

Yet more expansion of the role of Courts in private lives

Peter Watts considers the Law Commission's *Review of the Law of Trusts*

The Law Commission in November released its issues paper, *Review of the Law of Trusts: Preferred Approach* (NZLC IP 31, November 2012).

On a short perusal, there is much of value in this paper. One ought also to be grateful that, for the most part, the Commission, having set out a spectrum of suggestions for reform, has avoided the most totalitarian of them. However, the paper in places buys into the modern tendency, both academic and curial, to replace settlor-supremacy (putting the settlor first) with beneficiary-supremacy (putting the beneficiary first) in explicating the trust. Beneficiary-supremacy inevitably expands the judiciary's role in private lives, contrary to the Commission's hope (at [24]) that its proposals would "minimise court involvement" in the administration of trusts.

Before I turn to outline the fading orthodoxy of settlor-supremacy, let me say that I intend thereby to make no argument for the sanctity of the trust itself. The trust's uses (no pun intended) can be socially costly, if not in some circumstances downright pernicious. To the extent that unregulated dispositional freedom allows property owners, for example, to (a) burden the taxpayer with their disowned immediate relatives, (b) deprive alienated spouses of their contributions to what was a form of partnership, and (c) secrete assets from creditors, a powerful case can be made for some form of state intervention. The role of trusts in tax avoidance may also need some attention, and a degree of 'consumer' protection may be warranted in relation to pension trusts. The Law Commission recognises this in its paper, but, wisely I think, recommends that each social problem be addressed by

specific legislative intervention.

The starting point of settlor-supremacy is that, in the paradigm trust, it is the settlor who owns absolutely the property that is to be vested in the trustees. Having complete freedom to dispose of his or her property, the settlor who is inclined to give away some of that property could, as an alternative to creating a trust, gift the property to X in the mere hope and non-justiciable wish that X will do as the settlor has indicated. This is what is called a 'precatory gift' (or sometimes a 'precatory trust', an oxymoron). So, if the settlor is prepared to take the risk on X doing the right thing, the whole subject can be left to moral duty, the law excluded, and the 'beneficiaries' left right-less.

It is true that if the settlor chooses to create a trust rather than make a precatory gift, the settlor invites the intervention of the law. However, subject in some circumstances to compelling reasons of public policy, the Court remains the settlor's guest, and hence gets no more jurisdiction than the settlor gives it. Equally, the trustee takes on only such duties as he or she is prepared to accept, although trustees will need to clarify their position with the settlor before the drafting of the trust document is completed.

In orthodox thinking, therefore, the trust turns on the will expressed serially of the settlor and the trustee, and the beneficiaries get no more rights than these parties choose to give them. To talk, as the Commission does, of "enhancing the accountability of trustees" (at [22]) and of "beneficiaries who cannot protect their own interests" (at [24]) comes close



to hogwash on the orthodox view if isolated from the intent of the settlor and the undertaking of the trustee; to repeat, the beneficiaries were not entitled to anything in the first place. If all we were concerned with was ensuring that vulnerable beneficiaries get the rights the settlor intended, then well and good, but modern beneficiary-supremacy does not think like that.

Many consequences flow from the fundamental concept of settlor-supremacy. One is that it is plainly problematic for the Courts to override trust deeds that exempt trustees from negligence, even gross negligence. The view of Lord Justice Millett to this effect in *Armitage v Nurse & Ors* [1997] EWCA Civ 1279; [1997] 2 All ER 705 and of the majority of the Privy Council in *Spread Trustee Company Ltd v Hutcheson & Ors (Guernsey)* [2011] UKPC 13 must be right. The two dissents in *Spread Trustee* to the opposite effect, to which the Commission appears strongly attracted, are explicable only on the basis of paternalism (judges saying that “we know the settlor did not really intend trustees to act as they have”) or an abhorrence of human failing, including negligence. It is the mark of a totalitarian society when it wishes to intrude on all human shortcomings, be those carelessness, vindictiveness, callousness, or other weaknesses. Another factor driving opposition to the simplicity of Lord Justice Millett’s approach, one senses, is a desire for mystery; it adds to lawyerly mystique to ponder and pontificate (endlessly) about the ‘essence’, ‘nature’, or the ‘irreducible core’ of the trust.

As it happens, it is only what the Commission calls “the mandatory content duties” that it has ultimately recommended be compulsory. These duties are: (a) the duty to understand and adhere to the terms of the trust; (b) the duty to account to the beneficiaries for the trust property; and (c) the duty to exercise trust powers for a proper purpose. For other exercises of powers, such as investment decisions, only bad faith or recklessness, defined on a civil standard, are proposed as inexcusably unacceptable conduct.


This is a fairly unobtrusive approach, but even here it is probable that orthodoxy would give effect to a trust clause that excluded or limited the operation of these content duties. Certainly, settlors in a family context frequently wish to modify the content of the duties to account, knowing far better than anyone else just how difficult, litigious, self-centred, prone to

jealousy, insatiably greedy, or dysfunctional some of their children or other relatives can be.

So, by making mandatory its recommendations as to the trustee’s duties to provide information to beneficiaries (at [3.70] and following), the Commission has failed to adhere to settlor-supremacy. The Commission takes the view (at [3.79]) that to empower a trustee to withhold information from particular beneficiaries, as the New Zealand Law Society apparently recommended, would “in many cases be a ‘flag’ to litigate”. This may be so, but any such litigation is likely to be very much shorter than that which frequently follows where some beneficiaries get hold of information. The virtue of settlor-supremacy in this context is explained, extrajudicially, by Justice Campbell of the Supreme Court of New South Wales in “Access by Trust Beneficiaries to Trustees’ Documents, Information and Reasons” (2009) 3 J Eq 97, an important article.

Even where there is no exclusion clause

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in a trust deed as to the provision of information, it is arguable that the Commission overplays the Courts’ function. In this respect, the issues paper reflects one of the dangers of attempting to put common law rules and presumptions into statutory form, namely that the statute will give added weight to authorities that are not really the last word on a subject. *Schmidt v Rosewood Trust Ltd (Isle of Man)* [2003] 3 All ER 76; [2003] 2 AC 709 (PC) and *Foreman v Kingstone* [2004] 1 NZLR 841 (HC), on which the Commission understandably relied, are such cases.

Schmidt is the less problematic of the two cases, and no criticism is here intended of its principal holdings. Lord Walker of Gestingthorpe’s judgment also usefully sets out a list of factors that might be relevant to a Court’s discretion to decline to order trustees to make trust information available to beneficiaries. This list has found its way into the Commission’s draft recommendation P9. However, insofar as Lord Walker saw the trustee’s duties to provide information to beneficiaries as based on an inherent jurisdiction in Courts to supervise trusts (see [36], [51], and [65(3)]), rather than settlor intention, then, with respect, the Judge seems to me wrong.

Notions of the ‘essentials’ of the trust, and of the Court’s inherent jurisdiction, backed by threats that Courts might withhold their recognition of trusts where settlors do not meet the Court’s strictures, fail to address the fact that settlors have other options, in particular the precatory gift. The law of trusts needs to make sure that it stays ‘real’ in this regard, or we will see a lot more of such gifts.

Lord Walker’s dicta in this respect can usefully be contrasted with the approach to beneficiaries’ rights to information set out in the majority judgments of Justices Mahoney and Sheller in *Hartigan Nominees Pty Ltd & Anor v Rydge* (1992) 29 NSWLR 405. Lord Walker referred to this case, but mainly to put weight on the judgment of President Kirby, in fact a dissenting judgment. The whole of the majority judgments in *Hartigan* repay reading, but a short extract from Justice Mahoney’s judgment (at 436) gives a flavour of the analysis:

“I would, for myself, see the matter of confidentiality as being of particular significance in discretionary trusts of the present kind... Such a trust is not a mere commercial document in which the public may have an interest. It is a private transaction, a disposition by the settlor of his own property,

ordinarily voluntarily, in the manner which he is entitled to choose. Special cases apart, it is proper that his wishes and his privacy be respected.”

Lord Walker in *Schmidt* did not attempt to give much guidance as to how his list of factors might be weighed and applied. *Foreman v Kingstone*, however, has taken an open-government approach to the question and the Commission implicitly endorses this approach. In my view, *Foreman* has got the balance wrong. Even in the absence of an express power to withhold information, at least where a trust deed gives absolute discretion to trustees, it should be assumed that this discretion extends to how much information is to be made available to beneficiaries. In England, Justice Briggs in *Breakspear v Ackland* [2009] Ch 32 declined to adopt the approach in *Foreman*.

Nor does it follow from the fact that trustees need to be accountable, that they need to be accountable to beneficiaries rather than the Court. It ought to be possible for the Court to appoint an independent inspector to inquire into whether there has been a breach of trust. Indeed, Lord Walker in *Schmidt* seems to have contemplated this with his references (at [54]) to “professional inspection”. Once again, considerations of “open justice” need to be tempered by the fact that beneficiaries in such circumstances are better off than if the settlor had instead used a precatory gift and conferred no rights at all on them. The concept of independent but private inspection is already in place in company law in circumstances where shareholders allege misconduct within the company (see section 179 of the *Companies Act* 1993, and in respect of older United Kingdom legislation, *Re Pergamon Press Ltd* [1971] Ch 388 at 399-400 per Master of the Rolls Lord Denning).

The same tendency to aggrandisement of the judicial role flows through to Chapter 10 of the issues paper, where the Commission favours a mandatory judicial review procedure. Setting a presumptive test of review in the diverse range of situations where trusts are now used, from employee pension funds to small family trusts, is admittedly intractable. As a starting point, however, a strong case can be made for the ‘ultra vires and bad faith’ test that the Commission rejected. There might be room for implication of a more aggressive standard of review where a trust arises out of a contract, as normally pension trusts do.

Indeed, the volume of cases on judicial review of trustee discretion that is emerging around the Commonwealth is evidence, in my view, of overplay of the Courts’ function in this area. In company law, the traditional stance is that directors’ decisions are not reviewable at all (*Howard Smith Limited v Ampol Petroleum Limited and Others (New South Wales)* [1974] 1 All ER 1126; [1974] AC 821 (PC) at 832: “There is no appeal on the merits from management decisions to courts of law: nor will courts of law assume to act as a kind of supervisory board over decisions within the power of management honestly arrived at.”). Of course, in that setting shareholders normally have at their disposal the power to remove directors, which beneficiaries do not usually have in respect of trustees. Nonetheless, the constitutional function that Courts have in monitoring public officials is not present in the private context of trusts. One should assume that, except where there is demonstrable departure for the express terms of the trust, settlors intend the curial role to be one exercisable in extremis, especially when the trust document talks in terms of “absolute discretion”.

In conclusion, so long as we retain a belief in private property, settlor intention is the fundamental principle in an understanding of beneficiaries’ rights. Commitment to the freedom that that principle confers has been fading in recent decades. This is apiece with the fact that, particularly in New Zealand, a sort of benign totalitarianism has insinuated itself throughout private law. This trend provides at least the possibility of curial intervention for every setback or disappointment that one citizen suffers at the hands of another. It may well be that the general citizen prefers judges to have this sort of all-embracing power as referee (doing the right thing is a source of national pride), supported by the judge’s trusty lieutenant, the reasonable person.

There can certainly be far less objection to these developments where the jurisdiction is conferred by Parliament, as a revised *Trustee Act* would be. But one of the downsides of legislative reform, compared to common law methodology, is that it is very easy when people are making rules that may never affect them to set standards of perfection, and those whom they will affect rarely participate in the reform process. Setting standards that require doing the right thing as opposed to the minimal thing is also calculated to bring uncertainty with it. ☺