; Andrew S Butler “Trustees and Beneficiaries” in Andrew S Butler (ed) *Equity and Trusts in New Zealand* (2nd ed, Thomson Reuters, Wellington, 2009) 105 at 144.

## SECTION 72 – PAYMENT OF A COMMISSION TO A TRUSTEE

## RECOMMENDATION

R34 The new Trusts Act should re-enact section 72 of the Trustee Act 1956 (under which the court may authorise payment of a reasonable fee or remuneration to a trustee out of trust property) subject to the following modifications:

- (1) The new provision (replacing section 72) should provide that when determining what payment would be just and reasonable the court must consider:
  - (a) the total amount that has already been paid to any trustee of the trust, whether pursuant to the terms of the trust or to any earlier order of the court or to any agreement or otherwise;
  - (b) the amount and difficulty of the services rendered by the trustee;
  - (c) the liabilities to which the trustee is or has been exposed, and the responsibilities imposed on the trustee;
  - (d) the skill and success of the trustee in administering the trust;
  - (e) the value of the trust property;
  - (f) the time and services reasonably required of the trustee;
  - (g) whether any payment that might otherwise have been allowed should be refused or reduced due to the conduct of the trustee in the administration of the trust; and
  - (h) all other circumstances that the court considers relevant.
- (2) The court should only authorise payment under the provision where the trustee has provided services above and beyond what would normally be expected from a trustee.

- 12.9 Currently under section 72 the court may authorise payment out of trust property of a “commission or percentage” to a trustee of an amount for the trustee’s services before, during, or on termination of the administration of the trust. The current section also lists a number of important factors that the court must have regard to when determining whether payment of commission would be just and reasonable.<sup>275</sup>
- 12.10 It is clear that the courts will continue to need this power to approve the payment of remuneration to trustees where that is just and reasonable. We recommend that section 72 be modernised and retained. The replacement provision in new trusts legislation should use contemporary terminology such as “a fee” or “remuneration” rather than “commission” and “percentage”.
- 12.11 The few submitters who commented on section 72 all favoured including in the new provision a non-exhaustive list of factors that should be taken into account by the court when determining whether to authorise payment to a trustee and the level of such remuneration. Some minor modifications to the current list were considered desirable. Our recommendation reflects these points.

<sup>275</sup> Trustee Act 1956, s 72(1A).



- 12.12 Finally, it should be acknowledged that payment of remuneration on the authority of the court under this section is one of the few exceptions to a trustee’s duty to act without reward and not to profit from trusteeship. We recommend that the replacement provision be drafted in a manner that makes it clear that payment is an exception to the trustee’s default duty to act without reward and that the courts will authorise payment under the provision only where the trustee has provided services above and beyond what would normally be expected from a trustee.

## SECTION 74 – BENEFICIARY INDEMNITY FOR BREACH OF TRUST

### RECOMMENDATION

R35 The new Trusts Act should:

- (1) Re-enact section 74 of the Trustee Act 1956, under which the court may, where a trustee has committed a breach of trust at the instigation or request or with the consent in writing of a beneficiary, make any order the court considers just indemnifying the trustee from the beneficiary’s interest in the trust property.
- (2) Remove the antiquated reference to “married women restrained from anticipation”.

- 12.13 Section 74 currently provides that if a trustee commits a breach of trust at the instigation, request or with the written consent of a beneficiary, the court may indemnify the trustee. All of the beneficiary’s entitlements may be confiscated or impounded by the court in order to make good the loss and indemnify the trustee. The right to confiscate a beneficiary’s interest is subject to the discretion of the court.
- 12.14 In practice the provision enables trustees to give effect to compromises and settlements reached by beneficiaries. The most common use made of it is where a Family Protection Act 1955 or similar claim is settled. In such cases a compromise arrangement may require the trustees to depart quite substantially from the terms of the trust stated in a will. Where the beneficiaries have agreed to such an arrangement and the trustee acts on this at their behest, it seems only right that the beneficiaries should accept responsibility for any departure from the terms of the trust. Although mainly applicable to trusts under a will, interests under lifetime trusts may also be compromised by agreement with the beneficiaries.
- 12.15 In cases where beneficiaries simply consent to a breach of trust, but do not do this in writing, section 74 is not available and beneficiaries cannot be made to indemnify trustees. However, at equity they may not be able to sue the trustees for any loss they suffer as a result of any breach to which they consented. In such circumstances the beneficiaries may also be liable to account to the trust for any profit they may have made from the breach of trust.
- 12.16 We recommend retaining the provision. The few submitters who commented on this issue agreed that the current provision should be retained largely unchanged in scope. All considered this type of provision necessary to deal with the types of compromise situations noted above.
- 12.17 Finally, section 74, as currently drafted, contains a now very antiquated reference to a beneficiary “who may be a married woman restrained from anticipation”. This presumably predates legislative changes giving married women full and equal status under law and is now unnecessary.

## SECTION 75 – BARRING CLAIMS AND FUTURE CLAIMS

## RECOMMENDATION

R36 The new Trusts Act should:

- (1) Include a provision (replacing section 75 of the Trustee Act 1956) under which a trustee may give notice to any claimant or potential claimant requiring the trustee to take proceedings within three months from the date of service; or to enforce the claim through the court.
- (2) Provide that where a potential claimant on whom notice has been served fails to take proceedings, or fails to enforce the claim through the courts, the trustee may apply to the court for an order to have the claim barred.
- (3) Provide that, as is currently provided in section 75, nothing in the new provision applies to any claim under the Family Protection Act 1955.

- 12.18 Under section 75 the trustee may serve upon any claimant or potential claimant a notice requiring him or her to take legal proceedings (within three months from the date of service) to enforce and prosecute the claim through court proceedings. At the expiry of the notice period the trustee may apply to the court for an order barring the person's claim. The claimant or prospective claimant must be served with the application seeking to bar the claim. The court may make an order barring the claim or allowing the trust property to be dealt with without regard to the claim.
- 12.19 For the purposes of section 75, a claim or potential claim means any claim in respect of any estate or trust property or against the trustee personally where the trustee is entitled to be reimbursed out of the trust fund. The section can be used whether the claim is made under the Law Reform (Testamentary Promises) Act 1949 or as a creditor, next of kin, or beneficiary under the trust. Section 75 expressly does not apply to any claim under the Family Protection Act 1955.
- 12.20 Section 75 of the Trustee Act confers powers on a trustee for the dual purposes of facilitating the prompt distribution of an estate and also for managing claims that the trustee considers ill-founded. Where a trustee has received a claim but is not prepared to pay it or agree to a compromise with the claimant he or she can utilise section 75. Also, where the trustee anticipates a claim that has not been made yet he or she can use section 75 to give notice to the prospective claimant.
- 12.21 There is no question that the provision must be retained. Except for an update of the language and drafting style, the Commission recommends that section 75 be re-enacted without change.
- 12.22 As briefly discussed in the *Preferred Approach Paper* we considered the suggestion by some submitters that it was inconsistent that section 75 extended to claims under the testamentary promises legislation but not to Family Protection Act claims.<sup>276</sup> As noted in that paper, our view is that the Family Protection Act differs from the testamentary promises legislation in that it has more of a social welfare intent rather than the semi-contractual nature of testamentary promises claims. Further, people cannot contract out of it, which we consider means that there is less of a case for allowing the barring of Family Protection Act claims. We have consequently not recommended any change to this aspect of the provision.

<sup>276</sup> At [11.38].

- 12.23 In the *Preferred Approach Paper* the Commission also decided to “test the waters” on an alternative process for barring small value claims without involving the courts.<sup>277</sup> Our concern was that the expense and time involved in applying to the court means that it is not worthwhile for trustees to apply to bar small claims. However, such outstanding claims impede a final distribution of the trust assets and thus cause practical difficulties. We therefore proposed a simplified procedure involving an application to the Public Trust where a claim was under \$15,000 and proceedings had not been commenced to establish or enforce the claim. Under the proposed small claims process the trustee would still have been required to give three months’ notice to prospective claimants. However, if proceedings were not commenced by the prospective claimant by the expiry of that period, the trustee would have applied to the Public Trust for a certificate barring the claim. The trustee would then have been free to deal with the trust property disregarding the claim.
- 12.24 While there was some support for a simplified process, there was general opposition to proposals to expand the role of the Public Trust in this and some of the other areas. Submitters considered that this and other roles of its kind proposed elsewhere in the *Preferred Approach Paper* were quasi-judicial in nature, and that it would not be appropriate given the Public Trust’s involvement in the market for it to undertake these types of functions. In the face of widespread opposition from practitioners and others in the trust sector we have decided not to pursue the small claims process. The concerns of submitters and our modified proposals in respect of the Public Trust are discussed in chapter 15.

## SECTIONS 77 TO 79 – PAYMENTS TO THE CROWN

### RECOMMENDATION

- R37 The new Trusts Act should re-enact, with the following changes, the provisions in sections 77 to 79 of the Trustee Act 1956 under which trustees may pay unclaimed monies over to the Crown where they are unable to find beneficiaries and distribute the monies:
- (1) The requirement for trustees to file an affidavit should be abolished and trustees should be required to give the Secretary to the Treasury information about the trust and beneficiaries (such as a copy of the trust deed and a statement of accounts).
  - (2) The Secretary to the Treasury should have a power to refuse to accept money where he or she is not given the required information about the trust and its beneficiaries.
  - (3) The obligation on the Secretary to the Treasury to publish a statement of all money held annually in the Gazette should be replaced by a more general requirement that he or she make that information publicly available in a manner that is likely to bring it to the attention of potential claimants. The obligation could in practice be fulfilled by putting the information into an online directory of unclaimed funds on a website.
  - (4) There should be no requirement on the Crown to pay any interest to claimants on any of the funds held under the provisions.
  - (5) The Crown should have a power to deduct any reasonable costs and expenses before making payment to any claimant.

<sup>277</sup> At [11.40].

- 12.25 Where beneficiaries cannot be located, trustees may be relieved of their responsibilities as trustees by paying trust money or securities over to the Crown. Under section 77 trustees (or a majority of them) may:
- (a) file an affidavit in the nearest High Court registry giving particulars of the trust and beneficiaries; and
  - (b) serve a copy of the affidavit on the Secretary to the Treasury; and
  - (c) pay the money or transfer the securities to the Crown.
- 12.26 Where the majority of trustees wish to make use of the provision but other trustees do not agree, the court can make an order under the section requiring payment or transfer to the Crown. A receipt from the Secretary to the Treasury discharges the trustees and the money and securities are then administered by the Treasury. Where money has been paid to the Crown under section 77, an *ex parte* application for recovery can later be made under section 79 by any person claiming an interest in money or securities held by the Crown. The court may make such orders as it thinks fit.
- 12.27 The Treasury holds monies paid under section 77 in a trust account for six years. The Treasury must publish a statement of all money and securities held by the Crown under section 78 in the *Gazette* at the end of each financial year.<sup>278</sup> The Treasury's practice is to list the name of individual beneficiaries, where these are known, as well as the names of the funds and the amount being held. Where someone is able to establish a claim, the Treasury may pay the money held to that person. The reasonable costs and expenses of the Crown may be deducted before payment is made.
- 12.28 Money that is not claimed and paid out during the six years that it is held in a trust account by the Treasury is ultimately transferred to the Crown bank account as unclaimed money.
- 12.29 It is recognised that some final backstop procedure of this kind is necessary. Trustees need to have access to a mechanism under which they can lawfully pay unclaimed monies over to the Crown when they are unable to find beneficiaries and distribute it.
- 12.30 All submitters agreed that these long provisions (spanning over four pages of dense text) should be simplified and all unnecessary procedural requirements removed. Submitters considered that the requirement to file an affidavit unnecessarily added to the cost of using the provisions. They considered that trustees should only need to give the Treasury copies of statements of account and of the relevant trust documents (such as deeds and wills). A requirement to provide information about the trust and its beneficiaries would be sufficient.
- 12.31 Submitters also considered that the requirement that the Treasury advertise in the *Gazette* was no longer appropriate. Few people ever see these advertisements so it would make more sense for the Treasury to place the material on a website so that information about missing beneficiaries would be available to anyone who wished to search for it. The New Zealand Law Society submission said that it was unclear under the current provision whether the Treasury could refuse to accept money where the required information was not given. We agree that this point should be clarified. We also recommend that sections 77 to 79 be simplified and all unnecessary procedural requirements and detail, including the requirement that trustees file an affidavit, be removed. We recommend a simpler, less expensive process for dealing with unclaimed money. Given the potential administrative costs, we consider that the Crown should retain the power to deduct any reasonable costs and expenses before making payment to any claimant.

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<sup>278</sup> Trustee Act 1956, s 78.

- 12.32 At present a significant amount of money is never claimed from the Treasury and ultimately is absorbed into the Crown Account. This suggests that notification in the *Gazette* is insufficient to bring the existence of funds to the notice of unaware beneficiaries. We recommend instead publication of a directory of unclaimed funds on a website.
- 12.33 Finally, as discussed in the *Preferred Approach Paper*, we consider that it would be sensible, at some future date, for the Government to consider amalgamating all the different provisions and arrangements the Crown has for dealing with unclaimed money into one regime.<sup>279</sup> At present the Unclaimed Money Act 1971 covers unclaimed money from deposits in banks, financial institutions, some money in solicitors' trust accounts, unclaimed proceeds of life insurance policies, and unpaid wages and employee benefits. Money is paid to the Commissioner of Inland Revenue under that Act. However, under some Acts other unclaimed money and assets are to be paid to the Public Trust, and under others to the Māori Trustee. In addition, unclaimed awards from court cases and reparations to victims of crime are held by the Ministry of Justice, and unclaimed prisoners' allowances are held by the Department of Corrections. The number of different arrangements involving different arms of the Crown suggests that a review of this whole area may be desirable.

## SECTION 76 – DISTRIBUTION OF SHARES OF MISSING BENEFICIARIES

### RECOMMENDATION

- R38 The new Trusts Act should re-enact section 76 of the Trustee Act 1956 (under which the court has broad powers to approve distributions by trustees where beneficiaries cannot be traced). The following changes should be made to the advertising requirements in the provision:
- (1) Trustees should be required to give notice advertising for potential beneficiaries in a manner that is likely to bring the notice to the attention of potential beneficiaries.
  - (2) Trustees may seek directions from the court where there is doubt as to what notice advertising for potential beneficiaries is appropriate.

- 12.34 Section 76 provides the machinery for ascertaining the existence or whereabouts of unknown or missing claimants. It is a long and impenetrable provision that essentially sets out a process for trustees to follow where beneficiaries cannot be ascertained. Under it the court may give directions where a trustee is uncertain about what advertisements to place to notify potential beneficiaries.
- 12.35 The court also has broad powers under the section to approve distribution where beneficiaries cannot be traced. The process has been used in a few cases involving pension funds that have largely been distributed, but where a handful of outstanding beneficiaries cannot be located despite extensive efforts on the part of trustees. Where trustees obtain and comply with such directions they are protected against personal liability.
- 12.36 Only a few submitters commented on this section. Most submitters considered the current section to be unnecessarily detailed and long. However, all agreed that there is a need for some means to deal with missing beneficiaries. Submitters also suggested that the provisions relating to advertising need to be future-proofed so that the new Act continues to be relevant over time. Rather than specifying where and how trustees should advertise, the section should simply

<sup>279</sup> *Preferred Approach Paper*, above n 273, at [11.57].

require trustees to make such enquiries and give notification (whether in a newspaper or a website or any other way) as the trustee considers necessary to bring the matter to the attention of any potential beneficiary. We agree and have recommended the provision be changed in this way.

- 12.37 A few submitters responding to our original discussion on section 76 in the *Fifth Issues Paper* suggested that applications to the High Court for directions on advertising for missing beneficiaries could largely be avoided if trustees and their advisers were encouraged to seek advice from the Public Trust, other trustee corporations or lawyers with experience in this type of work. Some noted that trustee corporations have had experience in locating missing beneficiaries. The Public Trust in particular deals with a number of intestate estates and consequently has processes in place to deal with the identification of widely dispersed families.
- 12.38 We agreed that it would be useful to include a mechanism for trustees to seek advice as an alternative to seeking directions from the court. In the *Preferred Approach Paper* we proposed that trustees should be able to seek advice from the Public Trust where there was doubt as to what notice advertising for potential beneficiaries was required.<sup>280</sup> Under our proposal the new provision replacing section 76 would have allowed trustees to rely on the Public Trust's advice and would have protected trustees who acted in reliance on such advice from liability. Trustees could, if they preferred, seek directions from the court, as an alternative to seeking advice from the Public Trust.
- 12.39 However, most submitters responding to this and other proposals in the *Preferred Approach Paper* that conferred new roles on the Public Trust, were strongly opposed to an expansion of that entity's functions into the advisory area. There was concern that the Public Trust was a market participant and should not have a statutory advantage over competitors in any advice-giving role.
- 12.40 We have taken these concerns into consideration and have reviewed our proposal. We have determined that it is not necessary for the new Act to expressly refer to the option of trustees seeking advice from the Public Trust or indeed from any other trustee corporations or lawyer with experience in this type of work. A prudent trustee, who was uncertain what notice advertising for potential beneficiaries should be given, would seek advice. Having reviewed the matter we consider that the proposed provision is unnecessary as a trustee is free to seek advice from the Public Trust anyway. It is probably also better to let trustees determine for themselves which potential adviser they wish to approach for this type of advice in all the circumstances.
- 12.41 Provided that a trustee has made a conscientious effort to bring the matter to the attention of potential beneficiaries and, where there has been doubt about what was needed, has taken proper advice, whether from a trustee corporation or from any other similarly experienced person, the trustee is likely to be released from liability where he or she has distributed funds on the basis of the information known.

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280 *Preferred Approach Paper*, above n 273, at [11.60].

## SECTION 35 – PROTECTION AGAINST CREDITORS BY MEANS OF ADVERTISING

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### RECOMMENDATION

R39 The new Trusts Act should re-enact section 35 of the Trustee Act 1956, which protects trustees from liability where they advertise and give notice to potential creditors before distributing property under a trust. The following changes should be made to the advertising requirements in the provision:

- (1) Trustees should be required to give notice advertising for claims in a manner that is likely to bring the notice to the attention of potential claimants.
- (2) Trustees may seek directions from the court where there is doubt as to what notice advertising for claims is appropriate.

12.42 Where there is doubt as to what advertisements should be published by a trustee giving notice advertising for claims before distributing property under a trust, the court has a power to give directions under section 35(4). Where the trustees obtain and comply with such directions they are protected against personal liability.

12.43 The options for modernising the approach to advertising and giving notice that we have just discussed in relation to section 76 also apply in relation to section 35. We recommend that the approach recommended for modernising the advertising requirements in section 76 should also be taken here. Again, for the reasons already discussed we have not proceeded with the proposal in the *Preferred Approach Paper* that would have conferred an advisory role on the Public Trust in relation to advertising for claims here either.

### APPLICATION TO EXISTING TRUSTS

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12.44 The new provisions recommended in this chapter should apply in respect of trusts settled before as well as those settled after the provisions come into force. Specific transitional arrangements will need to be made for dealing with situations where proceedings are already before the court, or trustees have begun other actions, such as advertising under section 35 of the existing provisions. Any final decision about how existing proceedings under the Trustee Act are addressed should be resolved in the course of preparing a draft Bill.

# Chapter 13

## Jurisdiction of the courts

### INTRODUCTION

- 13.1 This chapter makes recommendations relating to:<sup>281</sup>
- the respective jurisdictions of the High Court and District Court to determine proceedings under the proposed new Trusts Act; and
  - the jurisdiction of the Family Court to make orders and give directions under the new Act.
- 13.2 The arguments for and against the District Court and Family Court having jurisdiction under new trust legislation were fully canvassed in the *Fifth Issues Paper* and the *Preferred Approach Paper*.<sup>282</sup>

### HIGH COURT AND DISTRICT COURT JURISDICTION

#### RECOMMENDATION

R40 The new Trusts Act should provide that:

- (1) The High Court has jurisdiction to hear any matter and make any order under the proposed new Trusts Act. It should have exclusive jurisdiction to determine any proceeding under the new Act where the amount claimed, or the value of the property claimed or in issue, is more than the upper limit of the equitable jurisdiction of the District Court specified in section 34(1) of the District Courts Act 1947 (currently \$200,000) or any replacement provision.
- (2) The District Court should have jurisdiction under the new Act (concurrent with the High Court) to determine any proceeding where the amount claimed or the value of the property claimed or in issue is not more than the upper limit of the equitable jurisdiction of the District Court (currently \$200,000).
- (3) The District Court should also have jurisdiction (concurrent with the High Court) to determine any proceedings or applications (such as an application to appoint or remove a trustee) that does not involve any claim for money or property.
- (4) Where the District Court and High Court have concurrent jurisdiction the person who commences proceedings (the applicant) may decide whether to commence the proceedings in the District Court or High Court.
- (5) Section 43 of the District Courts Act 1947 should apply to the transfer of proceedings commenced in the District Court. The effect of this would be that:

281 In this Report we will refer to the District Court and the Family Court in the singular, although there are in fact 63 District Courts and Family Courts located throughout New Zealand. Each District Court is separately constituted under the District Courts Act 1947. Each Family Court was established as a division of each District Court by the Family Courts Act 1980.

282 Law Commission *Court Jurisdiction, Trading Trusts and Other Issues: Review of the Law of Trusts – Fifth Issues Paper* (NZLC IP28, 2011) at chs 1–3; and Law Commission *Review of the Law of Trusts – Preferred Approach* (NZLC IP31, 2012) at ch 12.



- (a) where the proceedings involve a claim for money, relief or property with a value that exceeds the amount specified in section 43 (currently \$50,000) a defendant may object to the proceeding being determined in the District Court and have the proceeding transferred (as of right) to the High Court; and
- (b) where the proceedings do not include a claim for money, relief or property with a value that exceeds the amount specified in section 43 a defendant wishing to transfer the proceedings must apply to the District Court for an order removing the proceedings to the High Court. Proceedings that do not include any claim for money, relief or property fall within this category under section 43.

#### Notes

- (1) The Government has announced, in response to the Law Commission Report *Review of the Judicature Act 1908: Towards a New Courts Act* that new courts legislation soon to be introduced will increase the upper financial limit of the District Court's equitable jurisdiction from \$200,000 to \$350,000 and will increase the threshold specified in section 43 over which claims may be transferred as of right to the High Court from \$50,000 to \$90,000.
- (2) Section 237 of Te Ture Whenua Maori Act 1993 will apply to give the Māori Land Court all of the powers of the High Court under the proposed new Trusts Act in respect of trusts to which Te Ture Whenua Maori Act 1993 applies.

### Concurrent jurisdiction for the High Court and District Court

- 13.3 Civil jurisdiction is divided between the High Court and District Court primarily on the basis of the monetary value of the matter in dispute. The District Court, like the High Court, has a broad civil and equitable jurisdiction. Over the years, since the Trustee Act 1956 came into force, the District Court's jurisdiction has expanded in equity, as well as in other areas. Parliament gave the District Court its current broad equitable jurisdiction in 1992. Under section 34(1)(a) of the District Courts Act 1947, the District Court now has the same general equitable jurisdiction as the High Court providing the amount claimed or the value of the property in issue does not exceed the monetary threshold set.
- 13.4 Conceptually, we consider that it makes little sense for the District Court to have the same general equitable jurisdiction as the High Court but not to have jurisdiction to exercise powers under a new Trusts Act. We consequently recommend that the District Court should have all the tools that are necessary to exercise its equitable jurisdiction effectively in respect of trusts and thus should have concurrent jurisdiction with the High Court for matters under a new Trusts Act. This is consistent with the District Court now being a court of general civil jurisdiction.
- 13.5 Submissions on the *Preferred Approach Paper* largely opposed the proposal that the District Court should have jurisdiction under the new Act. Some did acknowledge that conceptually the proposal made good sense given the respective civil functions of the two courts. However, submitters from within the legal profession were concerned that the District Court does not currently have the capacity to adequately handle potentially complex trust litigation. Many of these submissions consequently argued that the High Court should retain exclusive jurisdiction. We have considered these submissions but have not been persuaded by them.
- 13.6 We do not think that a special case can be made for trust law on the basis that it is inherently more complex than other areas of equity. Some trust cases do certainly involve complex issues,

but so do other civil cases. In any event, many matters that will come before the courts under the proposed new Act will be straightforward and routine in nature. Many applications, such as approving the replacement of a retiring trustee or issuing a vesting order, will only rarely involve difficult legal questions.

- 13.7 We accept that some matters do raise complex legal issues and are consequently better brought in the High Court. However, it is not necessary to reserve jurisdiction exclusively to the High Court on all matters just to deal with this group of proceedings. Our view is that, provided the High Court retains concurrent jurisdiction, and there are appropriate powers of transfer, this is sufficient to deal with the needs of complex trust cases.
- 13.8 There are significant differences between the civil processes used in the District Court and High Court. Some submitters expressed concern over the suitability of the current District Court civil process for trust claims. They consider that the standard capsule procedure is poorly suited to the identification of legal issues and their prompt and efficient resolution. These submitters argued that the High Court originating application process is much better suited to trust disputes and that the High Court Part 18 procedure should be adopted as part of the District Court Rules if the District Court is to have jurisdiction.<sup>283</sup>
- 13.9 Submitters also questioned whether there would be any real cost advantage for litigants bringing proceedings in the District Court rather than the High Court. Some suggested that the cost differences are not significant. Our position is that irrespective of the comparative costs involved for litigants, concurrent jurisdiction still increases the range of options litigants will have, and in that sense at least, must improve access to justice. We think that for appropriate cases, the District Court should be available to provide a lower level dispute resolution option. While this matter does not come within our review, there has been significant concern expressed by the profession over aspects of the District Court procedure. Those matters are for the Rules Committee to address.
- 13.10 Our recommendation allows litigants to elect to file their claims in the High Court rather than the District Court if they consider that the High Court should hear the case, even if the amount in dispute is within the District Court's jurisdiction. Below we discuss our recommendations for transfer to the High Court where a party objects to the matter being determined in the District Court.

### *The jurisdiction of the District Court*

- 13.11 Currently section 34(1)(a) of the District Courts Act grants the District Court “the same equitable jurisdiction as the High Court”, so long as “the amount claimed or the value of the property claimed or in issue” is no more than \$200,000. The upper limit of \$200,000 set for the court's equitable jurisdiction is the same as the upper limit set by the Act for all civil claims. Where proceedings do not involve a claim or dispute over money or property the District Court has the same equitable jurisdiction as the High Court.
- 13.12 Relevant here is the Government's recent announcement in response to the Commission's Report *Review of the Judicature Act 1908: Towards a New Courts Act*.<sup>284</sup> The Government intends to introduce new courts legislation implementing the majority of the recommendations in that Report. It is proposed that new courts legislation will increase the upper financial limit of the District Court's civil jurisdiction to \$350,000.<sup>285</sup> In our view this should apply to trusts cases.

283 High Court Rules, pt 18.

284 Cabinet Social Policy Committee *Government response to the Law Commission's report: Review of the Judicature Act 1908: towards a new Courts Act* (Ministry of Justice, April 2013).

285 At [68].

- 13.13 The District Court should also have jurisdiction, concurrent with the High Court, to determine any proceedings (such as those to appoint or remove a trustee) that do not involve any claim for money or any claim or issue over property. This means that irrespective of the value of the assets in the trust, that court could determine any proceeding or application under the new Act that does not involve any claim for money or property.
- 13.14 There should also be an ability to transfer proceedings to the High Court where proceedings are commenced in the District Court. After considering whether any special arrangements for transfer are needed, we have determined that section 43 of the District Courts Act, which covers the transfer of civil proceedings to the High Court, should apply to proceedings under the new Trusts Act. Under section 43 a defendant in a proceeding may give notice objecting to the proceeding being determined in the District Court. A defendant has the right to have the proceeding transferred to the High Court where the sum sought, or the value of property or relief claimed, exceeds \$50,000. The Government's proposed new courts legislation will increase this threshold from \$50,000 to \$90,000.<sup>286</sup>
- 13.15 Where the proceeding does not include any claim for money, relief or property, or the claim falls below the threshold for transfer as of right, section 43 provides that any transfer of the proceeding will be at the discretion of the District Court. The Court may order that the proceeding be transferred if it is satisfied that some important question of law or fact is likely to arise.
- 13.16 Our recommendation is that section 43 (or its replacement) should apply to proceedings under the proposed Trusts Act.

*Jurisdiction of the Māori Land Court will continue unchanged*

- 13.17 For completeness, we also note that nothing we recommend here alters the current jurisdiction of the Māori Land Court. Under section 237 of Te Ture Whenua Maori Act 1993 the Māori Land Court has, in relation to trusts to which that Act applies, the same powers and authorities as the High Court, including those conferred by statute. Jurisdiction under the new Trusts Act will therefore consequently flow through to the Māori Land Court which will retain its current jurisdiction.

## FAMILY COURT JURISDICTION

### RECOMMENDATION

- R41 Where the Family Court has jurisdiction under section 11 of the Family Courts Act 1980 to hear and determine proceedings:
- (1) The Family Court should be able to make any order or give any direction available under the new Trusts Act during those proceedings where the Court considers such order or direction necessary to:
    - (a) protect or preserve any property or interest until the proceedings before the Court can be properly resolved; or
    - (b) to give proper effect to any determination of the proceedings before the Court.

286 At [70].

- (2) Where the parties consent, the Family Court should also be able to make any orders under the new Trusts Act to resolve any closely related dispute or issue between the parties where this is necessary or would assist the resolution of the substantive proceedings between the parties.

**Note**

The Family Court's jurisdiction under the new Trusts Act would not be subject to financial limits.

### Proceedings involving trusts before the Family Court

- 13.18 The Family Courts Act 1980 established the Family Court as a division of the District Court. Section 11 of that Act gives the Family Court jurisdiction for a wide variety of matters affecting couples, families and children.
- 13.19 The Family Court is at times required to consider aspects of trust law when they arise in proceedings under the Family Protection Act 1955 or the Property (Relationships) Act 1976. Some relationship property matters and other family proceedings that come before the Family Court involve components of trust law. In proceedings under the Property (Relationships) Act, the Family Court may make some ancillary orders under section 33(3) of that Act in respect of trusts to give effect to decisions under the Act. Section 33(3) has been interpreted as enabling the Family Court to “adopt one or more of a number of means of dividing the property so as to give effect to its conclusions as to entitlement”.<sup>287</sup> Section 33(3)(m) empowers the Family Court to vary the terms of an inter vivos trust, but not a testamentary trust.
- 13.20 Property settled on a trust by one of the partners to the relationship will only come within the Court's jurisdiction if the disposition to the trust was a defeating disposition caught by section 44 of the Property (Relationships) Act and can be set aside, or where one or both of the relationship partners has a property interest (that is a vested or contingent interest) in the trust.<sup>288</sup> In such cases, the Court can make orders dealing with the trust assets, including orders varying the terms of the trust under 33(3)(m).<sup>289</sup> For example, the Court may vary the terms of the trust to confer on a spouse or partner a vested interest or remove a contingency, or it could vary the final distribution date to the date of judgment.<sup>290</sup>
- 13.21 These ancillary powers go some way to allowing the Family Court to deal with trust law components of cases properly before the Family Court, but do not allow the court to make many of the orders or give the types of directions necessary to effectively resolve all the issues before it. In some situations this means that the parties need to make subsequent applications to the High Court to address the trust matters that are intertwined with relationship property.
- 13.22 Given our recommendation that the District Court should have jurisdiction under new trusts legislation, we think it is difficult to argue that the Family Court, which is a division of the District Court, should not also have those powers. We see no reason why the Family Court should not have the same powers under new trusts legislation to better deal with matters

<sup>287</sup> *Coxhead v Coxhead* [1993] 2 NZLR 397 (CA) at 408.

<sup>288</sup> Substantive orders cannot be made in respect of trust assets, unless s 44 applies, if a spouse's or partner's interest in the trust is merely a discretionary interest because the spouse or partner has no beneficial ownership in the assets in trust. He or she merely has a hope or expectation until the trustees exercise their discretion in the beneficiary's favour: see *Nation v Nation* [2005] 3 NZLR 46 (CA) and the discussion in Nicola Peart (ed) *Brookers Family Law — Family Property* (online looseleaf ed, Brookers) at [PR33.12].

<sup>289</sup> At [PR33.12].

<sup>290</sup> At [PR33.12].

properly before it and reduce the need for parties to bring subsequent proceedings in the High Court. Again our approach is that the court should be provided with the tools necessary to exercise its jurisdiction.

- 13.23 Although submitters responding to the *Preferred Approach Paper* did not generally favour the Family Court having jurisdiction, over the course of the project submissions have been quite evenly divided on this issue. We have taken the differing views of submitters into account in formulating our recommendations.

#### *Ancillary orders*

- 13.24 We are recommending that the Family Court should be able to exercise the powers and make orders under new trusts legislation as an ancillary jurisdiction, to provide a remedy where a matter is already within its jurisdiction. The Family Court already has the ancillary jurisdiction of the District Court under section 41 of the District Courts Act to give equitable relief where a matter is within its jurisdiction, but not jurisdiction to hear a cause of action founded in equity. Our recommendation does not give the Family Court substantive equitable or civil jurisdiction. Submitters were concerned about this issue so we wish to make it clear that, subject to the recommendation concerning closely related matters in R41(2), the Family Court could only exercise powers and make orders where the proceedings in question are already within its jurisdiction.
- 13.25 We recommend that the Family Court should be able to make orders under the new Act where these are necessary during the proceedings to protect or preserve any property or interest that is the subject of those proceedings until the issues are fully resolved by the court. Our recommendation would allow the Family Court to, for example, make an order removing one trustee and appointing (even on a temporary basis) a new independent trustee where this is necessary to manage serious deadlock, hostility between trustees, ascertain the nature of the trust assets, or to preserve those assets until the property claims of the parties can be properly resolved.

#### *Closely related matters*

- 13.26 In addition we consider that there would be merit in the Family Court also being able to make orders, with the consent of the parties, to resolve a closely related dispute or issue between the parties where this is necessary, or would better promote the resolution of the substantive proceedings between the parties. The intention here is to allow the parties to proceedings properly before the Family Court to consent to the court resolving closely related trust matters that may otherwise fall beyond its jurisdiction. Parties may wish to do this where those matters are so closely linked to the substantive proceedings that leaving them unsettled impedes the effective and fair resolution of the substantive proceedings. The recommendation would also allow the parties to avoid the need for a subsequent hearing to deal with closely related trusts matters that otherwise would fall beyond the Family Court's jurisdiction.
- 13.27 Where the parties do not consent, or a Family Court judge determines that there is not sufficient nexus between the related trusts matter and the substantive family proceedings, then the parties would need to have those matters resolved in either the District or High Court.

#### *Transfer to High Court to be more readily available*

- 13.28 At the time of writing the Family Court Proceedings Reform Bill was before the House. That Bill includes a provision amending the Property (Relationships) Act to make it easier for parties to

have relationship property proceedings transferred from the Family Court to the High Court.<sup>291</sup> The new provision provides that a Family Court Judge may order the transfer of proceedings to the High Court if satisfied that the High Court is the more appropriate venue for dealing with the proceedings. When deciding whether the proceedings should be transferred the Judge should consider, among other issues, the complexity of the issues in question in the proceedings and also whether there are other proceedings before the High Court between the parties involving related issues.

- 13.29 The new provision sets a lower threshold for transferring proceedings than the current provision. At present the Judge must be satisfied that the High Court is the more appropriate venue because of the complexity of the proceedings.<sup>292</sup> The amendment would likely mean that relationship property cases with trust issues can more readily be consolidated with other trust proceedings in the High Court.
- 13.30 However, making transfer more readily available does not dispense with the need for the Family Court to be able to make orders under the proposed new Trusts Act. In some cases, and for a range of good reasons, the Family Court remains the most appropriate forum. We consider it is still important for the Family Court to have jurisdiction to make any orders that are necessary to effectively deal with all issues properly before it.

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291 Family Court Proceedings Reform Bill 2012 (90-2), cl 95.

292 Property (Relationships) Act 1976, s 22(3)–(4).

# Chapter 14

## Resolving disputes outside of the courts

### INTRODUCTION

14.1 This chapter sets out the Law Commission’s recommendations regarding the use of alternative dispute resolution (ADR). This topic was discussed in the *Fifth Issues Paper* and *Preferred Approach Paper*.<sup>293</sup>

### THE USE OF ALTERNATIVE DISPUTE RESOLUTION

#### RECOMMENDATION

R42 The new Trusts Act should:

- (1) Clarify that trustees have a power to use alternative dispute resolution (ADR) to settle an internal dispute (between trustees and beneficiaries) or an external dispute (between trustees and third parties), other than a dispute as to the validity of all or part of a trust. This should be a default power that applies unless explicitly excluded or modified by the terms of the trust.
- (2) Make any provision in the terms of a trust that requires the settlement of a dispute by ADR enforceable, other than a dispute as to the validity of all or part of a trust.
- (3) Give trustees a specific power to give future assurances of actions that have been agreed to as a part of an ADR settlement.
- (4) Provide that trustees will not be liable to other parties for agreeing to the settlement if they acted honestly and in good faith while doing so.
- (5) Provide that by virtue of this provision, an ADR settlement cannot override creditor priority rules as they affect creditors that are not party to the settlement.
- (6) Provide that a beneficiary or trustee can make a request to the court that ADR be used to resolve a dispute rather than court proceedings and that the court can require ADR to be used. It should be open to the court to allow the costs of the mediation to be paid from the trust.
- (7) Provide that the court can appoint representatives of unascertained and incapacitated beneficiaries, who may be other beneficiaries, who can agree to a binding ADR settlement on behalf of the unascertained and incapacitated beneficiaries, subject to the court’s approval of the settlement.

<sup>293</sup> Law Commission *Court Jurisdiction, Trading Trusts and Other Issues: Review of the Law of Trusts – Fifth Issues Paper* (NZLC IP28, 2011) at ch 5; Law Commission *Review of the Law of Trusts – Preferred Approach* (NZLC IP31, 2010) at ch 13.

### Facilitating the use of alternative dispute resolution

- 14.2 The benefits of using ADR to resolve disputes are well accepted. When compared with a court hearing, these include lower costs, quicker resolution, achieving finality, maintaining confidentiality and privacy, and being less adversarial. ADR techniques, such as mediation, conciliation and arbitration, are used in some trust disputes. However, ADR is not available in all trusts and where it is available, the nature of trusts can prevent the use of ADR because there can be unascertained and incapacitated beneficiaries who are not able to give consent to the use of ADR or to any agreement reached under ADR.
- 14.3 While some trust deeds, particularly modern ones, explicitly allow the use of ADR, others do not. There is nothing in the Trustee Act 1956 that makes ADR generally available,<sup>294</sup> although it may be possible to vary the trust deed to provide this power or for parties to agree to the use of ADR. Where all parties, including beneficiaries, are capable of consenting, parties can agree to an ADR settlement. Where there are unascertained or incapacitated beneficiaries, the court can appoint a person to represent the interests of these beneficiaries. In this case, any settlement must be consented to by the court.
- 14.4 In our recommendations, we seek to clarify that trustees have the power to use ADR to settle trust disputes by including a default power to settle a dispute by ADR for both existing and new trusts.
- 14.5 If an ADR settlement requires trustees to commit to a future course of action, they are effectively fettering their decision-making, which may breach the default duties to consider the exercise of their discretions and not to fetter the future exercise of their discretions. We propose the legislation resolve this issue by providing trustees with a specific power to give future assurances of actions that have been agreed to as a part of an ADR settlement. Trustees may also be hampered in a decision to settle a dispute using ADR by the risk of liability if other parties to the settlement are unhappy with the settlement later on. The statute should provide that trustees will not be liable for agreeing to an ADR settlement if they acted honestly and in good faith.
- 14.6 We see merit in the option of introducing a provision which allows beneficiaries and trustees to apply to the court for an order that ADR be used to resolve a dispute rather than court proceedings. This would give beneficiaries increased power to select how disputes are settled, something that seems appropriate given that they are likely to be most affected by the outcome of a dispute. The court will exercise judgement as to whether ADR is appropriate in the circumstances of the dispute.
- 14.7 The legislation should provide that the court can appoint representatives of unascertained and incapacitated beneficiaries who can agree to a settlement on behalf of these beneficiaries, although any settlement involving unascertained and incapacitated beneficiaries would continue to require the approval of the court. This recommendation is for the purpose of clarifying that this option is available to the court, as the court currently has this power. We did consider whether “virtual representatives” of unascertained and incapacitated beneficiaries should be able to bind those beneficiaries to a settlement, but we do not think that this adequately protects the interests of beneficiaries who cannot represent themselves.
- 14.8 No submitter objected to the ADR proposals. Submitters to the issues papers have made it clear that they are generally satisfied with the state of the law in this area of trusts and do not want legislative change to be substantial. The comment was made that ADR should be

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294 ADR may sometimes be an option under section 20(g) of the Trustee Act 1956.



voluntary for the parties. Inland Revenue requested that the recommendation make it clear that a purportedly binding settlement cannot override existing creditor priority rules so as to defeat creditors that are not party to the settlement. We understand that the Commissioner of Inland Revenue wishes to be protected in situations where a settlement between a trustee and third party creditor is to the detriment of other creditors, and considers that the legislation should protect against this. We do not consider it necessary for this to be stated in legislation.

- 14.9 David Williams QC submitted that we should give consideration to the work of the United Kingdom's Trust Law Committee on the arbitration of trust disputes.<sup>295</sup> This work has been informative and we have aligned our proposals with several of the Committee's suggestions, including a provision giving legal validity to ADR clauses in a trust deed and a provision for a default ADR clause. The Committee's paper advocates for a legislative approach that would bind creditors and unascertained and incapacitated beneficiaries through the use of litigation friends.<sup>296</sup> Other submitters have made it clear that they think that such an approach should not be taken in New Zealand as the court should have oversight in order to protect potentially vulnerable parties and we agree with this view. We are not aware of a need to give arbitration greater preference than other forms of dispute resolution in relation to trusts in New Zealand, as a submitter advocated, but consider that the current law and our recommendations leave open and facilitate the use of a variety of forms of ADR in trust disputes.
- 14.10 We have chosen not to pursue the proposal that the Public Trust should be empowered to appoint an independent mediator or arbitrator where parties to a dispute desire it.<sup>297</sup> We no longer consider it necessary to have a body in this role. We also consider that it is not the type of role usually filled by the Public Trust.

### Application to existing trusts

- 14.11 The new provisions recommended in this chapter should apply to all trusts from the date of enactment of the new Act. These provisions are helpful for the management of trusts, particularly for those that do not have terms of trust regarding the use of ADR, and existing trusts should be able to benefit from them.

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295 Trust Law Committee "Arbitration of Trust Disputes" (2012) 18 T&T 296.

296 At 306.

297 *Preferred Approach Paper*, above n 293, at P53(f).

# Chapter 15

## The Public Trust

### INTRODUCTION

- 15.1 In the *Preferred Approach Paper*, we proposed that the Public Trust be given a number of new roles.<sup>298</sup> This was the first time we had suggested that the Public Trust's role under new trusts legislation could be expanded from what it is now, and we received significant feedback on the proposals. As a result we have altered the approach to limit the new roles for the Public Trust to those that are within its current skillset and expertise.

### NEW ROLES FOR THE PUBLIC TRUST

#### RECOMMENDATION

R43 The new Trusts Act should provide that:

- (1) Where carrying out any of the roles it has under the new Trusts Act would involve any element of dispute or contention or significant complexity, the Public Trust should not act.
- (2) The Public Trust should be accountable to the Government for the exercise of its roles under the new Trusts Act.
- (3) The Public Trust could charge a reasonable fee for carrying out the roles under the new Trusts Act.

#### Note

The roles recommended for the Public Trust in the Report are:

- the power to make decisions on behalf of a trustee where the trustee is temporarily unavailable and cannot be contacted for any reason and no delegation is in place (R12);
- overseeing the removal and/or replacement of a sole trustee on the ground of incapacity or similar where there is no one else with authority to do this apart from the court (R21);
- overseeing the appointment of a replacement of a sole trustee who dies while in office where there is no one with the power to appoint a new trustee under the trust deed (R22);
- overseeing the retirement and replacement of a sole trustee when there is no one else with the power to appoint a new trustee under the trust deed (R23);
- providing a vesting certificate to confirm that assets are vested in a named new trustee where a former trustee has not and cannot now transfer the trust assets (R26).

<sup>298</sup> Law Commission *Review of the Law of Trusts – Preferred Approach* (NZLC IP31, 2012) at ch 13.

## Status of the Public Trust

- 15.2 Under the Public Trust Act 2001 and the Crown Entities Act 2004, the Public Trust is established as a statutory corporation that is an autonomous Crown entity. It has functions relating to the business of providing estate management and administration services under the Public Trust Act, the Trustee Act 1956, and a number of other Acts. Under various statutes the Public Trust is given responsibility for managing public money, administering estates, filing certificates, holding securities, advancing and borrowing money on others' behalf, executing instruments to discharge a mortgage and overseeing property managers' property statements.<sup>299</sup>
- 15.3 Under the Trustee Act, the Public Trust is required to accept an appointment as a replacement trustee, effectively making it the trustee of last resort.<sup>300</sup> Following amendment in May 2013, the Act requires that, where the retiring trustee is a securities trustee, the Public Trust can only be appointed if the retiring trustee has failed to obtain another replacement and indemnifies the Public Trust for its reasonable fees and expenses in taking the appointment.<sup>301</sup> This limit to the Public Trust's obligation to perform the role of the trustee of last resort has been enacted because of particular concern regarding the failure of finance companies that use a trust structure and the significant cost to the Public Trust if it is required to be the replacement trustee in these trusts.<sup>302</sup>

## Proposals in Preferred Approach Paper

- 15.4 In the *Preferred Approach Paper*, we proposed that the Public Trust be given a number of roles under new trusts legislation. We saw the Public Trust as presenting an attractive alternative to the courts for carrying out relatively straightforward administrative processes and the provision of advice. It would act in place of a court in some situations resulting in reduced cost and delay.
- 15.5 The roles that were proposed for the Public Trust in the *Preferred Approach Paper* were:
- P9 – advising trustees on the release of trust information to beneficiaries;
  - P16 – acting as delegate where the trustee is unavailable and cannot be contacted;
  - P24 – overseeing the retirement and replacement of a sole trustee when there is no one else with the power to appoint a new trustee under the trust deed;
  - P25 – removal and/or replacement of a trustee on the ground of incapacity or similar where there is no one else with authority to do this apart from the court;
  - P28 – providing a vesting certificate to confirm assets are vested in a new trustee;
  - P46 – the power to bar small claims;
  - P48–P49 – advising trustees on advertising when trying to locate missing beneficiaries and any outstanding creditors; and
  - P53 – appointing a mediator or arbitrator to settle a trust dispute.

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299 For instance, Insolvency Act 2006, ss 273, 283–289, 385 and 387; Protection of Personal and Property Rights Act 1988, ss 37, 39, 46, 91 and sch 2; Property Law Act 2007, ss 109 and 112; Public Works Act 1981, ss 81 and 96–98; Life Insurance Act 1908, s 69; Administration Act 1969, s 19.

300 Trustee Act 1956, s 46(4).

301 Trustee (Public Trust) Amendment Act 2013, s 4. We understand that this amendment will no longer be required and will be repealed once the Financial Markets Conduct Bill 2011 (342-3) is in force as that legislation will provide an alternative process for replacing a securities trustee.

302 Ministry of Justice *Regulatory Impact Statement: Trustee Amendment Act* (8 May 2013).

### Submitter concerns

- 15.6 These proposals elicited a significant number of comments from submitters, with most opposing proposals to give the extra roles to the Public Trust. The reasons given by submitters were:
- the Public Trust would have an unfair business advantage and a monopoly when it is a competitor to other statutory and non-statutory trustee companies;
  - the Public Trust may be unsuitable for these roles as it is not suited to exercising independent jurisdiction and there are concerns regarding its efficiency and expertise;
  - the Public Trust may not be adequately resourced for the role and may need additional government funding;
  - concerns that the Public Trust had no more technical expertise, skills or resources than other trustee companies or practitioners;
  - a potential lack of accountability;
  - possible conflicts of interest when the Public Trust is involved as a trustee;
  - it would undermine the legal profession's role in providing advice to trustees; and
  - concerns about the fee structure.
- 15.7 Submitters who tentatively agreed with all or some with the proposals expressed a desire to see the details of the arrangement, such as timeframes, costs, and processes for resolving conflicts of interest.

### Reconsideration of the roles

- 15.8 Following submitter feedback, we have reconsidered the appropriateness of the Public Trust carrying out the roles we had proposed earlier. We think that the majority of the concerns from submitters arose in relation to the advice-giving roles where the Public Trust could have been seen as taking the place of a legal adviser or adjudicator. We now recommend confining the Public Trust's new roles to situations where it either stands in the shoes of a trustee or where it is involved in the formal certification and validation of a process. These are akin to its current statutory roles and are less controversial as they are less adjudicative in nature.<sup>303</sup> The new Act should make it clear that the Public Trust would only be able to exercise a decision-making power if there was no dispute, uncertainty or problems, in which case the matter would need to be decided by the court. It could preclude the Public Trust from being able to carry out the proposed roles where it is a trustee. We think the Public Trust should not be prevented from appointing itself as a replacement trustee.
- 15.9 We agree with submitters that there should be some constraints on the Public Trust's fee structure and processes, and accountability to the Government. As an autonomous Crown entity, the Public Trust is subject to the Crown Entities Act. The Public Trust is required to report quarterly and annually to the Minister responsible for the Public Trust on its commercial and non-commercial financial and operational performance. We see no difficulty for the Government in requiring performance information for the roles we recommend. We do not think it necessary for the Public Trust's fees to be set by regulation and this can cause problems as it can be inflexible over time. The Public Trust's fees should be required to be reasonable. We note that the Treasury has issued guidelines for user charges for services where Crown entities are monopoly suppliers, as would be the case here.<sup>304</sup>

303 For instance, Property Law Act 2007, s 112.

304 The Treasury *Guidelines for Setting Charges in the Public Section* (December 2002).

## Consideration of alternative options

- 15.10 Because it was raised by submitters, we have reconsidered whether another option for a lower-level decision-maker is viable. The options of having the other statutory trustee companies or any authorised trustee company fulfil the proposed roles are unsatisfactory at this stage. The Commission is yet to review the Trustee Companies Act 1967, which it will do in the review of corporate trustees, and it would be premature to place other trustee companies on a footing with the Public Trust before reforms are properly considered. The Public Trust has the advantage over other trustee companies of being accountable to the Government because of its status as a Crown entity. There would be the potential for the Government to have a contractual relationship with the other statutory trustee companies to provide the proposed services. However, those trustee companies are generally not given roles such as these, especially not in relation to private family trusts.
- 15.11 A new independent quasi-judicial panel or trusts ombudsman would have some advantages over the Public Trust. They could provide a high degree of independence and expertise, and would be well suited to the role. However, for the same reasons that we have not pursued these options after giving them consideration earlier in the review, we cannot recommend them at this stage. We consider that the costs are currently prohibitive. If in future there is appetite for the establishment of a new body, we suggest that these options should be considered further. The option of a new independent dispute resolution body or decision-maker was discussed in the *Fifth Issues Paper* and the *Preferred Approach Paper*.<sup>305</sup>

## Reasons for recommendation

- 15.12 We are convinced that it is necessary to have a neutral fiduciary power holder available under the new Trusts Act. Currently the Public Trust fills this role, and we are proposing an expanded role for it. It would be possible to create an alternative body, such as an independent panel, to carry out the proposed roles. However, we think it is unlikely that the Government would choose to fund a new body, and a better option is to utilise the body that currently holds this position.
- 15.13 The Public Trust is in the unique position of being a trustee company that is a Crown entity. It is, therefore, subject to public accountability and control in a way that other trustee companies are not. The Public Trust has a long history of carrying out trusteeships and supervisory roles in relation to trusts. It has the structures and expertise in place to handle the new roles. The new roles that we recommend the Public Trust fill are a significant aspect of the package of law reform put forward in this Report, as they provide an alternative to a costly court application in situations where there are mechanical difficulties that need resolving. Our view is that the Public Trust is the best option for carrying out the new roles.

## SECTION 83B – AUDIT OF ACCOUNTS

### RECOMMENDATION

R44 The new Trusts Act should re-enact section 83B of the Trustee Act 1956, relating to an application for the accounts of trust property to be audited, in modernised form and with modification so that the process continues to rely on an application to the Public Trust, but no longer also requires an application to a judge in chambers as is currently the case.

<sup>305</sup> *Preferred Approach Paper*, above n 298, at ch 13; *Law Commission Court Jurisdiction, Trading Trusts and Other Issues: Review of the Law of Trusts – Fifth Issues Paper* (NZLC IP28, 2011) at ch 4.

### **Current law and practice**

- 15.14 Section 83B provides a process by which a beneficiary or trustee can make an application for the accounts of trust property to be investigated and audited by a solicitor or chartered accountant appointed with the agreement of the applicant, the trustees and the Public Trust, or, if there is no agreement, by the Public Trust alone. The provision requires that an application be made to a judge in chambers in addition to requiring the agreement of the Public Trust.
- 15.15 It is a long and complex provision. We understand that applications under the section are seldom made, but that beneficiaries and trustees do on occasion apply to the Public Trust to begin this process. In most of these cases, the Public Trust's involvement in initiating negotiations as to how the audit might be carried out and who will pay for it leads the trustees and beneficiaries to settle the matter among themselves without an application to a judge ever being made or an auditor being appointed. The provision is considered to be a useful tool in encouraging trustees and beneficiaries to work out their disagreements. However, we have heard comment that the provision is overly bureaucratic as it effectively requires the double handling of an application to appoint an auditor because it involves both the Public Trust and the court.

### **Recommended reform**

- 15.16 We recommend that the provision is retained, but with a modified process so that the need for an application to a judge in chambers is removed. Instead, we think it would be appropriate and effective for the applicant beneficiaries and trustees to apply to the Public Trust to appoint an auditor with the agreement of the applicant and the trustees, if possible. This is unlikely to alter what actually happens in practice now. The role for the Public Trust is administrative rather than adjudicative and is consistent with its current range of roles.

### **Application to existing trusts**

- 15.17 This recommendation would apply to all trusts, including existing trusts, from the date of the enactment of the new Act as it provides assistance to trustees and beneficiaries by simplifying a statutory process.

**Part 5**  
**OTHER**  
**TRUST ISSUES**



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# Chapter 16

## Trustee's indemnity, corporate trustees and insolvency

### INTRODUCTION

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- 16.1 This chapter addresses various issues relating to corporate trustees, creditors, trustees' indemnity, and insolvency, which were previously discussed in the *Fifth Issues Paper* and the *Preferred Approach Paper*.<sup>306</sup> It includes discussion of previous proposals on:
- liability of directors of corporate trustees to creditors and beneficiaries;
  - disclosure of trustee status of companies acting as trustees and interaction with other registers; and
  - areas where trust law interacts with insolvency law.
- 16.2 This chapter also discusses recommendations in the following areas:
- the standing of the Official Assignee to challenge the validity of a trust;
  - the ability of the High Court to appoint a receiver for trusts;
  - principles regarding trustees' liability and indemnity; and
  - creditors dealing with trustees.
- 16.3 In some of these areas there have been changes from what was proposed in the *Preferred Approach Paper*. We have decided that some of those proposals are more appropriately dealt with later in the Law Commission's corporate trustee review. This chapter discusses submitters' comments and reasons for changes in position from the *Preferred Approach Paper*.

### PROPOSALS FROM PREFERRED APPROACH PAPER

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#### Liability of directors of corporate trustees

- 16.4 The *Fifth Issues Paper* and the *Preferred Approach Paper* discussed the problem of unsecured creditors that interact with a trust potentially being left without recourse to recover a debt. This could occur when the trustee has few or no assets of its own, and the creditor's subrogation claim is impaired because the trustee's indemnity is likewise impaired (for reasons that may be unrelated to the dealings with that creditor). This would leave the beneficiaries with what might be perceived as a windfall at the expense of creditors. This problem was initially approached in the context of trading trusts, and then corporate trustees, because it was perceived that creditors are particularly vulnerable where their only recourse is to an assetless corporate trustee.
- 16.5 The *Preferred Approach Paper* included a proposal to impose personal liability on directors of corporate trustees for liabilities incurred when acting on behalf of the trust. This would

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<sup>306</sup> Law Commission *Court Jurisdiction, Trading Trusts and Other Issues: Review of the Law of Trusts – Fifth Issues Paper* (NZLC IP28, 2011) at pt 3; Law Commission *Review of the Law of Trusts – Preferred Approach* (NZLC IP31, 2010) at ch 8.



have applied in certain circumstances where the liability could not be discharged through the trustee's indemnity. The proposal was based on the Australian provision in section 197 of the Corporations Act 2001 (Cth).<sup>307</sup>

- 16.6 Submitters were strongly opposed to this proposal and raised a number of issues with it. They argued that companies legislation already imposed sufficient obligations on directors and that there were no problems with the status quo. Submitters also said it was inappropriate to modify the fundamental principle of limited liability of companies and separate legal personality. They argued that the proposal would be impractical and ineffective and considered that significant numbers of people could become unwilling to act as directors of corporate trustees, due to the expansion of liability. In addition, submitters emphasised the prevalence and usefulness of corporate trustees, and expressed the view that they are generally established for legitimate purposes. Submitters emphasised to us that natural persons who act as trustees may be just as unable to fulfil their obligations due to an impairment of the trustee's indemnity as corporate trustees. They argued that corporate trustees should not be singled out.
- 16.7 We acknowledge the concerns raised by submitters about the proposal. We believe that more consideration of the proposal's wider implications needs to occur before we form any final views on its efficacy. We intend to consider the use of corporations as trustees more broadly in the corporate trustee review, which may also consider related issues such as directors' duties.
- 16.8 However, the Commission remains of the view that reform is needed to strengthen the position of creditors and prevent unfairness to those dealing with trusts who have given value to the trust. Therefore, while we are deferring consideration of the position of directors, we are recommending some changes that do fit more appropriately within this Report.

### Liability of directors to beneficiaries

- 16.9 The *Preferred Approach Paper* also included a proposal that directors (or equivalent) of a corporate acting as a trustee have the same obligations to the beneficiaries of the trust as if they had been the trustee.<sup>308</sup> That proposal was again strongly criticised by submitters for similar reasons to the proposal discussed above. The point was also made that it cut across the principle that directors owe a duty to the company but not to the beneficiaries of the trust, and that the proposed change would interfere with the settlor's ability to set up the trust as the settlor wished. Some argued that it would negate the use of a corporate trustee.
- 16.10 For the reasons discussed already we are deferring further consideration of the issue of directors' liability until the corporate trustee review. We will consider the position of beneficiaries of trusts with corporations as trustees more generally in that review.

### Disclosure of trustee status of corporate trustees

- 16.11 The *Preferred Approach Paper* included a proposal that section 25 of the Companies Act 1993 be amended to require a company acting as a trustee to disclose its trustee status in communications and contracts. This recommendation was directed at the problem that third parties, particularly creditors, may not be aware that a company they are dealing with is a trustee, and therefore may be misled into thinking that assets of the company are owned outright, when in fact they are being held on trust. As the *Fifth Issues Paper* discussed, disclosure would only be a partial solution. It would act as a flag to creditors about the capacity in which the company is acting, but would not provide any additional information about the company's

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<sup>307</sup> *Preferred Approach Paper*, above n 306, at P34.

<sup>308</sup> At P36.

asset base, and it would still fall to the creditor to make enquiries and take steps to protect its position if required.<sup>309</sup>

- 16.12 This proposal was supported by the majority of submitters who commented on it. Submitters generally agreed that this proposal would put creditors (and others) on notice as to the status of the company that they were interacting with. It would enable voluntary creditors to choose whether to deal with the company or to require additional security or guarantees.
- 16.13 A small number of submitters opposed the proposal on the basis that the mischief that disclosure purports to remedy was unclear, that there is no difference for creditors between dealing with a company in its own right or as a trustee, and that it would impact negatively on trusts' confidentiality and privacy. Several submitters raised practical points about the form of words to describe trustee status and questions over the appropriate consequences where there was a breach of the disclosure requirement.
- 16.14 This feedback from submitters was useful and has again raised various issues that require further consideration. This reform would involve a change to the Companies Act, rather than forming part of a new Trusts Act. Accordingly it will be more appropriate to address this recommendation in the corporate trustee review.

#### *Relationship with companies and land transfer registers*

- 16.15 Some submitters raised issues with the disclosure proposal in terms of its relationship with other legislative regimes, including the property law and companies regimes. The Auckland District Law Society considered that the proposal should be extended to apply to ownership of land, so that there was an automatic requirement to state on the land register when land was held by trustees on trust. Other submitters suggested that trustee status be noted on the companies register or in the company name itself. However, as another submitter acknowledged, this is likely to be impractical because many companies also act or own assets in their own right, or act as a trustee of various different trusts.
- 16.16 The Commission considered the notation of trusts on the land register and noting trustees as registered owners in its 2010 review of the Land Transfer Act 1952.<sup>310</sup> The Commission took the view that optional noting of trusts on the register would not necessarily lead to more transparency. Noting trusts could affect the ease and speed of land transfers, and could increase compliance costs and delay. It would bring in matters of trustees' duties and other trust law issues that are not the appropriate concern of a land registration statute. The Commission was not persuaded that an optional right or a mandatory obligation for trustees to register in their capacity as trustees was warranted. Having recently considered this matter in depth, the Commission has decided not to revisit it in the context of this review.

#### **Insolvent corporate trustees**

- 16.17 There are a number of areas where the law of trusts interacts with insolvency law. The *Preferred Approach Paper* identified issues that are currently uncertain and could be resolved by clarification in statute:
- (a) whether an insolvent corporate trustee should be liquidated;
  - (b) whether liquidators are entitled to claim fees and expenses from trust assets; and
  - (c) the distribution of assets and priority of creditors on liquidation.

309 At [8.29]–[8.46]; *Fifth Issues Paper*, above n 306, at [7.14].

310 Law Commission *A New Land Transfer Act* (NZLC R116, 2010) at [3.33]–[3.39].

- 16.18 Submitters supported the need for a review and statutory clarification of the matters referred to in this recommendation. Review of these areas will involve significant interactions with the company and insolvency regimes and the policy and statutory schemes in these areas. Accordingly we consider that it is desirable they be examined as part of the Commission’s later corporate trustee review.
- 16.19 Submitters also requested that the following matters be reviewed and clarified:
- insolvent trusts, and situations of insolvency (with that term being defined in terms of trusts carefully); and
  - liability of directors of a trustee company that is insolvent to beneficiaries for any losses incurred due to the insolvency.

## STANDING OF THE OFFICIAL ASSIGNEE TO CHALLENGE A TRUST

### RECOMMENDATION

R45 The Insolvency Act 2006 should be amended to provide that the Official Assignee has standing to apply to the court to challenge the validity of a trust regardless of whether the bankrupt could have done so prior to the bankruptcy.

### Discussion

- 16.20 Prior to the Court of Appeal’s decision in *Official Assignee v Wilson*,<sup>311</sup> the commonly understood position was that the Official Assignee was able to allege sham structures,<sup>312</sup> whether or not the bankrupt could have done so. However, in *Wilson* the Court held that the Official Assignee could not challenge a trust structure if the bankrupt himself could not have challenged it. The Official Assignee was standing in for the bankrupt, who was the settlor of the trust, not a trustee or beneficiary. Since the bankrupt himself could not have challenged the trust because he was the settlor, the Official Assignee could not challenge the trust either.<sup>313</sup>
- 16.21 The Court’s decision has been criticised by New Zealand and international commentators.<sup>314</sup> It has been argued that the position of the Official Assignee is not to be equated with the position of the bankrupt for all purposes. It ought to be open to the Official Assignee to claim that third parties hold property on trust for the bankrupt estate, and the result of such a claim ought not to depend on whether the bankrupt could have pursued such a claim prior to the bankruptcy. The benefit of the application would pass to the creditors, rather than the bankrupt.
- 16.22 Submitters to previous issues papers, including the New Zealand Law Society and the (then) Ministry of Economic Development, considered that legislative change was required to address the Court of Appeal’s decision.<sup>315</sup> Nearly all submitters to the *Preferred Approach Paper* also supported this recommendation. The New Zealand Law Society noted the relevance of section 412 of the Insolvency Act 2006, which allows the court to look at the “real nature of the

311 *Official Assignee v Wilson* [2007] NZCA 122, [2008] 3 NZLR 45 at [18]–[25].

312 That is, that the trust was merely a façade and the settlor did not truly intend to create a trust.

313 This issue was discussed in the *Preferred Approach Paper*, above n 306, at ch 16 and Law Commission *Some Issues with the Law of Trusts: Review of the Law of Trusts – Second Issues Paper* (NZLC IP20, 2010) at ch 4.

314 See J Guest “Is the trust fortress strong enough? ... Or ‘one door shuts and another door opens?’” (paper presented to the New Zealand Law Society Trusts Conference, June 2009) at 98; Paul Heath and Michael Whale *Heath & Whale on Insolvency* (online looseleaf, LexisNexis) at [4.65]; David Hayton “Current Trust Law Issues” (paper presented to 24th Annual Conference on Transcontinental Trusts, Geneva, June 2009).

315 The New Zealand Law Society emphasised this point in its submissions on both the *Introductory Issues Paper* and the *Second Issues Paper*.

transaction". It considered that the Official Assignee should not be constrained from doing something that a creditor could do, this being consistent with broader principles of insolvency law. The Official Assignee is likely to be the plaintiff in many cases where a trust structure is being used as a shield against the payment of debts.

- 16.23 The recommendation would clarify and provide more certainty about the position of the Official Assignee. A clear benefit of altering the position through a legislative provision would be the protection of creditors, since the Official Assignee is their main representative in proceedings and is likely to be the plaintiff in many cases alleging a sham trust or challenging the trust on another basis. The *Wilson* decision has made the current position highly inconvenient.

#### *Scope and form of provision*

- 16.24 Our recommendation is to amend the position to provide that the Official Assignee has standing to challenge a trust, regardless of whether the bankrupt could have done so prior to the bankruptcy. It should apply whether the bankrupt is a settlor, trustee, or both. The intention of the provision is that the Official Assignee ought to be able to challenge the validity of a trust, for example on the basis that one of the three certainties are not met (such as certainty of intention to create a trust) or alleging that it is a sham.<sup>316</sup> It would be up to the court to decide the claim, and the legal consequences if the trust is not valid. For instance, the court may find that the legal owner of the property is also the beneficial owner, or that he or she holds the property on a resulting trust for the settlor.
- 16.25 However, the recommendation is only intended to provide standing for the Official Assignee for claims involving challenging the validity of a trust. It is not intended to broadly equate the position of the Official Assignee with that of creditors for all purposes. There may also be other questions as to the role of the Official Assignee in the administration of a bankrupt trustee's estate. However, these are outside the scope of this Report.
- 16.26 The *Preferred Approach Paper* noted that the provision could potentially involve a leave application for the Official Assignee to obtain standing.<sup>317</sup> This point was not commented on by submitters. It is considered that it is unnecessary to require the Official Assignee to apply for leave. Such a requirement would add time and expense to the process and the Official Assignee as an officer of the court has a general obligation to act in good faith, which should prevent inappropriate claims.<sup>318</sup>
- 16.27 One submitter commented on the need to provide safeguards for the protection of the rights of beneficiaries. In our view additional safeguards for beneficiaries are not required as part of this recommendation. It would still be up to the court to decide whether a claim would succeed and the effect of a successful claim by the Official Assignee. The court is able to consider the position of any beneficiaries in this process and decide whose interests are to prevail. In addition, this provision will not affect section 104 of the Insolvency Act, which provides that property held by the bankrupt in trust for another person does not vest in the Official Assignee.
- 16.28 We have considered whether the provision should be effected as part of trusts legislation, or as a separate amendment to the Insolvency Act. We consider it is preferable for the amendment to be located in the Insolvency Act because that is where the other powers and duties of the Official Assignee are found. An appropriate location might be Schedule 1 of that Act, which sets out the

316 There is some indication that courts may consider the argument that a trust is illusory as a basis for challenging a trust: see *Financial Markets Authority v Hotchin* [2012] NZHC 323; *Clayton v Clayton* [2013] NZHC 309.

317 *Preferred Approach Paper*, above n 306, at [16.45].

318 *Galdonost Dynamics (NZ) Ltd (in liq)* [1994] 2 NZLR 605 (HC); *Re Condon, ex parte James* (1874) LR 9 Ch App 609, [1874-80] All ER Rep 388; *Re Wigzell, ex parte Hart* [1921] 2 KB 835 at 858.

Official Assignee's general powers, including the power in (b) to "begin, continue, discontinue, and defend legal proceedings relating to the property of the bankrupt", or as a separate stand-alone provision.

### Application to existing trusts and proceedings

16.29 This provision should not apply to proceedings commenced before the amendment comes into force. Once it comes into force it will apply to existing trusts as well as new trusts.

## APPOINTMENT OF RECEIVERS FOR TRUSTS

### RECOMMENDATION

R46 The new Trusts Act should:

- (1) Recognise the court's jurisdiction to appoint a receiver of a trust, which could manage the trust property, on application or on its own motion.
- (2) Provide that applications for appointment of a receiver of a trust would be heard only in the High Court.
- (3) Specify the grounds on which a receiver may be appointed; who may act as a receiver; the powers and duties of a receiver; priorities of those involved; a process for terminating the receivership; and provision for the receiver's fees to be paid out of the trust property.

### Statutory recognition of a receiver for trusts

- 16.30 The High Court currently has the ability to appoint a receiver in respect of trust assets under its inherent jurisdiction.<sup>319</sup> This jurisdiction is rarely exercised, although there is a recent example from the High Court in *Bank of New Zealand v Rowley*.<sup>320</sup> In the *Preferred Approach Paper* we proposed that trust legislation should provide expressly for the appointment of a receiver or liquidator of trusts.<sup>321</sup>
- 16.31 Submitters were overall very supportive of including a mechanism for the appointment of a receiver for trusts in legislation. Submitters commented that this reform would make the ability to appoint a receiver more accessible and modern, to deal with a wider range of issues. In our view the jurisdiction should be confined to the High Court since it is the court that currently has the receivership jurisdiction for companies law.
- 16.32 In order for the provision to be useful to creditors and others dealing with trusts, it will need to go beyond merely restating the availability of the court's jurisdiction to appoint a receiver and will need to include further detail about the process. The recommendation has been expanded to specify the main elements of the scheme that submitters agreed will need to be included in legislation. At the same time, the flexibility of the jurisdiction is preserved so that the court can make orders that are appropriate to the particular case.
- 16.33 The New Zealand Law Society submitted that the provision should limit the range of applicants to creditors, in the same manner as for other entities, rather than an open-ended scope for other parties to apply. However, the jurisdiction to appoint a receiver is broader than that for

319 Noel C Kelly, Chris Kelly and Greg Kelly *Garrow and Kelly Law of Trusts and Trustees* (6th ed, LexisNexis, Wellington, 2005) at [17.9.1].

320 *Bank of New Zealand v Rowley* [2012] NZHC 3540.

321 *Preferred Approach Paper*, above n 306, at P35.

companies. It may be used when there is a risk to the trust property or there is a problem with a trustee or trustees, especially on a temporary basis.<sup>322</sup> Accordingly it could be useful to permit applications by a trustee or beneficiary rather than confining it only to creditors.

16.34 The *Preferred Approach Paper* also included a proposal to appoint a liquidator to liquidate the trust property. Submitters were divided over whether the legislation should include the ability to appoint a liquidator. Some submitters were in favour. Others opposed it on the basis that it was not appropriate to have a liquidator for trusts as a trust was not a legal person. One submitter considered that neither should be applicable to a trustee of a retail fund. There may also be a need for a statutory regime dealing with set-off under netting arrangements entered into by trusts.<sup>323</sup> The Commission acknowledges that providing for a liquidator of trusts raises some complex conceptual and practical issues. In our view liquidation issues are better dealt with in a more comprehensive review of corporations as trustees, rather than in this general review. We intend, therefore, to revisit this issue in the corporate trustee review.

### Application to existing trusts

16.35 The recommended provision will enable applications to be made under it from the commencement of the Trusts Act.

## TRUSTEE'S RIGHT TO INDEMNITY

### RECOMMENDATION

R47 The new Trusts Act should include a provision setting out the following principles:

- (1) A trustee assumes personal liability for expenses and liabilities incurred by the trustee when acting on behalf of the trust.
- (2) A trustee is entitled to be reimbursed from the trust property, or may pay out of the trust property, expenses and liabilities reasonably incurred by the trustee when acting on behalf of the trust.
- (3) A trustee's indemnity in (2) cannot be limited or excluded by the terms of the trust and applies regardless of any contrary intention expressed in the terms of the trust.
- (4) Notwithstanding (3), the terms of the trust may rank the order in which the trust property may be used to meet the trustee's expenses through the trustee's indemnity; this ranking may be set aside on application to court by a trustee, creditor or beneficiary, if the court considers it appropriate, for example on the basis of fraud.
- (5) The indemnity in (2) is available to a former trustee in respect of actions taken by the trustee when acting as trustee.

### Well-understood principles concerning a trustee's indemnity

16.36 The Commission considers it is important to set out the fundamental and well-understood principles relating to the liability of trustees and their right of indemnity, in a modernised version of section 38 of the Trustee Act. The provision will provide clarification and guidance about these principles, particularly for non-lawyers who are trustees or who are dealing with

<sup>322</sup> Kelly, Kelly and Kelly, above n 319, at [17.9.1].

<sup>323</sup> One submitter suggested that there be a regime modelled on the bilateral netting provisions in ss 310A to 310J of the Companies Act, as New Zealand's position is inconsistent with Australia.

trustees, in a simple and concise format. The proposal in the *Preferred Approach Paper* to include these principles in trust legislation was generally supported by submitters.<sup>324</sup>

- 16.37 The provision will cover significant aspects that are not included in section 38 at present. The provision is not intended to cut across existing understandings of the indemnity's operation. It does not cover areas such as the expenses that are the subject of the indemnity, the equitable interest created in trust property, and the enforceability of the right of indemnity against beneficiaries.
- 16.38 The Commission has considered whether the provision should address the extent of the indemnity, particularly the circumstances in which the trustee's indemnity can be reduced or lost. A trustee's indemnity may be reduced or lost where, for example, the trustee was in breach of trust in incurring the obligation,<sup>325</sup> or lacked the authority or capacity to do so, or due to the trustee being indebted to the trust for an unrelated breach of trust, so that set-off arises. Some submitters considered it was necessary for these circumstances to be set out in the legislation. However, we take the view that it is preferable that such matters continue to be determined by the general law. It would be complex and difficult to enumerate the circumstances that could affect the indemnity, and these are very context-dependent. Attempting to set out a list would risk creating uncertainty and could inadvertently displace the current law in this area. Accordingly, the recommendation does not set out any of the circumstances that affect the indemnity. The provision also signals expressly that only expenses and liabilities "reasonably" incurred are covered.

### Indemnity cannot be limited or excluded

- 16.39 R47(3) provides that the indemnity cannot be limited or excluded in the trust instrument. Submitters previously agreed this was likely to be the case already, since it was central to the office of trustee, but that it required clarification.

### Ranking of trust property

- 16.40 However, during consultation it was suggested that the inability to limit or exclude the trustee's indemnity could present a potential difficulty for some trusts. In some cases it may be considered inappropriate that the trustee could potentially acquire an interest in the trust assets through recourse to the indemnity. Examples of situations where this might be the case include where the trust property is taonga Māori, or for legitimate commercial reasons. A submitter contended that the interests of trustees and creditors could still be protected by, for instance, an alternative indemnity or other form of credit enhancement from a third party.
- 16.41 This situation is now addressed in R47(4) which provides for a qualification to the recommendation in R47(3) that the indemnity cannot be limited or excluded. R47(4) provides that it will be possible for the trust deed to rank the order in which the trust property may be used to meet the trustee's expenses through the trustee's indemnity. In particular, it may provide that certain property is to be resorted to only after all other property has been exhausted. The recommendation also states that this ranking in the trust deed may be set aside on application to the court, if appropriate, for instance due to lack of good faith. This scheme enables some recognition for assets that may be significant, for example for social or cultural reasons, by ensuring that these assets will not be affected by the indemnity, unless there are insufficient other trust assets to which to look in order to satisfy the indemnity.

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324 *Preferred Approach Paper*, above n 306, (NZLC IP31, 2012) at ch 8.

325 Aligning with the approach to be taken to exemption clauses, in carving out dishonesty, wilful misconduct and gross negligence.

- 16.42 There is an indicative draft provision that would give effect to R47 set out below in clauses 45–47.

### Application to existing trusts

- 16.43 This recommendation should apply to existing trusts as well as new trusts, as it covers well established principles relating to the trustee's indemnity and content already in the Trustee Act. The provision for ranking trust property for the purposes of satisfying the indemnity will be available to new trusts from the time of commencement, and any existing trusts that are able to vary their terms to take advantage of it.

## CREDITORS DEALING WITH TRUSTEES

### RECOMMENDATION

R48 The new Trusts Act should provide that:

- (1) A creditor to whom a trustee has incurred liability (or the Official Assignee) can rely on the trustee's indemnity to claim against the trust property to satisfy the liability, even if the trustee is not entitled to be fully indemnified.
- (2) This section would only apply where the creditor has given value and the trust property has received a benefit from the transaction between the trustee and the creditor.
- (3) This section would only apply where the creditor has acted in good faith and would not apply if the creditor had knowledge of the circumstances that impaired the trustee's indemnity at the time the transaction was entered into.
- (4) The creditor would take priority over beneficiaries under this section, subject to a decision of the court.
- (5) The creditor would only be able to rely on the trustee's indemnity to the extent of the value that they have given.

### Current recommendation

- 16.44 The Commission is recommending a provision that was not included in the *Preferred Approach Paper*, to strengthen the trustee's indemnity as far as creditors and the Official Assignee are concerned.<sup>326</sup> The application of this provision is confined to the Official Assignee and bona fide creditors who have given value, and where the trust property retains the value from the particular transaction between the trustee and the creditor. In these circumstances the creditor will retain the ability to claim against the trust property through the trustee's indemnity. The creditor will not be considered to have acted in good faith if the creditor had knowledge of the circumstances that excluded or limited the trustee's indemnity.
- 16.45 The intention is that this recommendation will assist certain creditors and the Official Assignee in situations where the trust property would otherwise retain the benefit of the transaction between the trustee and the creditor, thereby receiving a windfall, since the creditor cannot rely on the impaired indemnity. It reflects principles familiar to equity and unjust enrichment. The Official Assignee has been included as the Official Assignee is the appropriate party to act on behalf of creditors in the event that the trustee becomes bankrupt or goes into liquidation.

<sup>326</sup> A similar proposal was discussed in *Fifth Issues Paper*, above n 306, at [7.40]–[7.45].



- 16.46 The effect of this recommendation would be to place the creditors that meet the requirements in the same position as they would otherwise have been but for the circumstances that impaired the indemnity, for example a breach of trust by the trustee. The consequences of the creditor being able to claim through the trustee's indemnity would remain the same as under the current law. This recommendation is not intended to give the creditor particular priority over other creditors in insolvency; nor would it give the creditor a security interest in the property. The creditor would not be in a better position than other trust creditors who were able to rely on an unimpaired indemnity. If payment were obtained under this section in an insolvency context, the proceeds would be distributed among creditors in a priority in accordance with ordinary insolvency law principles.
- 16.47 The current recommendation stops short of permitting creditors to claim directly against the trust property; although the effect may be similar, the claim would be against the trustee. This approach of strengthening the indemnity was preferred over providing creditors with the ability to claim against the trust assets directly. Direct recourse, while attractive in many respects, was considered a more significant departure from conventional trust principles and the approach taken in the rest of this Report, since it effectively treated the trust as a separate entity. We consider the recommended approach to be more conceptually sound and appropriately targeted.
- 16.48 We include below an indicative draft of the provisions relating to the trustee's indemnity. Clauses 45 to 47 give effect to R47. Clause 48 is intended to show how R48 would operate in the straightforward case of a creditor claiming against a trustee.

### Application to existing trusts

- 16.49 This recommendation should apply to existing trusts as well as new trusts. It should only apply to transactions entered into after the commencement of the new Trusts Act. This is because it involves a change to the existing law. It will impact on the interests of beneficiaries as they will not be protected by the severance of the trustee's indemnity where the transaction with the creditor falls within the requirements of this provision. Therefore it is appropriate only to apply this to transactions going forward.

## INDICATIVE DRAFT PROVISIONS – TRUSTEE'S INDEMNITY

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### Part 2 Trustee's indemnity

#### 45 Trustee is personally liable for expenses and liabilities

A trustee is personally liable for an expense or a liability incurred by the trustee when acting as a trustee.

#### 46 Trustee's right to indemnity

- (1) A trustee who reasonably incurs an expense or a liability when acting on behalf of the trust is entitled to—
  - (a) the payment or discharge of the expense or liability out of the trustee's own funds and reimbursement from the trust property; or
  - (b) the payment or discharge of the expense or liability from the trust property.
- (2) Subsection (1) applies regardless of any contrary intention expressed in the terms of the trust.
- (3) Subsection (1) applies to a former trustee in relation to an expense or a liability incurred as a trustee acting on behalf of the trust.

**47 Ranking of trust property**

- (1) For the purposes of **section 46(1)**, the terms of the trust may rank the order in which the trust property must be applied to reimburse the trustee or pay or discharge an expense or a liability.
- (2) However, the court may set aside a ranking of trust property under **subsection (1)** on the application of—
  - (a) the trustee; or
  - (b) a creditor; or
  - (c) a beneficiary.

**Commentary**

It should be noted that clause 45 does not prevent a trustee from agreeing in any contract with third parties, for example, that the trustee's liability shall be limited to the trust assets.

Clause 46 modernises the language of section 38(2) Trustee Act 1956. It expands it to include reference to the trustee's personal liability, and clarifies that the indemnity cannot be limited or excluded in the trust deed. Note that this recommendation concerns the trustee's indemnity for expenses and liabilities incurred as trustee. R4 contains recommendations about how the indemnity clauses in trust deeds apply in situations where there has been a breach of trust by trustees.

Subsection (1) of section 38 (on liability of co-trustees) will also need modernising and re-enacting in trust legislation in a separate section. We consider that the latter part of section 38(2) (on trustees being paid for professional services) will be covered adequately by the duty to act without reward, which will apply unless expressly varied by the terms of the trust (see R3).

**48 Creditor's limited claim to trust property through trustee's indemnity**

- (1) This section applies where—
  - (a) a trustee has incurred an expense or a liability to a creditor; and
  - (b) the creditor has given value; and
  - (c) the trust property has received a benefit from the transaction between the trustee and the creditor; and
  - (d) the creditor has acted in good faith.
- (2) In a case to which this section applies, the creditor may claim to be indemnified out of the trust property as if the creditor were a trustee, notwithstanding that the trustee for any reason is not entitled to be fully indemnified.
- (3) The creditor has not acted in good faith if the creditor had knowledge of any circumstances that excluded or limited the trustee's indemnity.
- (4) A claim under this section—
  - (a) is limited to the value given by the creditor; and
  - (b) must be paid in priority over any payment to a beneficiary, unless the court orders otherwise.

## **Commentary**

This clause as drafted does not address the position of the Official Assignee in respect of R48. Provisions would also need to be included providing for the operation of this process in relation to a bankrupt or insolvent trustee. These have not yet been drafted.

Examples of circumstances where the trustee is not entitled to be fully indemnified include where the trustee was in breach of trust, or lacked capacity or authority in incurring the liability, or due to beneficiary cross-claims against the trustee.

It is not intended that a creditor relying on this provision would receive particular priority over other creditors in the event of bankruptcy or liquidation. If a creditor or the Official Assignee relies on this provision in an insolvency context to obtain payment via the trustee, it is intended that the proceeds would be distributed among creditors in a priority in accordance with ordinary insolvency law principles.

If a creditor relies on this provision and obtains a payment, and then subsequently the trustee is bankrupted or liquidated, the payment could nonetheless still be voidable under the insolvent transaction regime in section 194 Insolvency Act 2006 or section 292 Companies Act 1993, as appropriate.

It is also not intended that this provision would give the creditor a security interest in the trust assets via the trustee's equitable lien.

# Chapter 17

## Perpetuities and the maximum duration of trusts

### INTRODUCTION

17.1 In this chapter we put forward recommendations for reform of the rule against perpetuities, which has the effect of limiting the duration of a trust. This issue was discussed in the *Third Issues Paper* and *Preferred Approach Paper*.<sup>327</sup> The topics examined in the chapter are:

- the rule against perpetuities/remoteness of vesting;
- the duration of trusts;
- the rule against accumulations; and
- exemptions to allow perpetual trusts in certain circumstances.

### MAXIMUM DURATION OF TRUSTS

#### RECOMMENDATION

R49 The new Trust Act should:

- (1) Repeal the Perpetuities Act 1964 and provide that the common law rule against perpetuities is of no application in New Zealand from the date of the repeal forward.
- (2) Provide a default duration of 150 years for all trusts (a shorter period may be specified in the terms of the trust).
- (3) Provide that at the expiry of 150 years from the date of the establishment of a trust, all trust property is to be vested in accordance with the provisions contained in the terms of the trust, or if the trust deed is silent about who is to receive the property, it is to be vested in all surviving beneficiaries in equal shares.
- (4) Provide that trusts which include a mechanism to calculate the vesting date rather than specifying a duration shall continue until the earlier of the date resulting from the calculation, or 150 years from the establishment of the trust.
- (5) Provide that, notwithstanding these reforms, distributions which were valid under the Perpetuities Act 1964 at the date they occurred remain valid.
- (6) Repeal section 59(2) of the Property Law Act 2007 to reflect the abolition of the rule against perpetuities.

<sup>327</sup> Law Commission *Perpetuities and the Revocation and Variation of Trusts: Review of the Law of Trusts – Third Issues Paper* (NZLC IP28, 2011) at pt 1; Law Commission *Review of the Law of Trusts – Preferred Approach* (NZLC IP31, 2010) at ch 14.

- (7) Update the rule against accumulations to reflect the abolition of the rule against perpetuities, and clarify that trustees may accumulate income, provided the terms of the trust do not prevent this, and provided the accumulated income is distributed upon or before the termination of the trust.
- (8) Carry over the existing exemptions allowing the trusts referred to in section 19 of the Perpetuities Act 1964 to continue indefinitely and apply these exemptions to the rule limiting the duration of trusts (trusts for retirement schemes under the Financial Markets Conduct legislation, currently referred to as superannuation schemes, and certain trusts of a share purchase scheme under section YA1 Income Tax Act 2007), as well as trusts currently exempted in their own legislation.
- (9) Provide that these reforms will apply to all trusts, not only express trusts within the new Act.

### Problems with current law

- 17.2 The rule against perpetuities is one of a collection of rules and restrictions developed by the courts to promote unfettered ownership and free transfer of property. It has the effect of setting a maximum duration of a trust. The classic statement of the rule is this: no interest is good unless it vests, if at all, not later than 21 years after some life in being at the creation of the interest.<sup>328</sup> Trusts must establish a date for the final distribution of trust property. The date may either be fixed, or calculated with reference to someone's life (or the lives of more than one person). Under the common law, a fixed date could not exceed 21 years from the date of settlement.<sup>329</sup>
- 17.3 Equity also developed a distinct rule precluding perpetual trusts.<sup>330</sup> In the Perpetuities Act 1964 and subsequent legislation, the phrase "rule against perpetuities" is used to refer to both the rule against remoteness of vesting, and the rule against perpetual trusts, depending on the context.<sup>331</sup> However, the two rules are conceptually distinct. For example, a future interest created to take effect beyond the perpetuity period will not be valid by reason of being created to benefit a charity, even though a charitable trust may exist "in perpetuity".<sup>332</sup>
- 17.4 The Perpetuities Act made a number of modifications to the common law position on remoteness of vesting, including the ability to specify a perpetuity period of 80 years or less and the "wait and see" approach to interests which may or may not vest within the perpetuity period.<sup>333</sup> Under the rule in *Saunders v Vautier*<sup>334</sup> a trust can also be varied by the agreement of all beneficiaries, to provide for an earlier distribution.<sup>335</sup> This means that since the Perpetuities Act

328 JC Gray *The Rule against Perpetuities* (4th ed, Little Brown & Co, Boston, 1942) at 201.

329 See *Cadell v Palmer* (1833) 1 Cl & F 372, 6 ER 956.

330 This is also known at times as the rule against indestructibility of trusts or the rule against inalienability. This rule had its most common application in relation to non-charitable purpose trusts. See David Hayton, Paul Mathews and Charles Mitchell (eds) *Underhill and Hayton: Law Relating to Trusts and Trustees* (18th ed, LexisNexis, London, 2010) at 279–281. For an example of the general rule limiting the duration of trusts as applied to an allowable purpose trust, see *Re Dean* (1889) 41 Ch D 557.

331 For example, most Treaty settlement legislation includes a provision to the effect that neither the rule against perpetuities nor the Perpetuities Act 1964 will prescribe or restrict the period during which a trust created under that legislation may exist. In contrast, the Perpetuities Act 1964 itself appears concerned mainly with the implications of the rule for remoteness of vesting.

332 *Attorney General v Webster* (1875) LR 20 Eq 483.

333 This is known as *cy-pres* modification. See Perpetuities Act 1964, ss 9–12.

334 *Saunders v Vautier* (1841) Cr & Ph 240, 41 ER 482.

335 If any of the beneficiaries are minors or otherwise incapacitated, the court may approve a variation. See *Third Issues Paper*, above n 327, at pt 2, and ch 10 of this Report.

commenced, most dispositions, which would otherwise have been invalidated under the rule against perpetuities, are able to be rescued through modification.

- 17.5 Even with the amendments under the Perpetuities Act, the rule against perpetuities is complex and causes considerable problems in practice.<sup>336</sup> Most obviously, it causes uncertainty and there is a risk it may invalidate legitimate dispositions. It is not well understood, and so trust deeds may inadvertently fall foul of its requirements. The rule is also difficult to reconcile conceptually with the modern discretionary trust.

### General approach

- 17.6 We recommend reform to simplify and modernise the law in this area by replacing the current common law and statutory rules with a bright-line, maximum duration limit for trusts of 150 years. The new law would be much easier to understand and would improve certainty in trust dealings. There are advantages to a clear limit that provides certainty at the outset of the creation of the trust. The 150-year period allows a high degree of flexibility for settlors to dispose of property as they choose.
- 17.7 Some submitters to the *Preferred Approach Paper* and previous issues papers considered that the original policy rationales for the rule against perpetuities are no longer persuasive in the modern context and that the rule should be abolished entirely. In recent years, many jurisdictions have abolished the rule against perpetuities and allowed perpetual trusts.<sup>337</sup> England and Wales are notable for not following this path, and reforming rather than removing the rule.<sup>338</sup> Some submitters expressed the view New Zealand should follow the global trend and allow perpetual trusts. However, we note that if New Zealand were to abolish the rule against perpetuities, rather than reform it, we would be doing so in the context of a tax system that does not otherwise discourage trusts of long duration.<sup>339</sup>
- 17.8 We continue to consider that extending the maximum duration of trusts is more appropriate than permitting trusts to continue indefinitely. In our view, there are strong policy reasons to retain some form of limit on the duration of private trusts. There is an important difference between trusts that continue for two or three generations and trusts that continue indefinitely. Perpetual trusts could create problems for trust administration and undermine the interests of the current generation of beneficiaries. It will be difficult for trustees to discharge their duties in a perpetual trust because the interests of successive generations of unborn beneficiaries would need to be considered. An ever-increasing class of beneficiaries would eventually make a trust administratively unwieldy, or invalid because of a lack of certainty of objects. The greater the number of beneficiaries, the more difficult it would be to vary the trust. There is also a risk that settlors may inadvertently create perpetual trusts, preventing the immediate beneficiaries from enjoying property, though the settlor's intention may be only to benefit the next few generations. Trusts of long duration may also create problems, such as a growth in the number of beneficiaries and the fragmentation of interests in real property, or the risk that the purpose for which the trust was established will cease to be relevant as times change. It is acknowledged

336 Law Commission (England and Wales) *The Law of Trusts: The Rules Against Perpetuities and Excessive Accumulations: A Consultation Paper* (Consultation Paper No 133, 1993) at [4.1]–[4.36].

337 The rule has now been abolished in six Canadian states and 21 states within the United States of America, as well as Ireland and South Australia. The Law Reform Commission of Nova Scotia has also recommended abolition: Law Reform Commission of Nova Scotia *The Rule Against Perpetuities* (Final Report, 2010).

338 See the Perpetuities and Accumulations Act 2009 (UK).

339 For example, the report by the Irish Law Commission recommended abolishing limits on the duration of trusts on the basis that the tax system provided sufficient disincentives for trusts of long duration, including through an annual tax on the capital held in trust. This argument for abolition does not apply in New Zealand. See Law Reform Commission of Ireland *Report on the Rule against Perpetuities and Cognate Rules* (LRC 62-2000).

that there are arguments to the contrary,<sup>340</sup> but we are persuaded that it is preferable to retain a limit on the duration of trusts, as England and Wales have done. We therefore recommend the more modest proposal of a statutory limitation on the duration of trusts.

### Intent of recommendation

- 17.9 Our recommendation is to repeal the outdated rule against remoteness of vesting, and create a statutory maximum duration for trusts of 150 years. This would address the practical concerns expressed by those who favoured reform or complete abolition, through providing a bright-line rule that is easy to understand and promotes certainty in trust dealings. It would prevent perpetual trusts, while allowing a high degree of flexibility for settlors to dispose of property as they choose.
- 17.10 The recommended change would apply to all trusts currently in existence, regardless of when the trust was created. The change would therefore “rescue” existing trusts that fail to comply with the current rule against perpetuities, without requiring modification of the trust deeds of such trusts. However, it would not validate trusts previously held invalid and would not affect prior distributions.
- 17.11 It should be noted that although the new limit will potentially apply to all trusts, existing trusts will continue to operate according to their own terms. Trusts do not automatically gain the benefit of the 150 year period, and must abide by the period set out in the trust deed. Further comments on the application of the reform to existing trusts are set out below.
- 17.12 Given increasing life expectancies, we prefer an upper limit of 150 years. This will allow most trusts established for the duration of a life in being plus 21 years to continue until their natural end.

### Property Law Act 2007

- 17.13 As part of the recommendation, it is also necessary to update section 59 of the Property Law Act 2007, which currently allows future interests to be created subject to the rule against perpetuities.<sup>341</sup> Reform to this section would provide that future interests may be created to take effect at any future date.
- 17.14 This reform will have implications for property transactions which involve deferred or contingent interests, such as an option to purchase.<sup>342</sup> This is an area where the traditional rationales of the rule against remoteness of vesting conflict with modern commercial practice. In addition, because the rule is concerned with the date interests take effect and not their duration, it can cause confusion as to what is included and what is excluded. The area is not well understood, and causes confusion as well as potentially altering the burdens and benefits in property arrangements through voiding some elements of the arrangement, but not others. For these reasons, we prefer the repeal of section 59(2) of the Property Law Act, rather than requiring all future interests to take effect within 150 years of their creation.

### Rule against accumulations

- 17.15 A related rule is the rule against excessive accumulations. This provides that a direction to accumulate funds is void if it extends beyond the perpetuity period. This is significant in relation to charitable trusts and other trusts that are able to exist in perpetuity. The Perpetuities

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340 See *Third Issues Paper*, above n 327, at pt 1, and *Preferred Approach Paper*, above n 327, at ch 14.

341 See further *Preferred Approach Paper*, above n 327, at [14.22]–[14.33].

342 The common law rules relating to options to purchase have been modified by s 17 of the Perpetuities Act 1964.

Act reformulated the common law rule by providing that a direction to accumulate and dispose of funds will be valid if the disposition is valid, and will be invalid if the disposition is invalid.<sup>343</sup>

- 17.16 It is proposed that the rule against accumulations be retained but updated for consistency with other reforms. The new rule would clarify that trustees may accumulate income, provided the trust deed does not prevent this and provided the accumulated income is distributed upon the termination of the trust. This has been changed from the *Preferred Approach Paper* proposal which stated that trustees may accumulate income provided the trust deed so allows, to allow more flexibility.<sup>344</sup> The proposal to state a maximum accumulations period for trusts has been removed, since the accumulated income must be distributed on termination of the trust, which must be within the 150-year maximum duration, so it is not necessary also to specify a maximum accumulations period.
- 17.17 An issue arises with the position in relation to charitable trusts and other allowable perpetual trusts where there is a direction to accumulate. The position at common law is that a direction requiring a charitable trust to accumulate income beyond the perpetuity period is a fetter on the use of the fund for charitable purposes and is therefore void.<sup>345</sup> The case of *Re Armstrong*<sup>346</sup> establishes that this position continues in New Zealand notwithstanding the Perpetuities Act. It may be desirable for legislation to restate this principle and extend it to other non-charitable purpose trusts, by providing that a direction to accumulate income is void if it extends for longer than a set period. This period could be the accumulations period if one were set, or could match the maximum duration period. There may be a case for directions to accumulate income to be limited for charitable trusts to a shorter period, for example 25 years, based on the idea that a binding direction to accumulate is a fetter on the charitable use of the fund. However, we intend to explore this question and consult further in the context of our upcoming charitable and purpose trusts review.
- 17.18 It should be noted that the issue of directions to accumulate for charitable trusts is separate from the situation where there is a discretion for the trustee to accumulate. There is no intention to affect any provision in trust deeds permitting trustees to exercise their discretion in respect of capitalisation and accumulation of income.

### Application to different types of trust

- 17.19 In our view it is simplest to have a maximum limit for all trusts, and list any specific additional exemptions. A maximum duration of 150 years is of a sufficient length to ameliorate the current problems with remoteness of vesting and allow for commercial certainty in developing trust structures. However, any trusts currently exempted from the perpetuity period in individual statutory schemes would also be exempted from the 150 year maximum duration; this may require consequential amendments to those statutes.

#### *Trusts for superannuation/retirement schemes and unit trusts*

- 17.20 It is intended that those trusts currently exempted from the rule against perpetuities<sup>347</sup> will be exempted from the maximum duration rule. This will include trusts for superannuation

343 It is arguable that the common law rule was never in effect in New Zealand due to its amendment by the Accumulations Act 1800 (UK), which was held to apply in New Zealand in *The Trustees, Executors, and Agency Company (Limited) v Bush and Anor* (1908) 28 NZLR 117. The provision in s 21 of the Perpetuities Act 1964 can therefore be seen as reverting to the common law rule and departing from the statutory variation passed by the Parliament of the United Kingdom.

344 *Preferred Approach Paper*, above n 327, at P54.

345 *Martin v Margham* (1844) 14 Sim 230, followed in *The Trustees, Executors, and Agency Company Limited v Bush and Anor* (1908) 28 NZLR 117 at 119–120.

346 *Re Armstrong* [2006] 1 NZLR 282 (HC) (also cited as *Perpetual Trust Ltd v Roman Catholic Bishop of the Diocese of Christchurch*).

347 Perpetuities Act 1964, s 19.



schemes (soon to be termed retirement schemes under the Financial Markets Conduct Bill) and certain trusts under section YA1 of the Income Tax Act 2007.

- 17.21 The *Preferred Approach Paper* also put forward a proposed exemption for unit trusts;<sup>348</sup> these will also soon be covered under the Financial Markets Conduct Bill. On reflection, we have decided not to include a specific exemption for unit trusts in the final recommendation. This is because unit trusts tend to be relatively short-term structures and do not have the same policy reasons necessitating a maximum duration for other trusts, that is, concerns about “dead hand” control and tying up assets indefinitely.

#### *Māori land trusts and Treaty settlement trusts*

- 17.22 All Acts relating to Treaty of Waitangi settlement claims passed in recent years have included a provision that expressly excludes the rule against perpetuities and the provisions of the Perpetuities Act from applying to the settlement entity trust, for example section 20 of the Ngāti Whātua Ōrākei Claims Settlement Act 2012. In line with the approach of applying current perpetuities exemptions to the new maximum duration rule, these settlement trusts would need to be exempted from the maximum duration rule by consequential amendment.
- 17.23 A slightly different approach is taken in Te Ture Whenua Maori Act 1993, which provides in section 235 that Māori land trusts established under that Act are not “subject to any enactment or rule of law restricting the period for which a trust may run”. It is intended that these trusts also would be exempted from the 150 year maximum duration rule. The wording of this provision would seem to be sufficient to exempt these trusts from the new maximum duration rule without amendment. However, if not, a consequential amendment should be made to maintain their current status as perpetual trusts.

#### *Energy trusts*

- 17.24 Energy trusts are currently bound by the Perpetuities Act and rule against perpetuities. We have considered whether there should also be an exemption for these trusts. Energy Trusts of New Zealand and individual energy trusts such as the Auckland Energy Consumer Trust strongly submitted that existing energy trusts should be permitted to continue indefinitely. They argued that the policy reasons for the rule against perpetuities and limits on the duration of trusts are not relevant to the circumstances of energy trusts. In their view, permitting energy trusts to continue indefinitely would not defeat the intention of the settlor. Arguments were also made that it would be too expensive for the smaller energy trusts to go to court to apply for a variation, and accordingly, all existing energy trusts should be made indefinite with the ability to “opt out”.
- 17.25 The *Preferred Approach Paper* proposed an exemption from the maximum duration rule for new energy trusts.<sup>349</sup> However, we have reached the conclusion that whether energy trusts, new or existing, should be perpetual is a policy issue we cannot resolve as part of this review. We take the approach that energy trusts, which do not currently have an exemption, should be in the same position as other trusts. It is not feasible for us to consider the issues around creating new exemptions for types of trust that are not currently exempted from the perpetuities rule. Energy trusts will be subject to the same transitional process as other trusts since there are still final beneficiaries affected by a change in the trusts’ termination date. Any exemption for a particular type of existing trust will need to justify the departure from the general presumption that the trust property will vest according to its terms. We consider that the appropriateness of allowing

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348 *Preferred Approach Paper*, above n 327, at P54(i).

349 At P54(j).

existing energy trusts to operate indefinitely is a policy question better reserved for a decision by the Government rather than being resolved in this Report. We have therefore treated energy trusts the same way as any trust not currently exempted from the perpetuities rule.

### Application to existing trusts

- 17.26 The 150 year maximum duration rule will apply to all trusts currently in existence, as well as any trusts established after the rule comes into effect. However, the 150 year duration period will not apply to existing trusts automatically, and existing trusts will continue to be bound by the provisions in their respective trust deeds. Several submitters to the *Preferred Approach Paper* raised practical questions about how the proposed changes would be applied to existing trusts. We have attempted to avoid creating complex transitional provisions for existing trusts.
- 17.27 More significantly, in this area it is important to take account of the intention of the settlor and beneficiaries' interests. It is difficult to say in any particular instance that a settlor would have opted for a 150 year period. Extending the period would risk going beyond what the settlor intended. Once settled, trusts are only changed by agreement between the beneficiaries, by a court order or as provided for in the terms of the trust. Importantly, changing the vesting date not only changes the date by which all assets must vest, but would likely change the identity of the beneficiaries in whom the assets ultimately vest. Our view is that it is not appropriate to be able to easily alter the period because this will also alter these beneficial interests.
- 17.28 Trusts (both existing and new) which include a mechanism to calculate the vesting date rather than specifying a duration, would continue until the earlier of the date resulting from the calculation, or 150 years from the establishment of the trust.
- 17.29 Where the distribution date in an existing trust is fixed, this date will continue to apply. It may be possible to vary the vesting or termination date of the trust using provision in the trust deed where it allows for this. It may also be possible to extend the period by variation, agreement of the beneficiaries, or applying to the court for approval of a variation.
- 17.30 Some submitters argued for some form of simple, less costly process to extend the duration of a trust to 150 years. We have considered various options including allowing trustees to vary the trust to extend the period, notwithstanding that the terms of the trust do not provide for this. We also considered providing a specific provision allowing the court to extend the duration of a trust using a less onerous test for approving a variation. However, we do not think it is appropriate for trustees to be able to effect this change where this is not provided for in the terms of the trust, since it affects those beneficiaries who may be about to receive property if a trust is close to its vesting date. Likewise, it is not appropriate to formulate any different or lower test for variation by the courts, as this also affects beneficial interests. We acknowledge that there is a cost involved in taking an application to court, but we consider that the question of whether the duration of a trust can be extended is best left to the courts.

# Chapter 18

## Regulation

### INTRODUCTION

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- 18.1 In the *Fifth Issues Paper* the Commission considered whether a register of trusts should be introduced to keep an official record of trust relationships.<sup>350</sup> The Commission also considered whether there was any need for additional regulation of individuals and companies that provide services to settlors establishing trusts or to trustees administering and managing trusts.<sup>351</sup> We concluded in the *Preferred Approach Paper* that we should not introduce either a system for registration of trusts or regulation of those providing advisory services relating to trusts.<sup>352</sup>
- 18.2 This chapter briefly confirms those conclusions and reports back on the views of submitters.

### REGULATION OF ADVISERS

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- 18.3 In this area, occupational regulatory regimes apply to lawyers, chartered accountants and financial advisers.<sup>353</sup> Trustee companies are regulated by a specific statutory regime.<sup>354</sup> The Securities Trustees and Statutory Supervisors Act 2011 introduced a licensing regime for trustees and statutory supervisors of unit trusts and retirement villages.<sup>355</sup> However, these regimes do not cover everyone who provides advisory and management services to settlors and trustees. There are companies and individuals providing services that are not covered by any professional standards regime.
- 18.4 For completeness, we mention also the Anti-Money Laundering and Countering Financing of Terrorism Act 2009 which, since 30 June 2013, has imposed anti-money laundering reporting requirements on any person in the business of forming trusts (unless exempted) and statutory trustee companies.<sup>356</sup> Under this regime, those providing trust-related services as a business are reporting entities required to comply with the regime's requirements.<sup>357</sup> Of course, the purpose of the regime is to deter and detect money laundering and the financing of terrorism. It is not

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350 Law Commission *Court Jurisdiction, Trading Trusts and Other Issues: Review of the Law of Trusts – Fifth Issues Paper* (NZLC IP28, 2011) at ch 9.

351 At ch 10.

352 See Law Commission *Review of the Law of Trusts – Preferred Approach* (NZLC IP31, 2012) at P55 and P56.

353 Lawyers are regulated under the Lawyers and Conveyancers Act 2006 and the Lawyers and Conveyancers Act (Lawyers: Conduct and Client Care) Rules 2008. Chartered accountants are a self-regulated professional group. They must be members of the New Zealand Institute of Chartered Accountants and are subject to its regulatory standards, mandatory professional development, code of ethics and professional standards. Financial advisers and financial service providers are regulated by the Financial Advisers Act 2008 and the Financial Service Providers (Registration and Dispute Resolution) Act 2008.

354 Trustee companies listed in s 2 of the Trustee Companies Act 1967 are regulated by that Act, the Trustee Companies Management Act 1975, and the Trustee Companies Management Amendment Act 1978.

355 The Securities Act 1978 requires all public issuers of debt and equity securities to appoint a trustee and the issuers of other participatory securities to appoint statutory supervisors. The Unit Trusts Act 1960 similarly requires that a trustee be appointed in respect of a unit trust, and the Retirement Villages Act 2003 requires retirement villages to appoint a statutory supervisor. Note that the Financial Markets Conduct Bill 2011 (342-2) currently before Parliament will repeal the Securities Act and the Unit Trusts Act, and also amend and rename the Securities Trustees and Statutory Supervisors Act 2011.

356 Since 30 June 2013, all reporting entities have been required to maintain records and report against anti-money laundering measures contained in the Anti-Money Laundering and Countering Financing of Terrorism Act 2009. A reporting entity is partially defined in the Act but also includes a person or class of persons declared by regulations to be a reporting entity; see s 5. Reg 17 of the Anti-Money Laundering and Countering Financing of Terrorism (Definitions) Regulations 2011 provides that a person who carries out, as a principal part of their business, the formation of trusts will be a reporting entity. However, reg 20 exempts lawyers who do this in the ordinary course of their business.

357 Anti-Money Laundering and Countering Financing of Terrorism (Definitions) Regulations 2011.

concerned with monitoring or regulating the professional competence of the advisers involved in the activities covered, although one might anticipate some flow-on benefits here.

- 18.5 Finally, general consumer protection regulation is also relevant. The Consumer Guarantees Act 1993 applies to all trade and professional services of a personal or consumer nature. This Act guarantees that such services will be carried out with reasonable skill and care and that they will be fit for any particular purpose that the consumer makes known to the service provider. It also guarantees that services will be completed within a reasonable time and at a reasonable cost. Where a service provider fails to meet these standards, consumers are able to cancel services, refuse payment (or part-payment) or claim compensation.
- 18.6 The Fair Trading Act 1986 prohibits traders from making false or misleading representations about their services. Remedies are also available under that Act where service providers breach that obligation.

### Regulatory “gap”

- 18.7 There is currently a regulatory “gap” in occupational regulation. Everyone who is in the business of providing trust formation and management services or advice to consumers, rather than to other commercial clients or businesses, is covered by consumer protection legislation, but that consumer legislation does not set occupational standards and obligations in the way occupational regulation does. Not all advisers or service providers are required to be registered or required to comply with standards of professional competence in the way that lawyers and financial advisers are. Also, consumer protection does not apply in a commercial context.
- 18.8 The extent and significance of the regulatory gap is unclear. The number of service providers that operate in this unregulated gap and the nature and quality of the services they provide are not specifically monitored. However, as discussed in our earlier papers, the (then) Ministry of Economic Development advised us that it considered the gap in occupational regulation to be very small.<sup>358</sup>

### Additional regulation not recommended

- 18.9 The Commission considered but rejected the option of requiring everyone providing trust formation and management services or advice in relation to trusts to be registered and regulated. We canvassed the issues fully in the *Fifth Issues Paper* and summarised the different regulatory options in the *Preferred Approach Paper*.<sup>359</sup>
- 18.10 A few submitters who favoured regulation commented on the *Preferred Approach Paper*. The point was made that without some form of registration it would continue to be difficult to gauge whether unregulated service providers are a problem. Given the large numbers of trusts in New Zealand containing significant wealth, these submitters said that it is important that trusts are well administered. They said that there is some anecdotal evidence to suggest that some service providers are not reaching an acceptable standard.
- 18.11 We carefully weighed these points when reaching our final view. We recognise that there are some difficulties in forming an accurate picture of the sector. However, the information that is available does not indicate any significant problems. We found no evidence of the type of systemic problems that would justify the costs and intrusion involved in establishing a register of service providers and resourcing a regulator to establish and monitor standards.

358 Ministry of Economic Development “Comment on External Paper” (21 November 2011). The Ministry of Economic Development is now a part of the Ministry of Business, Innovation and Employment.

359 *Fifth Issues Paper*, above n 350, at ch 10; *Preferred Approach Paper*, above n 352, at ch 15.

- 18.12 The majority of those providing advisory and management services in relation to trusts are already regulated. The financial advisers' regime, current professional regulation and the anti-money laundering legislation together cover most of those operating in this market. We think that the gap in occupational regulation is relatively small and it should, at least at this stage, be left to the market and general consumer protection legislation to moderate the standard of services. In our view it would be appropriate for the Ministry of Business, Innovation and Employment to continue to monitor the situation for developments.

### *Foreign trust industry*

- 18.13 A few submitters, most of whom did not favour regulation for domestic service providers, considered that there may be a separate case for regulating organisations acting as professional trustees or otherwise providing trust related services to foreign or offshore trusts in New Zealand. They argued that this would be desirable to help protect and support New Zealand's reputation as a global centre for trust administration. The New Zealand Branch of the Society of Trust and Estate Practitioners were concerned that unscrupulous service providers could harm New Zealand's international reputation. The New Zealand Branch of the Society of Trust and Estate Practitioners and a few other submitters supported a standalone, light-handed regulatory model for trust and company service providers servicing the offshore market. They considered that this would help develop and promote New Zealand as a jurisdiction of choice. It was noted by one submitter that other jurisdictions regulate their international trust administration industries because internationally there is a competitive advantage for trust companies to hold themselves out as being regulated. Regulation can attract foreign trusts and promotes confidence in the jurisdiction.
- 18.14 We acknowledge the development in New Zealand of the offshore market and the accompanying international trust administration industry. We have not formed any views about whether New Zealand might wish to consider regulating to promote the development of an offshore market. Nor have we attempted to address any issues relating solely to New Zealand developing as an offshore jurisdiction for foreign trusts in this Report.
- 18.15 Our focus throughout our review has been on New Zealand's domestic or onshore jurisdiction and on addressing the central matters of trust law in that context. In ensuring that core matters of trust law are appropriate for our onshore jurisdiction, we will also protect and support New Zealand's international reputation in trust law. This in turn promotes confidence in New Zealand's trust law jurisdiction, which may have flow-on benefits for the offshore or foreign trust industry in New Zealand.
- 18.16 Whether there should be a specific regulatory scheme to cover those individuals and organisations servicing the foreign or offshore trust industry in New Zealand is not an issue we have considered as part of this review. That question is part of a broader question concerning whether New Zealand wishes to develop specific regulatory infrastructure to promote and protect the foreign trust industry. Such economic issues fall beyond the scope of this review and will need to be considered elsewhere.

## **REGISTRATION OF TRUSTS**

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### **Law and issues**

- 18.17 At present there is little registration of trusts in New Zealand. Charitable trusts that wish to incorporate as charitable trust boards register when incorporating under the Charitable Trusts Act 1957. Charitable trusts (whether incorporated or not) must also register with the Charities Board under the Charities Act 2005 if they want to be recognised as charities. Foreign trusts

must be registered with the Inland Revenue regardless of whether they derive taxable income or not.<sup>360</sup> Income-earning trusts also must register as tax payers with Inland Revenue.

- 18.18 However, there is no register for standard inter vivos or testamentary trusts. In respect of incorporated charitable trust boards, registration is the process that establishes such a trust board as a corporate body. As trusts otherwise do not have legal personality, there is not the same necessity for a registration system to establish legal personality. Most trusts registration systems can only serve information collection and record-keeping functions.
- 18.19 There are also no external reporting requirements for trusts other than the requirement for income-earning trusts to submit a tax return to the Inland Revenue. Up until 1 October 2011, those making gifts in excess of \$12,000, including settlors gifting to private trusts, had to submit an annual gifting return to the Inland Revenue indicating how much had been given in order to be assessed for gift duty. This included settlors who were gradually gifting to the trust the value of the settlement of trust property at a rate that was under the threshold for gift duty. This created a de facto reporting requirement for a number of trusts. Gift duty has now been abolished so the accompanying reporting has ceased. The Anti-Money Laundering and Countering Financing of Terrorism Act imposes some reporting requirements in respect of trusts. Those who form trusts in the course of their business are required to obtain, verify and retain records of the beneficial ownership and control of trusts.<sup>361</sup>

### **Fifth Issues Paper explored registration**

- 18.20 In the *Fifth Issues Paper* we discussed in some detail the option of requiring trusts to be registered.<sup>362</sup> Registration is normally suggested as a way of attempting to make more information about the use of trusts and about individual trusts available. Because most trusts are essentially private arrangements, in the same way most contracts are private arrangements, there are few official requirements that alert the Government or the public to the existence of a trust. The Government has limited information about the use of trusts generally in New Zealand and about features of individual trusts that may be relevant to applications for government assistance.
- 18.21 It can also be difficult for third parties to know that they are actually contracting with a trustee rather than a beneficial owner. The requirements for the administration of trusts are obligations owed only to the beneficiaries. There is no official body that has the responsibility and access to information to ensure that trusts are being properly administered. A general register of trusts had been suggested by members of the public and media, as a way of officialising trusts and making them more transparent. Compared with the registration and reporting requirements for companies, the absence of a register for trusts means it is comparatively easy for trusts to be established, administered and altered, and for property ownership in trusts to be flexible.

### **Preferred Approach Paper**

- 18.22 After carefully considering the case for registration, including considering all the matters raised by submitters responding to the *Fifth Issues Paper* we concluded in the *Preferred Approach Paper* that a system of registration for trusts should not be introduced.
- 18.23 As we acknowledged in the *Preferred Approach Paper*, a register of trusts would have some important benefits. The nature and extent of these would depend somewhat on the amount

360 Resident trustees of a foreign trust must disclose the name or other identifying particulars of the trust (such as the date of settlement of the trust), the name and contact details of resident foreign trustees, and details of membership of trustees in approved professional organisations.

361 Anti-Money Laundering and Countering Financing of Terrorism (Definitions) Regulations 2011, reg 17.

362 *Fifth Issues Paper*, above n 350, at ch 9.

- of information that was collected and also on who was able to access this information once a trust is registered. But generally, registration would mean that more information would be available about the number of trusts in existence and how they are being used. Government agencies, beneficiaries and potential creditors would all be likely to gain some benefit from having information available about trust relationships.
- 18.24 However, as we explained in the *Preferred Approach Paper*, we did not consider the benefits of registration to be sufficient to warrant the introduction of a registration requirement for trusts. Our main reasons were that a register would significantly alter the nature of trusts by giving them a publicly registered status. We considered that this would be a significant shift away from the current treatment of most trusts as essentially private arrangements between citizens. We also questioned whether some of the “problems” identified by some people should truly be viewed as problems. Some of those calling for registration identify the private nature and confidentiality of trusts as a significant problem. However, privacy and confidentiality have historically been recognised as among the essential virtues of the trust form.
- 18.25 We also concluded that the overall costs associated with registration are a significant barrier. First, the costs of establishing and maintaining a register are likely to be substantial. Secondly, registration would impose compliance costs on all trusts, many of which are modest family trusts that could gain no benefits from registration. Unlike companies, which obtain corporate status and with it limited liability via the registration process, trusts would gain nothing through registration; they would only incur cost. The benefits obtained from a system of registration are of a public nature, taking the form of more accurate and better quality information that can be made available to (at least some) government agencies and possibly others. Thirdly, it would be difficult to enforce the registration of the hundreds of thousands of existing trusts without significant resources being expended.
- 18.26 Finally, we also made the point in the *Preferred Approach Paper* that registration is not the most appropriate way to improve accountability to beneficiaries. It is too blunt an instrument to use for that purpose. We recommend in chapter 5 of this Report that problems relating to proper trust record-keeping and accountability should be addressed by imposing enforceable record-keeping obligations on trustees. We also make recommendations in chapter 5 that have the effect of enhancing the rights of beneficiaries to access trust information. Our overall approach to addressing issues over the misuse or abuse of the trust form is to strengthen the traditional accountabilities within the trust relationship rather than to consider an overlay of regulation.
- 18.27 Most submissions received during the course of our review, on both the *Fifth Issues Paper* and on the *Preferred Approach Paper*, have firmly opposed the introduction of registration requirements for trusts. Most have cited one or more of the reasons we have already discussed. A few also stressed the potential risks posed by departing from historical and international norms relating to the private nature of trust arrangements, particularly to the foreign trust industry.

### **No registration recommendation**

- 18.28 Since issuing the *Preferred Approach Paper*, we have not been persuaded to alter our position or that we should recommend any other systems of registration for trusts. However, we received three significant submissions from government agencies in support of registration. We think that these warrant some further discussion.

*Inland Revenue – Registration of trading trusts*

- 18.29 Inland Revenue agreed that a compulsory registration system for all trusts may impose unnecessary additional compliance costs on trusts which do not receive any benefit from registration. However, in its submission on the *Preferred Approach Paper*, Inland Revenue restated the case for either a compulsory or voluntary register for trusts operating as businesses. It suggested that these could, for example, be defined as all trusts registered for Goods and Services Tax.
- 18.30 As discussed in the *Preferred Approach Paper*, Inland Revenue supports the introduction of some form of register.<sup>363</sup> It considers that the value of privacy in trusts needs to be balanced against the rights of creditors to know who they are dealing with in a commercial world. Its view was that, in an open market economy like New Zealand's, the default position should be transparency in relation to business or asset-holding entities, unless there is a good reason why this should not be the case. It submitted that compliance costs associated with registration could be reduced by utilising an existing register, such as the Companies Register. Although not suggested by Inland Revenue, another existing register administered by Inland Revenue might be a better option. As we discussed in the *Fifth Issues Paper*, a number of jurisdictions, including Canada and the United Kingdom, now register all trusts with their tax offices.<sup>364</sup>
- 18.31 We did, in the course of this review, consider both the options of a compulsory or a voluntary register of trusts engaged in business, as one of a suite of possible measures to address trusts that have a corporate trustee, in order to encourage disclosure of status as a trustee. We agree with the Inland Revenue that such a register has the advantage of not applying to most trusts, but of increasing the transparency of some business or estate-holding entities where this would be most useful.
- 18.32 We concluded that a voluntary register would only be effective if there were incentives for trustees to register information about the trust. If corporate trustees were required to disclose their status as trustees in some way, a voluntary register could provide a straightforward method for them to disclose. An incentive suggested by Inland Revenue was that registration could be deemed to provide evidence of the existence of a trust.
- 18.33 However, because we proposed an alternative method for corporate trustees to disclose their status as trustees in the *Preferred Approach Paper*, we did not consider it necessary to proceed further with consideration of a voluntary register.<sup>365</sup> For the reasons already outlined in chapter 16 of this Report, we have now resolved that all the proposals relating to corporate trustees we had included in the *Preferred Approach Paper* need further consideration. The Commission intends to look at these issues as part of the corporate trustee review of the project. As part of that fuller re-examination of measures relating to corporate trustees, we intend to consider all disclosure options, including registration, for corporate trustees. We will consider Inland Revenue's proposals as part of that process.

*Statistical information*

- 18.34 We received substantive submissions from Statistics New Zealand and the Reserve Bank of New Zealand in favour of registration. Although we have not been persuaded to change our position, we consider that these agencies raised an important argument for registration, based on the significance of the trust form to New Zealand at an economy-wide level.

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363 *Preferred Approach Paper*, above n 352, at [15.11].

364 *Fifth Issues Paper*, above n 350, at [9.21]–[9.30].

365 *Preferred Approach Paper*, above n 352, at P33.



- 18.35 Statistics New Zealand supported the establishment of a register of trusts because of its potential to improve the statistical information needed to inform key policy areas. Its submission highlights issues around the accuracy of data currently collected and available on trusts and the importance of accurate data for the national accounts, measurements of New Zealand's international investment position, and measurements of household savings and wealth used to support social, monetary and retirement policy. The Reserve Bank favoured the establishment of a register for trusts (even if it were a closed register rather than a searchable public one) for these same reasons and stressed the fundamental importance of accurate economic data.
- 18.36 Both agencies were concerned to have accurate information available on trusts from which they, and other public policy agencies, can make assessments at a macro-economic level for policy development. The Reserve Bank identified problems with having to rely solely (as it currently does) on data from the Household Saving Survey and the Annual Enterprise Survey. The Reserve Bank considered that data on the total assets and liabilities that trusts hold would be likely to improve national measures of wealth and saving. It stated that accurate economic information has always been important, but has become more significant in the wake of the global financial crisis.
- 18.37 The Reserve Bank argued that the need for adequate economic statistics was of itself sufficient to justify the establishment of a closed register for trusts. It suggested that the register should capture details of assets and liabilities of all trusts so the information can be used at an aggregate level but that information about individual trusts need not be made public. The Reserve Bank argued that even a register that shows only how many trusts exist would be valuable. The Reserve Bank could then survey samples to get reliable aggregated information on wealth and assets. The Reserve Bank suggested that the current requirement for income-earning trusts to register with Inland Revenue should be expanded to cover all trusts, whether income-earning or not, to create a simple register. Inland Revenue would keep and maintain the register as a closed register.
- 18.38 We are not convinced that the benefits of making better information at a macro-economic level available to government agencies are sufficient to justify the registration of all trusts and the consequential changes to the nature and use of trusts implicit in a registration system. There would need to be strong and compelling evidence that registration would truly generate substantially more accurate and reliable information than the methods currently used. We do not think that a simple registration scheme, of the type suggested in the Reserve Bank submission, could possibly generate the breadth of statistical information discussed.
- 18.39 A register may provide a more accurate picture of the total number of trusts, assuming all trusts are registered, but little more. Agencies might well be able to construct sample surveys from accessing the register, but unless participation was voluntary, such arrangements would add significant complexity to registration. In our view, a substantial amount of information would need to be obtained via registration, and regularly updated, for registration to be at all effective for the purposes these agencies have suggested.
- 18.40 Even if registration would net a substantial amount of robust and useful information for government agencies, that does not necessarily justify registration. In order to compile aggregated information on wealth and assets, the state would be collecting a significant amount of individualised data through registration. The fact that this would be useful to the Government is not of itself sufficient to justify the degree of intrusion into people's private arrangements implicit in registration. We do not consider that a case for registration on that basis has been justified.

# Chapter 19

## Relationship property and trusts

### INTRODUCTION

- 19.1 The *Preferred Approach Paper* included a chapter on sections 44 and 44C of the Property (Relationships) Act 1976 (PRA) and section 182 of the Family Proceedings Act 1980 (FPA).<sup>366</sup> These provisions apply to give relief to a disadvantaged spouse or partner on the breakdown of a relationship where property has been transferred to a trust. Submitters on the earlier *Second Issues Paper*<sup>367</sup> singled out sections 44 and 44C of the PRA as inadequate. Some argued that these sections do not go far enough to ensure a just division of assets produced or enhanced by a relationship.
- 19.2 Our overall approach to this review of the law of trusts has been to address matters of core trust law rather than problems that arise solely at the point where trust law interacts with other policy areas. However, we chose to include in the *Preferred Approach Paper* the proposal that section 182 of the FPA be amended to extend to de facto partners.<sup>368</sup> We also suggested, as an option for comment, that section 44C(2)(c) of the PRA could be amended to provide the court with broader compensation powers. While we were cautious about proposing changes to the PRA and FPA given the scope of our review, these two potential amendments were identified during the course of our work as reforms that would go some way to addressing identified concerns.

### SECTION 44C OF THE PROPERTY (RELATIONSHIPS) ACT 1976

#### RECOMMENDATION

R50 Section 44C(2)(c) of the Property (Relationships) Act 1976 should be amended to provide that the court may make an order requiring the trustees of the trust to pay to one spouse or partner a specified sum of money from the trust property or to transfer to one spouse or partner any property of the trust. A consequential amendment would need to be made to the wording in section 44C(3)(b)(i) to replace the reference in that subsection to “distribute the income of the trust” with something like “distribute a sum of money or property of the trust”. Section 44C should otherwise remain unchanged.

#### Current law and issues

- 19.3 Section 44C of the PRA makes provision for compensation where relationship property is disposed of to a trust. It provides:

#### **44C Compensation for property disposed of to trust**

- (1) This section applies if the court is satisfied—

<sup>366</sup> Law Commission *Review of the Law of Trusts – Preferred Approach* (NZLC IP31, 2012) at ch 17.

<sup>367</sup> Law Commission *Some Issues with the Use of Trusts in New Zealand: Review of the Law of Trusts – Second Issues Paper* (NZLC IP20, 2010).

<sup>368</sup> *Preferred Approach Paper*, above n 366, at P59.

- (a) that, since the marriage, the civil union, or the de facto relationship began, either or both spouses or partners have disposed of relationship property to a trust; and
  - (b) that the disposition has the effect of defeating the claim or rights of one of the spouses or partners; and
  - (c) that the disposition is not one to which section 44 applies.
- (2) If this section applies, the court may make 1 or more of the following orders for the purpose of compensating the spouse or partner whose claim or rights under this Act have been defeated by the disposition:
- (a) an order requiring one spouse or partner to pay to the other spouse or partner a sum of money, whether out of relationship property or separate property;
  - (b) an order requiring one spouse or partner to transfer to the other spouse or partner any property, whether the property is relationship property or separate property;
  - (c) an order requiring the trustees of the trust to pay to one spouse or partner the whole or part of the income of the trust, either for a specified period or until a specified amount has been paid.
- (3) The court must not make an order under subsection (2)(c) if—
- (a) an order under subsection (2)(a) or (b) would compensate the spouse or partner; or
  - (b) a third person has in good faith altered that person's position—
    - (i) in reliance on the ability of the trustees to distribute the income of the trust in terms of the instrument creating the trust; and
    - (ii) in such a way that it would be unjust to make the order.
- (4) The court may make 1 or more orders under subsection (2) if it considers it just to do so, having regard to—
- (a) the value of the relationship property disposed of to the trust;
  - (b) the value of the relationship property available for division;
  - (c) the date or dates on which relationship property was disposed of to the trust;
  - (d) whether the trust gave consideration for the property, and if so, the amount of the consideration;
  - (e) whether the spouses or partners, or either of them, or any child of the marriage, civil union, or de facto relationship, is or has been a beneficiary of the trust;
  - (f) any other relevant matter.

19.4 Section 44C was introduced into the PRA in 2002 to redress the detrimental effect trusts were having on property rights under that Act.<sup>369</sup> Earlier, the Ministerial Working Group on Matrimonial Property and Family Protection had concluded that the difficulty of proving intention to defeat under section 44 of the Act, and the increasing use of trusts, had placed large amounts of relationship property beyond the reach of the courts, often to the detriment of one of the spouses or partners.<sup>370</sup>

19.5 Section 44C provides that the court may order compensation where relationship property is transferred to a trust and the effect of that transfer is to defeat one of the party's rights, even though at the time of the transfer there was no intention to defeat those rights.<sup>371</sup> Section 44C can be contrasted with section 44, under which the court must determine the disposition was

<sup>369</sup> Section 44C was inserted by s 51 of the Property (Relationships) Amendment Act 2001 (2001 No 5).

<sup>370</sup> See Department of Justice *Report of the Working Group on Matrimonial Property and Family Protection* (October 1988) at 28–31 [*Matrimonial Property and Family Protection*].

<sup>371</sup> *Matrimonial Property Amendment Bill 1999* (109-2) (select committee report) at xii.

made “in order to defeat the claim or rights of any person” under the Act before it can set aside any disposition of property to a trust.<sup>372</sup>

- 19.6 Under section 44C(2), as currently drafted, the court may make an order:<sup>373</sup>
- (a) requiring one partner to pay the other a sum of money out of relationship property or separate property;
  - (b) requiring one partner to transfer to the other any relationship property or separate property; or
  - (c) requiring the trustees of the trust to pay one partner the whole or part of the income of the trust for a specified period or until a specified amount has been paid.
- 19.7 The court’s power to order the trustees to pay compensation is limited. Under section 44C(2)(c) it may order the trustees to pay the income (but not capital) of the trust to the defeated partner. It may only make such an order where there is insufficient relationship or separate property from which to otherwise compensate the defeated partner. Also, the court must not make any order against the trustees if this would prejudice beneficiaries of the trust who have altered their position in the bona fide belief that they could rely on the ability of the trustees to distribute the income from the trust.
- 19.8 The most problematic constraint imposed on the court is that the court has no power to require trustees to distribute capital or to withdraw assets from the trust. In its 1988 report the Working Group on Matrimonial Property and Family Protection recommended that the court’s power to award compensation from trust assets should be broader. The Working Group proposed that where the other partner’s share of relationship or separate property was insufficient to adequately compensate for the disposition, the court should have the power not only to divert income from the trust, but also to distribute capital from the trust and, as a last resort, to withdraw assets from the trust.<sup>374</sup>
- 19.9 Notwithstanding the Working Group proposal, the legislature determined that section 44C should only allow distributions of income and that the courts should not have the power to distribute capital or claw back assets. The reason given in the Select Committee report for limiting compensation to income was that trusts are created for legitimate reasons and so should be permitted to fulfil that purpose where there is no intention to defeat a relationship property claim at the time the trust was established.<sup>375</sup>

### Amendment proposed

- 19.10 One of the stated principles of our review is that individuals can utilise trusts to hold property as they wish. We recognise that there are legitimate reasons for establishing trusts and that consequently the courts should not interfere with trusts lightly. However, as provisions like sections 44 and 44C in the PRA and provisions for the protection of creditors in other legislative regimes demonstrate,<sup>376</sup> there are competing policy reasons that mean property held in trust is not absolutely protected.

372 Initially the courts interpreted s 44 narrowly; see *Coles v Coles* (1987) 3 FRNZ 101. However, following the Supreme Court decision in *Regal Castings Ltd v Lighbody* [2008] NZSC 87, [2009] 2 NZLR 433, which has been applied to s 44, the position is that if a person has knowledge that a consequence of the disposition of property will be to defeat the other person’s rights, then he or she is considered to have intended that consequence, even if it was not actually his or her wish to cause that loss.

373 Property (Relationships) Act 1976, s 44C(2).

374 See *Matrimonial Property and Family Protection*, above n 370, at 28–31.

375 Matrimonial Property Amendment Bill 1999 (109-2) (select committee report) at xii.

376 For example, Property Law Act 2007, ss 344–350 and Insolvency Act 2006, pt 3, sub-pt 7.

- 19.11 For a number of reasons, section 44C does not strike the right balance between the interests of a partner whose rights have been defeated by the transfer to the trust and those beneficially interested in the trust. The constraints on the compensation powers mean it is too easy for one partner to circumvent the PRA and place relationship property beyond the reach of the courts.
- 19.12 Our review of cases under the PRA revealed that there have been cases in recent years where section 44C applied but there was insufficient relationship or separate property outside the trust from which the court could adequately compensate the partner whose interests were defeated by the disposition of property to the trust.<sup>377</sup> In most cases the property in the trust did not produce income, which resulted in the current power the courts have to require the trustees to pay the income of the trust to the defeated partner almost never being used.<sup>378</sup>
- 19.13 In a few of the cases we reviewed, the defeated partner was able to successfully make an alternative application for relief under section 182 of the FPA.<sup>379</sup> However, in others the defeated partner was left with no redress under either section. In some of these cases the courts considered alternative arguments seeking to challenge the validity of the trust. As ways of dealing with the perceived injustice in some cases where the property has been placed beyond the reach of sections 44 and 44C, applicants have employed arguments questioning the validity of the trust, such as sham trusts, alter ego trusts, illusory trusts and the bundle of rights doctrine.<sup>380</sup> These theories often cannot get to the basic issue of restoring the effectiveness of the equal sharing of relationship property policy of the PRA, and risk distorting trust law.
- 19.14 The number of cases where section 44C provides no remedy due to insufficient relationship or separate property outside the trust from which to source compensation is likely to increase. In a portion of the cases we reviewed, the main relationship asset from which compensation was sourced was the debt back from the trust to the transferor following the disposition to the trust. The repeal of gift duty in 2011 has now largely removed the need for dispositions to trusts to be coupled with a debt back and a staggered programme of debt forgiveness. If there is no debt back, from which compensation might be sourced by the court, the result is likely to be more cases where the provision applies but no compensation is available.
- 19.15 Also, as noted, our review of cases revealed that it is rare for an order against trustees requiring the payment of income to be made. The circumstances in which this would be appropriate occur only occasionally in relationship property cases. Most of the trusts under consideration contain little more than residential properties, so do not generate income. The Commission has recommended in chapter 7 of this Report that the distinction between capital and income for the purposes of investment and distribution of trust funds be removed (see paragraphs [7.19] to [7.25]). Consequently, in future under the default provisions, trustees will determine what

<sup>377</sup> A search of Brookers Online Family Law and Trust Law databases identified cases that referred to s 44C over the last five years (1 February 2008 to 1 February 2013). A manual sifting exercise then identified all those cases where s 44C was discussed in the judgment. We then reviewed these cases to see what they might reveal about the application of s 44C. Where decisions had been appealed we reviewed the decision of the highest court.

<sup>378</sup> In the one case found where an order was made against trustees, the property was a family farm generating a monthly income; *DAM v PRM FC* Masterton FAM-2008-035-512, 30 March 2011.

<sup>379</sup> For example, in *Ward v Ward* [2009] NZSC 125, [2010] 2 NZLR 31 an application was made under s 44C. However, the matter was determined under s 182 of the FPA so no ruling was given on whether s 44C applied. Also in *INK v KAK (aka) W* [2012] NZFC 4435, [2012] NZFLR 880 a claim under s 44C was not pursued because counsel said there was no relationship property or other separate property from which compensation could be awarded if the claim was successful. An unsuccessful s 182 claim was pursued instead.

<sup>380</sup> For example, in *W v F* the Family Court Judge determined that the trust was a sham and the assets purportedly transferred into it were relationship property. As a result the alternative application under s 44C was not determined by the court. The Family Court's decision was overturned on appeal in *F v W* and the High Court remitted the case back to the Family Court; see *F v W* HC Wellington CIV-2009-485-531, 3 August 2009. In *Grant v Grant* the bundle of rights doctrine was applied and consequently the s 44C claim was not determined. The decision was appealed but the bundle of rights approach was not challenged in the High Court on appeal; *Grant v Grant* HC Auckland CIV-2010-404-5158, 31 March 2011. For a discussion on issues around sham trusts, alter ego trusts and the bundles of rights doctrine see Law Commission *Some Issues with the Use of Trusts in New Zealand: Review of the Law of Trusts – Second Issues Paper* (NZLC IP 20, 2010) at [4.33]–[4.43]; for the recent development of illusory trusts see the discussion in *Clayton v Clayton* [2013] NZHC 301.

returns are to be treated as capital and income for the purposes of distribution. Again, this is likely to make section 44C even less effective than it is now if it continues to restrict the courts' compensation powers to income.

#### *Orders against trustees under section 44C(2)(c)*

- 19.16 After much consideration, we recommend that section 44C(2)(c) be amended. Courts should have the power to make an order requiring the trustees to pay a specified sum or transfer property of the trust to compensate the partner whose rights were defeated by the disposition of relationship property to the trust. That power to order compensation should be restricted to the value of the relationship property that was transferred to the trust. A consequential amendment would need to be made to the wording in section 44C(3)(b)(i) replacing the reference to "income of the trust" with something like "money or property of the trust".
- 19.17 The recommended change would essentially give effect to the original proposal that was put forward by the 1988 Working Group to address dispositions to trusts. While it was important for Parliament to move cautiously in respect of the PRA's reach into trusts in 2002 when section 44C was enacted, subsequent cases have convinced us that the provision has been proved to be too easily circumvented.<sup>381</sup>

#### *Protections preserved*

- 19.18 Our recommended amendment does not change the requirements in section 44C(1) that define the scope of the section. The property disposed of to a trust must be relationship property at the time of disposition; it must have been transferred by one of the partners rather than by someone else; and the disposition must have the effect of defeating the claim or rights of one partner rather than affecting both partners equally.
- 19.19 Further, section 44C(3) contains important safeguards:
- the court must not make an order against the trustees under section 44C unless there is insufficient relationship or separate property from which to otherwise compensate the defeated partner for the disposition to the trust; and
  - the court must not make any order against the trustees if it would be unjust to do so because beneficiaries of the trust have, in good faith, altered their position in the belief that they could rely on the ability of the trustees to distribute funds.
- 19.20 Section 44C(4) also lists a number of relevant matters the court must have regard to when considering whether it would be just to make an order for compensation under section 44C(2). These factors, which the court must consider, include whether the trust gave consideration for the property, and if so, the amount of the consideration; whether one or both of the partners or any child of their relationship is or has been a beneficiary of the trust; and any other relevant matter.<sup>382</sup> Therefore, before making any order, the court must weigh the overall fairness of ordering compensation from the trust. In some cases such relevant matters have resulted in the court making no award of compensation or reducing the level of the award.<sup>383</sup>

381 The Select Committee report on the original Bill records that the New Zealand Law Society's view was s 44C did not go far enough and could be easily circumvented; see *Matrimonial Property Amendment Bill 1999 (109-2)* (select committee report) at xiii. The *Matrimonial Property Amendment Bill 1999* later became the *Property (Relationships) Amendment Act 2001*.

382 *Property (Relationships) Act 1976*, ss 44C(4)(d)–(f).

383 For example, in *Grigson v Walker* [2012] NZFC 5566 the party seeking compensation had remained living rent free in the trust property for five years after separation and had also retained the sole benefit of other items of relationship property. The court determined that it would not be just to order compensation to be paid in these circumstances.

19.21 There are, in our view, adequate protections in the section to ensure that recourse to the trustees for compensation will be the last option. Further, proper consideration will be given by the court to the interests of the beneficiaries. Before exercising its discretion the court must consider whether, in all the circumstances before the court, it is just to make orders against the trustees.

#### *Views of submitters*

19.22 As noted, submissions on the *Second Issues Paper* generally considered that the current provisions in the PRA should be strengthened because the court's ability to make orders in respect of property transferred to trusts in property relationship cases was too limited. However, only a few submitters responding to the *Preferred Approach Paper* supported amending section 44C in the way we are recommending. Most submitters did not support the proposal. Some considered that changes to the PRA should not be addressed within a review of core trust law. Some also considered that any recommendation would likely be controversial and that there are wider social questions over how far look-through provisions in the PRA should go.

19.23 Some submitters, and some commentators,<sup>384</sup> have expressed much more significant and substantive concerns over the approach we recommend. It has been argued by opponents that the proposed amendment undermines core principles of trust law. To allow the courts to make orders against the capital of the trust suggests that for relationship property purposes the trust can be disregarded. This means that dispositions of relationship property to a trust will be unreliable and vulnerable to recovery from the trust to satisfy a PRA claim. Submitters commented that not only does this defeat the interests of the beneficiaries, but it introduces a considerable amount of uncertainty into the operation of trusts because all of the assets of a trust can potentially be clawed back to compensate one of the partners under section 44C. Any disposition of property to a trust and all assets held in any trust to which qualifying dispositions are made would potentially be available as compensation.<sup>385</sup> This arguably prioritises the relationship partner's interests over those of the trust's beneficiaries and others such as creditors. It has also been argued that the amendment gives partners greater protection and better remedies in respect of trusts than creditors and taxpayers.<sup>386</sup>

19.24 We carefully weighed these points when developing the recommendation. We believe that such concerns should not be overstated. Although it is confined to income, conceptually section 44C(2)(c) already allows the court to claw back property (in the form of income) from the trust. The section already gives partners a degree of priority, at least in respect of income. Conceptually the recommended amendment is a change in the degree, although obviously a significant one, to which property of the trust would be vulnerable to a claim for compensation. It does not introduce the concept of claw-back into the section, because it is already there. Rather, it gives the court a more effective tool to use.

19.25 It should also be remembered that compensation from the trust must not exceed the value of the dispositions of relationship property (valued at the date of hearing) that have been made to the trust. Although all the assets of the trust are potentially available to compensate the defeated partner, other assets of the trust (over and above the value of the qualifying dispositions) are only at risk where the assets that made up the qualifying dispositions have been disposed of

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384 For example, Professor Nicola Peart has written about the problems she sees with the Commission's recommended approach in her paper "Protecting Children's Interests in Relationship Property Disputes on Separation" (paper presented to NZLS CLE Ltd Conference "The PRA in the GFC – uncertainty in uncertain times", Wellington, 22 February 2013).

385 At 31.

386 At 32.

by the trustees, or the value of those assets has decreased for some reason. Where relationship assets are transferred to trusts, trustees are on notice that a portion of the assets remains vulnerable to a claim for compensation.<sup>387</sup> They would be wise to plan accordingly.

- 19.26 Finally, as already noted, there are protections for beneficiaries. The court must not make an order where any third party has acted in good faith and altered their position in reliance and it would be unjust to make an order. Further, the court, when considering whether it would be just to make an order against the trustees for compensation, must consider all relevant factors. Consequently, the claim of a defeated spouse or partner to assets in the trust as compensation is not necessarily prioritised by the court over the interests of the trust's beneficiaries.
- 19.27 We believe that the courts are perfectly competent to exercise discretion in this area and to determine in any case, after taking account of relevant matters, whether or not it is just to make orders against trustees for compensation.

### Transitional matters

- 19.28 The transitional arrangements in respect of the amendment may in practice be significant so careful attention will need to be given to these when drafting a Bill.
- 19.29 The amendment to section 44C should apply to existing relationships covered by the PRA from the date of enactment.<sup>388</sup> We propose that, consistent with previous legislative amendment and case law, the amended section 44C should apply in all cases except where the hearing of proceedings has already commenced. When the Property (Relationships) Amendment Act 2001 came into force on 1 February 2002, its provisions (including section 44C) applied to all proceedings between married partners commenced after 1 February 2002, even if the marriage had ended before that date. Where proceedings had been commenced under the Matrimonial Property Act 1976 before 1 February 2002, but had not begun to be heard, then the new PRA provisions also applied.<sup>389</sup> However, where proceedings had been commenced before 1 February 2002 and had begun to be heard before that date, the PRA did not apply. In that case the proceedings were to be completed under the Matrimonial Property Act.
- 19.30 In the case of de facto partners, the PRA was applied from 1 February 2002 to de facto relationships whether they had begun before or after that date. However, the PRA does not apply to de facto relationships that ended before the 1 February 2002.<sup>390</sup> Unlike marriages, de facto relationships came under the Act for the first time on 1 February 2001.
- 19.31 Consistent with the approach taken with the 2001 Amendment Act, we consider that the amended section 44C should apply in all cases except where the hearing of proceedings has already commenced. The amended provision would apply to all proceedings commenced after it comes into force, regardless of whether the qualifying relationship ended before the provision came into force. It would also apply to proceedings commenced before the amendment came into force, provided they had not already begun to be heard. Where proceedings have begun to be heard, then they would be determined under the pre-amended version of section 44C. The transitional provisions should include a clear definition of when proceedings have begun to be determined so that there is no confusion.

387 This is, of course, already the case in relation to income under s 44C(2)(c) as it currently stands.

388 Part 3 of the PRA governs the application of the Act. But this must be read together with various transitional sections in pt 8 of the Act and the definitional sections in pt 1.

389 Part 3 of the PRA must be read together with various transitional sections in the Act to determine how s 44C of the PRA currently applies to marriages that predated the enactment of the Property (Relationships) Amendment Act 2001. Also carved out were proceedings commenced under the Matrimonial Property Act 1963 before 1 February 2002. Partners to civil unions later came under the Act on 26 April 2005 when the Civil Union Act 2004 came into force.

390 Property (Relationships) Act 1976, s 4C.



- 19.32 The one exception to this general approach would, of course, be that the PRA would continue not to apply to any de facto relationship that ended before 1 February 2002 because such relationships are not currently covered by the PRA.<sup>391</sup>
- 19.33 Consistent with the current provisions of the PRA, the application of the amended section 44C should apply to dispositions that occurred before it came into force. Section 44C, although introduced on 1 February 2002, was applied retrospectively by the 2001 Amendment Act to qualifying dispositions of relationship property made before that date. The amended section 44C would also apply retrospectively to dispositions that predate its coming into force, including those made before 1 February 2002. The alternative approach, which would be to apply the amended section only to future dispositions, would simply be too complex and confusing because the courts would apply one version of section 44C to dispositions before a certain date and another to subsequent transactions.

## SECTION 182 OF THE FAMILY PROCEEDINGS ACT 1980

### RECOMMENDATION

- R51 Section 182 of the Family Proceedings Act 1980, under which the courts may vary the terms of ante- and post-nuptial settlements, including trusts, when a marriage or civil union is dissolved, should be amended to also cover de facto relationships. The following changes should be made to the jurisdictional requirements of section 182:
- (a) the terms “de facto partner” and “de facto relationship” should have the same meaning as these terms have in sections 2C and 2D of the Property (Relationships) Act 1976;
  - (b) the triggering event that allows an application to be made to the court, or the court to make an order varying any qualifying settlement, should be changed from when a marriage or civil union is dissolved to when the parties to a relationship separate; and
  - (c) an application to the court should be able to be made in respect of relationship settlements rather than nuptial settlements. The term “relationship settlement” may need to be defined.

### Current law and issues

- 19.34 Under section 182 of the FPA the court may vary the terms of ante- and post-nuptial settlements, including trusts, when the marriage or civil union of the parties comes to an end. The section 182 jurisdiction is separate from the PRA rules and the concept of equal sharing in the PRA is not directly relevant to a determination under section 182. The Supreme Court in *Ward v Ward* made it clear that there is no entitlement to a 50/50 or any other fractional division of the trust property under section 182.<sup>392</sup> What is relevant, however, is that the nuptial settlement was premised on the continuation of the marriage.<sup>393</sup> Under section 182, the court must assess whether an order is necessary and, if so, in what terms, to reflect the fact that that fundamental premise (the continuation of the marriage) no longer applies.<sup>394</sup>

391 Property (Relationships) Act 1976, s 4C(2).

392 *Ward v Ward*, above n 379.

393 At [15].

394 At [62].

- 19.35 A “post-nuptial settlement” under section 182 clearly includes any trust established after a marriage if the trust is intended to provide for the couple (and their children). If, in light of all the circumstances, there is good reason to intervene, then the court is able to remove capital or assets from the trust, vary the terms of the trust, or resetttle the trust for the benefit of one or both parties to the marriage or civil union. The court may also make orders concerning administration and management of the trust.
- 19.36 Much has been written about section 182 and whether it is an anachronism overlooked when the PRA was enacted. As discussed, the PRA rules and the concept of equal sharing in the PRA are not directly relevant to a determination under section 182. Under section 182 the court seeks to give effect to the parties’ original expectations of the nuptial settlement in a logical and fair way where the parties’ circumstances have fundamentally changed.<sup>395</sup> It is sometimes suggested that this means section 182 is inconsistent with the principles in the PRA. However, the Supreme Court has noted there is no necessary inconsistency in allowing the courts to exercise a trust-varying power in the circumstances covered by section 182 while providing that, in the wider and distinct relationship property context, trusts will prevail over relationship property rights, subject to sections 44 and 44C.<sup>396</sup>
- 19.37 Whether or not section 182 was overlooked at the time the PRA was enacted, it provides an additional and alternative option in some circumstances for challenging the division of property following a relationship breakdown, where property has been settled on a trust as an ante- or post-nuptial settlement. It, however, applies only to married and civil union couples. It does not apply to de facto relationships so rather unfairly only provides a remedy for some couples and not for others. We consider that this inconsistency in the treatment of de facto couples is now an anomaly that should be addressed.

#### *Extend section 182 of the FPA to de facto partners*

- 19.38 We recommend amending section 182 of the FPA to apply also to ante-relationship and post-relationship trusts (and other settlements) established to benefit de facto partners as well as married and civil union partners. The recommendation would allow the court to vary the terms of any relevant ante-relationship and post-relationship settlement (including any trust) when a qualifying relationship between de facto partners as well as married or civil union partners ends. It should be noted that section 182 applies to all ante-nuptial and post-nuptial settlements, so the change applies to all such settlements and not just to trusts. The reform necessitates changing the triggering event for applications to separation rather than legal dissolution and a shift away from the language of “nuptial”.
- 19.39 The reform proposed does not alter the fundamentals of the provision or the test applied by the courts, but rather expands the class of potential applicants. Further, the basis on which the jurisdiction is exercised, as carried out in *Ward v Ward*,<sup>397</sup> seeks to perpetuate the objects of the settlement. This means that there is no departure from core trust principles.

#### *Submitters’ views*

- 19.40 Submissions responding to the *Preferred Approach Paper* were evenly divided over this proposal. Those opposed to the amendment argued that section 182 is an anachronistic anomaly that was overlooked by Parliament and is inconsistent with the PRA. Some said it should simply be repealed because the PRA was intended to be a comprehensive and complete set of rules to

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395 At [62].

396 At [19].

397 At [62].

determine status and division of property between qualifying couples, while others argued for a separate review of the PRA that could consider section 182 as well.

- 19.41 Those submitters who agreed that section 182 should be retained and extended to de facto couples said that, despite its history, it has become a useful provision that is utilised effectively by the courts to deal with situations not addressed by the PRA.<sup>398</sup> Some noted, as we have, that there is not necessarily any inconsistency between section 182 and the PRA. There was support for separation rather than dissolution being the end-of-relationship triggering event. In practice, waiting the two years for a formal dissolution delays the resolution of all property issues.
- 19.42 We have taken the various views of submitters into account. Our primary reason for recommending the amendment is that the current differing treatment of de facto relationships from married and civil union couples cannot be justified. This section continues to discriminate against some relationships when most other family law legislation does not. This anomaly should be removed.
- 19.43 The controversy and difference of opinion between submitters is over whether section 182 should be retained at all. For the reasons outlined, we recommend that it must be retained. It has become a useful provision that gives effect to the original intention of parties that settle trusts and deals with real injustice that would otherwise be caused by changed circumstances. While we do not consider that it is inconsistent with the PRA, consideration could be properly given, when drafting our proposed amendment to section 182, to whether the amended provision could reasonably be included in the PRA.<sup>399</sup>
- 19.44 Some consequential changes to the mechanics of section 182 are obviously needed to put de facto relationships, marriages and civil unions on an equal footing. There is no equivalent to “dissolution” at the end of a de facto relationship, nor is there the equivalent of a “nuptial” at the commencement. As already noted, we recommend that the court should be able to exercise its jurisdiction under the amended provision where the parties have separated and are living apart. This would essentially change the triggering event for the provision from dissolution to separation and bring it more into line with the PRA. Separation, rather than dissolution, is now widely accepted as the end of a marriage or civil union. The amendment would ensure that section 182 applications are not unduly delayed for all relationships. Another consequential amendment would be to change the language of “nuptial” settlements to “relationship” settlements. The approach taken in the PRA to defining a qualifying de facto relationship and to determining when separation occurs should also apply.

#### *Application to existing trusts*

- 19.45 We have reached the view that the amendment to section 182 should apply to de facto relationship settlements entered into before, as well as after, the amended provision comes into force. Despite reservations generally over retrospective application, because people have entered into existing arrangements based on the current law, we think that in this case the advantages of parties being able to apply for relief under section 182 outweigh those general concerns. At present the courts apply section 182 to give effect to the parties’ reasonable expectations of the relationship settlement when it was made. If the provision applies retrospectively to de facto couples then they are given the opportunity to apply under the section to the court to give effect to their expectations of their relationship settlements. It is more likely that their expectations will be able to be realised. If they are not able to apply under section 182 then an arrangement

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<sup>398</sup> See Peart “Protecting Children’s Interests in Relationship Property Disputes on Separation”, above n 384, at 29.

<sup>399</sup> Although it may make sense to move s 182 into the PRA, the section has an effect on maintenance agreements in certain contexts, so the implications of that would need to also be worked through before that step could be properly taken.

that no longer meets the parties' expectations of that arrangement will continue unchanged. We think that retrospective application is likely to largely be of benefit. It provides a mechanism for remedying a situation where there currently is no remedy. An important consideration here also, is that the court has a wide discretion when dealing with a settlement under section 182. The court must consider the interests of other beneficiaries of the trust.

- 19.46 Another factor in favour of the provision applying to existing settlements is that the PRA already applies retrospectively. We think that it would be better for section 182 also to do so. While section 182 and the PRA serve different purposes, they are both concerned with resolving property disputes when a relationship ends. It would seem desirable for a consistent approach to be taken and this will mean that in some cases the parties will have the alternative option of applying under section 182.

# Appendices



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# Appendix A

## Indicative draft provisions

### Trusts Bill

#### Part 1

##### *Preliminary provisions*

#### 1 Interpretation

- (1) In this Act, unless the context otherwise requires,—
- beneficiary** means a person who receives, or who will or may receive, a benefit under the terms of a trust; and includes a discretionary beneficiary; and may include a settlor or trustee if the settlor or trustee is included as a beneficiary under the terms of the trust
- discretionary beneficiary** means a person who may benefit under an express trust at the discretion of the trustee or under a power of appointment but who does not have a fixed, vested, or contingent interest in the trust property
- express trust** has the meaning given to it in **section 3**
- permitted purpose** means a charitable purpose and any other purpose for a trust that is permitted in law
- settlor** means a person who settles property on a trust, or transfers value to a trust or for the benefit of a trust on terms of trust; and includes a person who creates an express trust under a will to take effect after his or her death
- terms of the trust**—
- (a) means the terms on which the trust property is settled; and
- (b) includes any valid variations or amendments
- trust property** means any form of property that is settled on the trustees in accordance with the terms of the trust, and includes property derived from or accruing to the trust property (for example, income received)
- trustee** means a person who holds property under a trust.
- (2) In this Act, unless the context otherwise requires, a reference to a trust is a reference to an express trust.
- (3) Nothing in this Act prevents a court, in interpreting the provisions of this Act, from having recourse to the general law of trusts and equity where that law is consistent with this Act.

#### 2 Act applies to express trusts

- (1) This Act applies to express trusts.
- (2) However, in a particular case relating to a resulting trust or a constructive trust, a court may make orders applying so much of the Act to the trust as it thinks appropriate.

##### Subpart 1 — Express trusts

#### 3 Meaning of express trust

For the purposes of this Act, an **express trust** means a trust that—

- (a) has the characteristics set out in **section 4**; and
- (b) is created in accordance with **section 5**.

#### 4 Essential characteristics of express trust

- (1) The characteristics of an express trust are:
- (a) it is a legal relationship in which a trustee holds or deals with trust property in 1 or both of the following cases:

- (i) trust property held or dealt with on behalf of the beneficiaries (where a trust has beneficiaries);
- (ii) trust property held or dealt with for the purpose of the trust (where a trust is for a permitted purpose); and
- (b) the trustee is under a fiduciary obligation to deal with the trust property for—
  - (i) the benefit of the beneficiaries (where a trust has beneficiaries); or
  - (ii) the purpose of the trust (where a trust is for a permitted purpose); or
  - (iii) the benefit of the beneficiaries and the purpose of the trust; and
- (c) if the trustee's duties are enforceable, they may be enforced against the trustee by—
  - (i) any 1 or more of the beneficiaries where a trust has beneficiaries; or
  - (ii) the Attorney-General where the trust is a charitable trust; and
- (d) as a consequence of **paragraphs (a) to (c)**, the beneficiaries have equitable rights in or in respect of the trust property.
- (2) An express trust must not have the sole trustee as the sole beneficiary of the trust.

#### **5 Creation of express trust**

An express trust is created,—

- (a) subject to any formalities prescribed by a statute, by the settlor who, with reasonable certainty and by words or actions,—
  - (i) indicates an intention to create a trust; and
  - (ii) identifies the beneficiaries or the trust purpose; and
  - (iii) identifies the trust property; or
- (b) if a statute provides for the creation of an express trust, in accordance with that statute.

#### **6 No express trust except under section 5**

- (1) A trust, if it is to be an express trust, must be created in accordance with **section 5**.
- (2) Nothing in **subsection (1)** precludes the invalidity of an express trust on any other ground recognised at law.

### Subpart 2 — Duties of trustee

#### *General*

#### **7 Types of trustee's duties**

A trustee has—

- (a) mandatory duties (*see* **sections 9 and 10**); and
- (b) default duties (*see* **sections 11 to 23**).

#### **8 No requirement that beneficiaries be treated equally**

- (1) The exercise of a trustee's duty does not require that all beneficiaries are treated equally, provided that beneficiaries are treated in accordance with the terms of the trust.
- (2) Nothing in **subsection (1)** derogates from **section 18**.

*Mandatory duties***9 What is trustee's mandatory duty**

A trustee's mandatory duty is a duty that—

- (a) the trustee must perform; and
- (b) may not be excluded or diminished; and
- (c) applies regardless of anything that may be contained in the terms of the trust.

**10 Mandatory duties**

The trustee of a trust is under the following mandatory duties:

- (a) a trustee must be familiar with the terms of the trust; and
- (b) a trustee must act in accordance with the terms of the trust; and
- (c) a trustee must act honestly and in good faith; and
- (d) a trustee must, in accordance with the terms of the trust, act for the benefit of the beneficiaries or for the purpose of the trust; and
- (e) a trustee must exercise stewardship over the trust property for the beneficiaries or the purpose of the trust; and
- (f) a trustee must exercise the powers of a trustee for a proper purpose.

*Default duties***11 What is trustee's default duty**

- (1) A trustee's default duty is a duty that the trustee must perform unless it is modified or excluded by the terms of the trust or the statute under which the trust is created.
- (2) A trustee's default duty may only be modified or excluded to the extent that is consistent with the mandatory duties.
- (3) However, a trustee may depart from the default duties under **sections 19** (duty not to profit) and **20** (duty to act without reward) if all the adult beneficiaries agree.
- (4) In **subsection (3)**, **adult beneficiaries** means the beneficiaries with full legal capacity who are together absolutely entitled to the trust property.

**12 Default duties**

The default duties of a trustee are set out in **sections 13 to 23**.

**13 Duty not to exercise power for own benefit**

A trustee must not exercise a power of a trustee directly or indirectly for the trustee's own benefit.

**14 Duty to consider exercise of power**

A trustee must actively and regularly consider whether the trustee should be exercising 1 or more of the trustee's powers.

**15 Duty not to fetter future exercise of powers**

A trustee must not fetter the future exercise of the trustee's powers.

**16 Duty to avoid conflict of interest**

A trustee must avoid a position where the interests of the trustee and the interests of the beneficiaries conflict.

**17 Duty to keep proper accounts**

A trustee must maintain a statement of the trust property that—



- (a) adequately identifies the assets, liabilities, and income and expenses of the trust; and
- (b) is appropriate to the value and complexity of that property.

**18 Duty of impartiality**

A trustee must not be unfairly partial to 1 beneficiary or group of beneficiaries to the detriment of the others.

**19 Duty not to profit**

A trustee must not make a profit from the trusteeship of the trust.

**20 Duty to act without reward**

A trustee must not take any reward for acting as a trustee, but this does not affect the right of a trustee to be reimbursed for the trustee's legitimate expenses and disbursements in acting as a trustee.

**21 Duty to act unanimously**

If there is more than 1 trustee, the trustees must act unanimously.

**22 Duty to exercise care and skill in management and administration of trust property**

- (1) A trustee who exercises any power of management or administration of the trust property must do so in accordance with the standard of care set out in **section 25**.
- (2) In **subsection (1)**, a power of management or administration of the trust property—
  - (a) includes a power, whether created by law or by the terms of the trust, to—
    - (i) hold trust property; and
    - (ii) maintain and develop trust property; and
    - (iii) deal with trust property; and
    - (iv) insure trust property; and
    - (v) carry on a business that is trust property; and
    - (vi) appoint an agent, nominee or custodian; and
    - (vii) appoint a delegate; and
    - (viii) any other power affecting the management or administration of trust property; but
  - (b) does not include the exercise of a discretion to distribute trust property to beneficiaries.

**23 Duty to invest prudently**

- (1) When investing trust property, a trustee must invest prudently.
- (2) For the purposes of **subsection (1)**, a trustee invests prudently if the trustee complies with the standard of care set out in **section 26**.

Subpart 3 — Trustee's standard of care

**24 Types of standard of care**

This subpart sets out the standard of care—

- (a) for the exercise of a power of management or administration of trust property (*see* **section 22**); and
- (b) for investment of trust property by a trustee (*see* **section 23**).

**25 Standard of care for exercise of power of management or administration of trust property**

In the exercise of a power set out in **section 22(2)**, a trustee must exercise the care and skill that are reasonable in the circumstances, having regard in particular—

- (a) to any special knowledge or experience that the trustee has or holds the trustee out as having; and
- (b) if a person acts as a trustee in the course of a business or profession, to any special knowledge or experience that it is reasonable to expect of a person acting in the course of that business or profession.

**26 Standard of care for power of investment**

In the exercise of a power of investment, a trustee must exercise the care and skill that a prudent businessperson would exercise in managing the affairs of others, having regard in particular—

- (a) to any special knowledge or experience that the trustee has or holds the trustee out as having; and
- (b) if a person acts as a trustee in the course of a business or profession, to any special knowledge or experience that it is reasonable to expect of a person acting in the course of that business or profession.

Subpart 4 — Trustee exemption clauses and indemnity clauses

**27 Restriction on trustee exemption clauses**

The terms of a trust must not limit or exclude a trustee's liability for any breach of trust arising from the trustee's own dishonesty, wilful misconduct, or gross negligence.

**28 Restriction on trustee indemnity clauses**

The terms of a trust must not grant the trustee any indemnity against the trust property in respect of liability for any breach of trust arising from the trustee's own dishonesty, wilful misconduct, or gross negligence.

**29 Indemnification with agreement of beneficiaries**

- (1) A trustee may be indemnified from the trust fund for a specific exercise or non-exercise of a trustee duty, power, or function if all the adult beneficiaries agree.
- (2) In **subsection (1)**, **adult beneficiaries** means the beneficiaries with full legal capacity who are together absolutely entitled to the trust property.

**30 Invalidity of restricted exemption clause or indemnity clause**

A clause of the terms of a trust is invalid to the extent that it purports to have the effect stated in **section 27** or **28**.

**31 Adviser must alert settlor to liability exclusion or indemnity clause**

- (1) This section applies where a person who is paid to advise on the terms of a trust or the drafting of a trust deed (the **adviser**) recommends the inclusion of, or includes, a liability exclusion or indemnity clause in the terms of the trust.

- (2) The adviser must, before the creation of the trust, take reasonable steps to ensure that the effective settlor is aware of the meaning and effect of the clause.
- (3) The liability exclusion or indemnity clause has no effect with respect to an adviser who is a trustee of the trust and who is in breach of **subsection (2)**.
- (4) In this section, **liability exclusion or indemnity clause** means a clause that has the effect of—
  - (a) limiting or excluding the liability of a trustee for negligence; or
  - (b) granting a trustee an indemnity against the trust property in respect of liability for negligence.

*Relief of personal liability*

**32 Court may relieve trustee from personal liability**

- (1) If **subsection (2)** applies, the court may relieve a trustee who is or may be personally liable for any breach of trust from personal liability for the breach.
- (2) The court may relieve the trustee if it appears to the court that—
  - (a) the trustee has acted honestly and reasonably; and
  - (b) the trustee ought fairly to be excused for the breach of trust.
- (3) The court may relieve the trustee in whole or in part.

Subpart 5 — Trustees' obligations in relation to information

*Retention of documents by trustees*

**33 Trustee must retain core documents**

Each trustee of a trust must retain, so far as is reasonable, copies of the following documents relating to the trust:

- (a) the trust deed; and
- (b) any variations made to the trust deed or trust, including variations made to the beneficiaries of the trust; and
- (c) a list of all of the assets currently held as trust property and liabilities of the trust; and
- (d) any records of trustee resolutions made during that trustee's trusteeship; and
- (e) any written contracts entered into during that trustee's trusteeship; and
- (f) any accounting records and financial statements prepared during that trustee's trusteeship; and
- (g) deeds of appointment and retirement of trustees; and
- (h) any letter or memorandum of wishes from the settlor or settlors; and
- (i) any documents referred to in paragraphs (a) to (h) that were retained by a former trustee during that person's trusteeship and passed on to the current trustee.

**34 Retention of documents where there is more than 1 trustee**

If there is more than 1 trustee of a trust, a trustee complies with the obligation in **section 33** if—

- (a) every trustee holds copies of the documents in **section 33(a)** and **(b)**; and

- (b) one of the trustees holds copies of the other documents in **section 33** and makes those documents available to the other trustees on request.

**35 Duration of retention of documents**

A trustee must retain, so far as is reasonable, the documents for the duration of the trustee's trusteeship.

**36 Trustee must pass on documents**

At the time that a trustee ceases to be a trustee of a trust, if the trust continues, the trustee must give at least 1 replacement trustee or continuing trustee the documents that the trustee holds at that time.

**37 Record-keeping requirements under other legislation**

Nothing in this Act affects the obligations of a trustee to keep records under other legislation.

*Provision of information to beneficiaries: general obligation*

**38 Trustee must provide sufficient information**

A trustee must provide sufficient information to sufficient beneficiaries to enable the terms of the trust to be enforced against the trustees.

*Provision of information to beneficiaries: specific obligations*

**39 Definitions for purposes of sections 40 to 44**

In **sections 40 to 44**,—

**qualifying beneficiary** means a beneficiary whom the settlor intended to have a realistic possibility of receiving trust property under the terms of the trust

**representative** means the parent, guardian, or property manager of a beneficiary who is a minor or in respect of whom a guardian or property manager has been appointed

**trust information**—

- (a) means any information—
- (i) regarding the terms of the trust, the administration of the trust, or the trust property; and
  - (ii) that it is reasonably necessary for the beneficiary to have in order for the trust to be enforced; but
- (b) does not include reasons for trustees' decisions.

**40 Presumption that trustee must notify basic trust information**

- (1) There is a presumption that a trustee must, as soon as is practicable, provide every qualifying beneficiary or representative of a minor or incapable qualifying beneficiary with the information set out in **subsection (3)**.
- (2) However, the presumption does not apply if the trustee reasonably considers that the information should not be provided (to be determined by consideration of the factors set out in **section 42(2)**).
- (3) The information referred to in **subsection (1)** is—
  - (a) the fact that a person is a beneficiary of the trust in question; and
  - (b) the names and contact details of the trustees; and
  - (c) the right of the beneficiary to request a copy of the trust deed or trust information.

**41 Presumption that trustee must provide information on request**

- (1) There is a presumption that a trustee must within a reasonable period of time provide a beneficiary with the trust information that the beneficiary has requested.
- (2) However, the presumption does not apply if the trustee reasonably considers that the information should be withheld (to be determined by consideration of the factors set out in **section 42(2)**).

**42 Procedure for deciding against provision of information**

- (1) For the purposes of **sections 40** and **41**, a trustee must not decide against providing information unless the trustee has taken into account—
  - (a) the trustee's obligation under **section 38**; and
  - (b) the factors set out in **subsection (2)**.
- (2) The factors referred to in **subsection (1)(b)** are the following:
  - (a) the nature of the interests held by the beneficiary and the other beneficiaries of the trust, including the degree and extent of the beneficiary's interest in the trust or the beneficiary's likely prospects of receiving trust property in the future;
  - (b) whether the information is subject to personal or commercial confidentiality;
  - (c) the expectations and intentions of the settlor at the time of the creation of the trust as to whether the beneficiaries as a whole and the qualifying beneficiary in particular would be provided with information;
  - (d) the age and other circumstances of the beneficiary;
  - (e) the age and circumstances of the other beneficiaries of the trust;
  - (f) the effect of providing the information on the trustees, other beneficiaries of the trust, and third parties;
  - (g) in the case of a trust that is a family trust, the effect of providing the information on—
    - (i) relationships within the family;
    - (ii) the relationship between the trustees and some or all of the beneficiaries to the detriment of the beneficiaries as a whole;
  - (h) in a trust where there is a large number of beneficiaries or there are unascertainable beneficiaries, the practicality of providing information to all beneficiaries or all members of a class of beneficiaries:
    - (i) the practicality of providing some or all of the information to the beneficiary in redacted form;
    - (j) the practicality of imposing restrictions and other safeguards on the use of the information (for example, by way of an undertaking, or restricting who may inspect the documents).

**43 Beneficiary may be required to pay cost of providing information**

The trustee may require the beneficiary to whom trust information is provided under **section 41** or in accordance with the terms of the trust to pay the reasonable cost of providing that information.

**44 Application to court**

- (1) The trustee may apply to the court for directions before deciding against providing the information under **section 40** or **41**.

- (2) A beneficiary may apply to the court for an order that the trustee supply the beneficiary with the information the beneficiary has requested.

## Part 2

### Trustee's indemnity

#### 45 Trustee is personally liable for expenses and liabilities

A trustee is personally liable for an expense or a liability incurred by the trustee when acting as a trustee.

#### 46 Trustee's right to indemnity

- (1) A trustee who reasonably incurs an expense or a liability when acting on behalf of the trust is entitled to—
- (a) the payment or discharge of the expense or liability out of the trustee's own funds and reimbursement from the trust property; or
  - (b) the payment or discharge of the expense or liability from the trust property.
- (2) **Subsection (1)** applies regardless of any contrary intention expressed in the terms of the trust.
- (3) **Subsection (1)** applies to a former trustee in relation to an expense or a liability incurred as a trustee acting on behalf of the trust.

#### 47 Ranking of trust property

- (1) For the purposes of **section 46(1)**, the terms of the trust may rank the order in which the trust property must be applied to reimburse the trustee or pay or discharge an expense or a liability.
- (2) However, the court may set aside a ranking of trust property under **subsection (1)** on the application of—
- (a) the trustee; or
  - (b) a creditor; or
  - (c) a beneficiary.

#### 48 Creditor's limited claim to trust property through trustee's indemnity

- (1) This section applies where—
- (a) a trustee has incurred an expense or a liability to a creditor; and
  - (b) the creditor has given value; and
  - (c) the trust property has received a benefit from the transaction between the trustee and the creditor; and
  - (d) the creditor has acted in good faith.
- (2) In a case to which this section applies, the creditor may claim to be indemnified out of the trust property as if the creditor were a trustee, notwithstanding that the trustee for any reason is not entitled to be fully indemnified.
- (3) The creditor has not acted in good faith if the creditor had knowledge of any circumstances that excluded or limited the trustee's indemnity.
- (4) A claim under this section—
- (a) is limited to the value given by the creditor; and
  - (b) must be paid in priority over any payment to a beneficiary, unless the court orders otherwise.

## Part 3 Supervision of trustees

### *Court's review power*

**49 Court may review trustee's act, omission, or decision**

- (1) The court may review an act, omission, or decision (including a proposed act, omission, or decision) of a trustee of an express trust on the ground that the act, omission, or decision was or is not reasonably open to the trustee in the circumstances.
- (2) The court may review an act, omission, or decision under **subsection (1)** on the application only of—
  - (a) a beneficiary; or
  - (b) if a beneficiary does not have full legal capacity, his or her personal representative.
- (3) The review must be conducted in accordance with **section 50**.

**50 Procedure for trustee review**

- (1) An applicant for review under **section 49** must adduce evidence that raises a genuine and substantial dispute as to whether the act, omission, or decision in question was or is reasonably open to the trustee in the circumstances.
- (2) If the court is satisfied that the applicant has established a genuine and substantial dispute, the court must allow the trustee the opportunity, and may require the trustee, to appear before it to adduce evidence establishing that the act, omission, or decision was or is reasonably open to the trustee in the circumstances.
- (3) If the court, after hearing the trustee, is satisfied on a balance of probabilities that the act, omission, or decision was or is not reasonably open to the trustee in the circumstances, the court may (but subject to **subsection (4)**)—
  - (a) set aside the act or decision or direct the trustee to act in the case of an omission;
  - (b) restrain the trustee from acting or deciding in the case of a proposed act or decision, and direct the trustee to act in the case of a proposed omission;
  - (c) make such other orders as the court considers necessary.
- (4) The court must not make an order that affects—
  - (a) a distribution of the trust property that has been made not in breach of trust and before the trustee had notice of the application; or
  - (b) any right or title acquired by a person in good faith and for value.

## Part 4 Administration of trusts

### Subpart 1—Revocation and variation of trusts

**51 Revocation by unanimous consent of beneficiaries**

- (1) The trustees of a trust must terminate the trust and distribute the trust property on being required to do so by the beneficiaries if the conditions set out in **subsection (2)** are satisfied.
- (2) The conditions for the termination of the trust under **subsection (1)** are as follows:
  - (a) the trustees have received a written notice requiring the trustees to terminate the trust; and

- (b) the notice is signed by each beneficiary or by the duly authorised agent of that beneficiary; and
  - (c) each beneficiary is, at the date of receipt of the notice, 18 years of age or older and otherwise a person of full legal capacity.
- (3) The conditions in **subsection (2)** are treated as satisfied in respect of a person on whose behalf the court has made an order of approval under **section 54** or an order of waiver of consent under **section 55**.

## **52 Other actions with unanimous consent of beneficiaries**

- (1) The beneficiaries of a trust acting unanimously may do any of the following things, if the conditions set out in **subsection (2)** are satisfied:
- (a) confer new powers upon the trustees;
  - (b) vary the terms of the trust;
  - (c) deviate from the terms of the trust;
  - (d) consent to the resettlement of the trust.
- (2) The conditions for an action by the beneficiaries under **subsection (1)** are:
- (a) the trustees have received a written notice of the proposed new powers, variation, deviation, or resettlement, as the case may be; and
  - (b) the notice is signed by each beneficiary or by the duly authorised agent of that beneficiary; and
  - (c) each beneficiary is 18 years of age or older and otherwise a person of full legal capacity; and
  - (d) the trustees have agreed to the proposal.
- (3) The conditions in **subsection (2)** are treated as satisfied in respect of a person on whose behalf the court has made an order of approval under **section 54** or an order of waiver of consent under **section 55**.

## **53 Beneficiary's right to share of trust property**

A beneficiary of a fixed share of the trust property may require the trustees to transfer that share to the beneficiary (and the trustees must do so) if—

- (a) the beneficiary is absolutely entitled to that share (for example, any condition relating to the vesting of that share set by the terms of the trust has been met); and
- (b) the property is in a form, or can be changed into a form, that can be transferred to the beneficiary; and
- (c) the transfer is not detrimental to the interests of the other beneficiaries; and
- (d) the beneficiary is 18 years of age or older and otherwise a person of full legal capacity.

## **54 Power of court to approve revocation, variation, or resettlement of trust**

- (1) The court may, on behalf of any of the persons set out in **subsection (2)** who has an interest in property held under a trust, approve the revocation, variation, or resettlement of the trust.
- (2) The persons referred to in **subsection (1)** are as follows:
- (a) a person under the age of 18 years;
  - (b) a person who lacks full legal capacity;



- (c) a person who may acquire an interest at a future date or on the happening of a future event or on becoming a member of a certain class of persons:
- (d) a future person.
- (3) On an application for an order of approval under **subsection (1)**, the court—
  - (a) must take into account the following factors:
    - (i) the nature of any person’s interest in the trust property and the effect of the proposed order on that interest; and
    - (ii) the benefit or detriment that may result from the proposed order to any person having an interest in the trust property; and
    - (iii) the benefit or detriment that may result to any person having an interest in the trust property if the court refuses to make the proposed order; and
    - (iv) the intentions of the settlor of the trust in settling the trust property, if it is practicable to ascertain those intentions; and
  - (b) must not make an order of approval if its effect would be to reduce or remove any vested interest in the trust property or other property right held by a beneficiary.
- (4) An order of approval under **subsection (1)** binds the person on whose behalf it is made and takes effect without any further step.
- (5) In this section, **interest** includes—
  - (a) a direct or an indirect interest:
  - (b) a contingent interest.

**55 Power of court to waive requirement of consent to revocation, variation, or resettlement of trust**

- (1) The court may waive the requirement that the consent of a person be obtained for the revocation, variation, or resettlement of a trust.
- (2) On an application for an order of waiver of consent under **subsection (1)**, the court—
  - (a) must take into account the following factors:
    - (i) the nature of any person’s interest in the trust property and the effect of the proposed order on that interest; and
    - (ii) the benefit or detriment that may result from the proposed order to any person having an interest in the trust property; and
    - (iii) the benefit or detriment that may result to any person having an interest in the trust property if the court refuses to make the proposed order; and
    - (iv) the intentions of the settlor of the trust in settling the trust property, if it is practicable to ascertain those intentions; and
  - (b) must not make an order of waiver of consent if its effect would be to reduce or remove any vested interest in the trust property or other property right held by a beneficiary.
- (3) An order of waiver of consent under **subsection (1)** binds the person on whose behalf it is made and takes effect without any further step.
- (4) In this section, **interest** includes—
  - (a) a direct or an indirect interest:
  - (b) a contingent interest.

**56 Power of court to vary or extend trustees' powers in relation to property**

- (1) The court may vary or extend the powers of the trustees of a trust in relation to property transactions if—
  - (a) the court considers that the variation or extension is necessary for the proper management of the trust property; and
  - (b) the variation or extension does not alter or otherwise affect a beneficiary's interest under the trust.
- (2) An application for an order under **subsection (1)** may be made by—
  - (a) the trustees or any 1 of them;
  - (b) any person beneficially interested under the trust.
- (3) In this section, **property transaction**, in relation to trust property, means the acquisition of, disposition of, or other dealing with trust property and includes sale, lease, mortgage, surrender, release, purchase, investment, retention, and expenditure.

# Appendix B

## List of submitters

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### **Introductory Issues Paper**

- Auckland Energy Consumer Trust
- Ayers Legal
- Tobias Barkley
- Chapman Tripp
- Justice John Fogarty and Geeti Faramarzi
- Gorden Goodall
- Guardian Trust
- Grace Haden, Verisure Investigations Ltd
- Hutt Valley Community Law Centre
- KPMG
- Ministry of Economic Development
- New Zealand Law Society
- New Zealand Trustee Services
- Stace Hammond
- Taylor Grant Tesiram
- Jill Thompson
- Trustee Corporations Association
- Trustee Executors Ltd

### **Second Issues Paper**

- Auckland District Law Society
- Ayers Legal
- Tobias Barkley
- Cash Flow Doctors Ltd
- Chapman Tripp
- Jennifer Dalziel, Chartered Accountant
- Ernst & Young
- Peter Kellaway, Kellaways Lawyers
- KPMG
- Lawler & Co

- John McIlwaine
- Ministry of Economic Development
- Ministry of Social Development
- Grant Nelson, The Gama Foundation
- New Zealand Law Society
- Martin Riley, Stirling Tax Services
- Alan Tate, Harris Tate
- Taylor Grant Tesiram
- Gary Thomas, Ryan Thomas and Co
- John Tripe, Jack Riddet Tripe
- Trustee Corporations Association
- Ivan Turk
- Veda Advantage
- Julie Walker
- WHK

### **Third Issues Paper**

- Auckland District Law Society
- Auckland Energy Consumer Trust
- Ayers Legal
- Capital Trust Management
- Chapman Tripp
- Chris Kelly, Greg Kelly Law
- Ministry of Social Development
- New Zealand Law Society
- Perpetual Trust
- Russell McVeagh
- Tauranga Energy Consumer Trust
- Taylor Grant Tesiram
- Trustee Corporations Association

### **Fourth Issues Paper**

- Anchor Trustees
- Auckland District Law Society
- Auckland Energy Consumer Trust
- Phillip Bartlett, Bartlett Partners

- Chapman Tripp
- Charities Commission
- Samuel Chatwin
- Cone Marshall Ltd
- Grace Haden, Verisure Investigations Ltd
- Chris Kelly, Greg Kelly Law
- KPMG
- Garth Lucas, Lucas and Lucas Ltd
- Māori Land Court
- Liam McNeely
- Ministry of Social Development
- National Council of Women
- New Zealand Law Society
- Simon Scannell, SJ Scannell and Co
- Society of Trust and Estate Practitioners New Zealand
- Taylor Grant Tesiram
- Tripe Matthews and Feist
- Trustee Corporations Association

#### **Fifth Issues Paper**

- Auckland Energy Consumer Trust
- Chapman Tripp
- Energy Trusts of New Zealand
- Ernst & Young
- Justice John Fogarty
- Greg Kelly Law
- Dirk Hudig
- Inland Revenue
- Jeff Kenny
- KPMG
- Ministry of Economic Development
- Ministry of Social Development
- New Zealand Law Society
- New Zealand Trustees Association
- Perpetual Trust
- Susan Robson

- Taylor Grant Tesiram
- Trustee Corporations Association
- And one submitter who wishes to remain anonymous

### **Preferred Approach Paper**

- Allen, Needham & Co Ltd
- Amicorp NZ Ltd
- Anchor Trustees
- Asiaciti Trust
- Auckland District Law Society
- Auckland Energy Consumer Trust
- Ayers Legal
- Anne Stewart Ball
- Tobias Barkley
- Timothy Bell
- John Brown
- Chapman Tripp (3 submissions)
- Samuel Chatwin
- Elizabeth Cotton
- Counties Power Consumer Trust
- Daniel Overton & Goulding
- DLA Phillips Fox
- Donnell & Associates
- Eastern Bay Energy Trust
- Electra Trust
- Energy Trusts of New Zealand Inc
- Andrew Fraser
- Dennis Friis
- Damien Grant
- Grace Haden
- Graham Halstead
- Hawke's Bay Power Consumers' Trust
- Miles Hayward-Ryan
- David Hillary
- Dirk Hudig
- Inland Revenue

- Jeff Kenny
- Kensington Swan
- King Country Electric Power Trust
- Linetrust South Canterbury
- Marlborough Electric Power Trust
- David McLay
- Minter Ellison Rudd Watts (2 submissions)
- Sean Moore
- MtH Chartered Accountants Ltd
- Network Tasman Trust
- New Zealand Institute of Chartered Accountants
- New Zealand Institute of Legal Executives
- New Zealand Law Society
- Northpower Electric Power Trust
- Professor Nicola Peart
- Public Trust
- Jack Reddan
- Reserve Bank of New Zealand
- Rogers & Rutherford
- Ross & Whitney
- Russell McVeagh
- David Sceats
- Society of Trust and Estate Practitioners
- Southland Power Trust
- Statistics New Zealand
- Tappenden Holdings Ltd
- TGT Legal
- The New Zealand Guardian Trust Company Ltd
- Trustee Corporations Association
- Trustees Executors Ltd
- Veda Advantage (NZ) Ltd
- Waipa Networks Trust
- Waitaki Power Trust
- Waitomo Energy Services Customer Trust
- WEL Energy Trust

- West Coast Electric Power Trust
- WHK
- David A R Williams QC
- And one submitter who wishes to remain anonymous



# Appendix C

## Consultation list

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The Law Commission has consulted with the following during the review of the law of trusts:

- Vicky Ammundsen
- Professor Tony Angelo
- Auckland District Law Society
- Auckland Energy Trust Board
- David Bigio
- John Brown
- Chapman Tripp
- Helen Dervan
- Judge Caren Fox
- Glaistor Ennor Solicitors
- Anthony Grant
- Richard Green
- Selwyn Hayes
- Inland Revenue
- Simon Karipa
- KPMG
- Law Commission for England and Wales
- Legal Services Agency
- Māori Land Court
- Denham Martin
- Ministry of Business, Innovation and Employment
- Ministry of Justice
- Ministry of Social Development
- Anthony Molloy QC
- New Zealand Law Society
- New Zealand Institute of Chartered Accountants
- New Zealand Trustee Services Ltd
- Office of the Official Assignee
- Office of Treaty Settlements

- Professor John Prebble
- Price Waterhouse Coopers
- Public Trust
- Reserve Bank of New Zealand
- Scottish Law Commission
- Damian Stone
- Ingrid Taylor
- Taylor Grant Tesiram
- Te Puni Kōkiri
- The Treasury
- Simon Weil
- Nick Wells
- Justice Joseph Williams

We are grateful for their contribution.