GLACIERS AND THE TRUSTS BILL 2017

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The Trusts Bill 2017 was introduced to Parliament on 1 August 2017, received its First Reading on 5 December 2017 (after the 2017 General Election) and was reported back by the Justice Committee on 31 October 2018. As at 21 February 2019, the Bill has not yet had its Second Reading and was languishing as Item 17 on the Parliamentary Order Paper of 19 December 2018.[1]

The Justice Committee's commentary on the reported back Bill refers to the "comprehensive review of trust law from 2009 to 2013" by the Law Commission as well as the public consultation on an exposure draft. Glaciers move slowly but do eventually make significant changes to the landscape – the Trust Bill is, in my opinion, a glacier.

Given the length of the process of reform of trust law, my task is somewhat enviable. For many lawyers, there is considerable familiarity with the major changes being made to the trusts landscape in New Zealand, but for others the excessive length of the process has been wearying so that boredom may have set in.

The main objectives of the Bill as stated by Justice Committee are:

- set out clear and accessible core trust principles
- ensure more efficient trust administration
- simplify and clarify the role of the courts in relation to trusts.

This paper is in three parts. The first addresses the major changes to the law of trusts that will be effected by the Bill once enacted, albeit on a deferred basis as the commencement date is 18 months after the date of Royal assent: Clause 2. The second part of this paper addresses a number of changes of significance made during the select committee process, as contained in the recommendations of the Justice Committee. The third part of this paper addresses what lawyers need to be doing now in order to prepare themselves and their clients for the commencement of the Trusts Act (assuming enactment).

[1] It was Item 16 as at 24 January 2019 !

Part One – Key Features

The key features of the Bill that will change the trusts landscape in New Zealand may depend upon one's own approach to trusts and the use made by trusts by one's clients. That caveat needs to be considered when reading my summary of key features.

Rule Against Perpetuities

The rule against perpetuities and the Perpetuities Act 1964 will be repealed and replaced by a legal rule specifying the maximum duration of most express trusts. That period will be 125 years. Clause 16(4) provides that where the terms of a trust, specify or imply a mechanism for determining the date of final distribution, the trust continues until the earlier of the date so determined by that mechanism or the date that is 125 years after the creation of the trust.

In recent years, a small number of trusts have been formed stipulating that the maximum duration is the maximum period permissible by law applying in future, albeit with a specification of the 80-year period for the purposes of the Perpetuities Act 1964 as a backstop provision. Such trusts will be able to avail themselves of the 125-year rule after enactment.

The impact of the repeal of the rule against perpetuities specified in clause 16(5), when taken together with the repeal of the Perpetuities Act 1964 by clause 155(b), may might conceivably produce some unexpected results over the next 60 years. In some respects, the Bill approaches the issues of repeal of the Perpetuities Act and abolition of the rule against perpetuities as being a statutory issue. In particular, Schedule 5 contains a table of amendments consequential upon that repeal and abolition. The "wait and see" rule contained in section 8 of the Perpetuities Act will be repealed but probably without possible adverse consequences because of the language used in clause 16(4):

> If the terms of a trust specify or imply a mechanism for or means of determining the date on which the trust property will be finally distributed, the trust continues until the earlier of—
>
> (a) the date determined by that mechanism or means; and
>
> (b) the date that is 125 years after the creation of the trust.

So, if use of a "Royal Lives" provision were to result in a trust with a maximum duration of say 126 years (being a live in being aged 105 plus 21 years), clause 16(4) would require final distribution at the expiry of 125 years. However, the "wait and see" rule might have applied in other situations, such as where there was a partial charitable gift, so that its repeal needs to be noted by advisers.

Age of Majority

The age of majority is specified to be 18 years. This clarifies some difficulties under current law. However, it is important to note that the age of majority only applies for the purposes of an "express trust" (as defined in the Bill). So, for a constructive trust, the age of majority will remain as 20 years by virtue of the Age of Majority Act 1970.

Trustee Duties

Mandatory duties and default duties will apply to trustees under Part 3 of the Bill. The

bill contains five mandatory duties of trustees. The relevant provisions of the Bill, as reported back, are:

> **22 Duty to know terms of trust**
>
> A trustee must know the terms of the trust.
>
> **23 Duty to act in accordance with terms of trust**
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> A trustee must act in accordance with the terms of the trust. 10
>
> **24 Duty to act honestly and in good faith**
>
> A trustee must act honestly and in good faith.
>
> **25 Duty to act for benefit of beneficiaries or to further permitted purpose of trust**
>
> A trustee must hold or deal with trust property and otherwise act—
>
> (a) for the benefit of the beneficiaries, in accordance with the terms of the trust:
>
> (b) in the case of a trust for a permitted purpose, to further the permitted purpose of the trust, in accordance with the terms of the trust.
>
> **26 Duty to exercise powers for proper purpose**
>
> A trustee must exercise the trustee's powers for a proper purpose.

These five duties are unexceptional from the perspective of a specialist trusts practitioner, but recent case law indicates that these duties are not consistently upheld in practice in New Zealand.

The Bill does, however, add a slight gloss by way of clause 19A. That additional provision, as recommended by the Select Committee, emphasises "the context and objectives of the trust". Clause 19A provides:

> **19A Guiding principle in performing duties**
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> In performing the mandatory duties set out in sections 22 to 26 and (except to the extent modified or excluded by the terms of the trust) the default duties set out in sections 27 to 36, a trustee must have regard to the context and objectives of the trust.

The default duties may be grouped in the following manner:

- Investment and Administration (excluding distribution) - clauses 27 and 28 contain codification of the differential standard of care applying to professional and lay trustees in relation to administration of the trust and investment of trust property.
- Exercise of Powers – clauses 29 to 35 codified the fiduciary duties that apply to trustees with the Bill opting to specify particular rules rather than a single generic rule. The specific rules cover exercising a power for the benefit of the trustee, active and regular consideration of whether to exercise powers, not binding trustees to a future exercise or non-exercise of the discretion, avoidance of conflicts of interest, acting impartially (although this does not require treating all beneficiaries equally), not making a profit from the trusteeship, and not taking any reward for acting as trustee (although reimbursement of expenses is permitted).

- Unanimity – clause 36 requires trustees to act unanimously. Obviously, the this is a provision that will often be modified where there is a charitable trust (as majority decision-making is not unusual in that context).

Clause 36A (formerly clause 21) requires a paid adviser (who advises on the creation of the trust or prepares the terms of the trust, and who recommends modification or exclusion of default duties) to take reasonable steps to ensure that the initial settlor is aware of the meaning and effect of modifications or exclusions of default duties.

Although the description used in clause 36A of a person who is paid to advise or draft is a relatively broad one, it is notable that the provision does not apply to professionals who advise or draft charitable trust documentation on a *pro bono* basis.

Non-compliance does not automatically invalidate the modification or exclusion in the terms of the trust.

Exculpatory Provisions

The use of trustee exemption clauses and indemnity clauses will be restricted. The relevant provisions are contained in Subpart 2 of Part 3. Clauses 37 and 38, respectively, restrict the use of trustee exemption clauses and trustee indemnity clauses. They provide:

> **37 Restriction on trustee exemption clauses**
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> The terms of a trust must not limit or exclude a trustee's liability for any breach of trust arising from the trustee's dishonesty, wilful misconduct, or gross negligence.
>
> **38 Restriction on trustee indemnity clauses**
>
> The terms of a trust must not give a trustee any indemnity against the trust property for liability for any breach of trust arising from the trustee's dishonesty, wilful misconduct, or gross negligence.

The key change arguably effected by these provisions is the introduction of a standard of "gross negligence". Although many trust practitioners, particularly in the international trust sphere, have experience of this term, it is one that is not capable of definitive explanation. It is not a term that has a precise meaning under New Zealand law. Accordingly, it is not surprising that the Justice Committee proposed a provision about the operation of the "gross negligence" standard. There are two aspects to clause 40A. The first is a general requirement for a court to decide whether the conduct of the trustee was "so unreasonable" that no reasonable trustee would have considered it to be consistent with the role and duties of a trustee. The second aspect is a list of eight factors that a court must have regard to when making its appraisal of unreasonableness. The factors listed in clause 40A(3) are:

> (a) the circumstances, nature, and seriousness of the breach of trust; and
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> (b) the trustee's knowledge and intentions relating to the breach of trust; and
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> (c) the trustee's skills and knowledge that are relevant to the role of trustee; and
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> (d) the purpose for which the trustee was appointed; and

(e) any other circumstances, including whether the trustee has been remunerated for the role, or characteristics of the trustee that are relevant to the role of trustee; and

(f) the type of trust, including, without limitation, the degree to which the trust is part of a commercial arrangement, the assets held by the trust, how the assets are used, and how the trust operates; and

(g) the purpose of the trust, including, without limitation, what the trust is intended to achieve, and whom the trust is intended to benefit and in what ways; and

(h) any other factor the court considers relevant.

These prohibitions on the use of trustee exemption and indemnity clauses may be contrasted with the default duties provisions – clause 39 stipulates that a clause in the terms of the trust is invalid "to the extent that it purports to have the effect prohibited by section 37 or 38". There is also a provision similar to clause 36A in relation to a paid adviser, but with two noteworthy changes. The recommendation by the paid adviser of any trustee exemption and/or indemnity clauses requires the adviser to take reasonable steps to ensure that the settlor (rather than the initial settlor)[2] is aware of the meaning and effect of the clause. Non-compliance by the paid adviser does not invalidate the trustee exemption and indemnity clauses, except that an adviser who does not comply **and** is, or subsequently becomes, a trustee cannot rely on those provisions. The Bill does not clarify the application of these rules in relation to existing trusts, but it is logical to suggest that this is a new adviser duty and cannot apply to pre-existing trusts.

Trust Documents

Documents to be kept by trustees and information that must be given by trustees to beneficiaries will be specified in the legislation. These provisions represent a codification of the law as it has developed since about 2000 with the decisions in **Schmidt v Rosewood Trust Ltd** [and New Zealand cases such as **Manukau City Council v Lawson**, **Kain v Hutton**, and **Cats' Protection League v Deans.**

Clause 41 requires a trustee to keep "so far as is reasonable" documents relating to the trust as listed in the provision. There are nine categories of document, together with any such documents that have been received from a former trustee.

Paragraphs (a) and (b) refer to the trust deed and any variations, while paragraphs (g) and (h) refer to deeds of appointment removal and discharge of trustees and any memorandum of wishes from the settlor. These are documents that would ordinarily be expected to be retained, and they should not be problematic in practice. So too are records of trustee decisions that will be required to be retained by virtue of paragraph (d).

Clause (c) refers to records of the trust property that identify assets, liabilities, income and expenses and requires that they are appropriate to the value and complexity of the trust property. Clause (f) is related because it refers to any accounting records and financial statements prepared during the trusteeship of the trustee. In the writer's experience, it is unlikely that financial statements have been retained for each financial

[2] It is not obvious why a different approach has been adopted in the two provisions. If "initial settlor" is appropriate for default duties, it surely is appropriate for exculpatory provisions.

year of a trust. Prospectively, however, retention of such financial statements will be required.

Paragraph (e) will require the retention of any written contracts entered into during the trusteeship of the trustee. Except for the "so far as is reasonable" language in the opening line of clause 41, retention of written contracts for a period of up to 125 years seems to be an extraordinarily onerous requirement. A similar comment might also be made in relation to paragraph (i)'s requirement for any other documents necessary for the administration of the trust.

Clauses 47 to 51 create a procedure for the provision of information by trustees to any beneficiary. Clause 47 establishes a presumption that a trustee must make available to every beneficiary the basic trust information set out in clause 47(3). That basic information is the fact that a person as a beneficiary, the name and contact details of the trust deed, details of appointments removals and retirements of trustees, and the right of the beneficiary to request a copy of the terms of the trust (previously referred to as a trust instrument) or "trust information". Clause 48 creates a presumption that a trustee must within a reasonable period of time give a beneficiary the trust information requested by the person. Both provisions state that they are subject to the trustee considering the factors set out in clause 49. The clause 49 factors are extensive and reflect recent case law, including **Erceg v Erceg**. Clause 49 is appended to this paper.

Clause 50 applies where in the trustee decides not to give information. Subclause (2) requires the trustee to apply to the court for directions except where (under subclause (3)) the basic trust information is given to at least one beneficiary after an interim period of up to 12 months when no beneficiary has trust information. Although there is no express statutory cross-reference, the "basic trust information" must be that set out in clause 47(3).

Clause 51 empowers the trustee to require payment by the beneficiary of reasonable costs of providing clause 48 information (or other information in accordance with the terms of the trust). The Select Committee added a stipulation that the trustee may require prepayment of some or all that cost before the information is given.

Part Two - Select Committee Changes

The Committee, unlike the Commission and the Ministry of Justice, has heeded the submissions noting the problems of applying the full scope of the new trusts law to all express trusts. Those problems arose particularly in the case of securitisation trusts where the exclusion of full duties on the trustees was an intentional and negotiated feature. Clauses 5(3A), (3B) and (3C), plus Schedules 2 and 3, permit the modification and exclusion of certain provisions of the Trusts Bill.

The term "power of appointment" will be defined to be the ability to appoint or remove a beneficiary. This is "to avoid ambiguity". However, that will only be a defined term for the purposes of the Trusts Bill. The other usages of "power of appointment" will remain in Equity and in trust practice. One usage is not too common in New Zealand as it relates to the power of the powerholder to "appoint" capital to a person – see **Thomas**

on Powers.[3] The other usage is the power to appoint (and remove) trustees. The writer's view is that the ambiguity cannot be removed.

A new Clause 16A has been recommended so that the application of the new maximum duration rule, replacing the rule against perpetuities, to resettlements will be clear. As with the rule against perpetuities, resettlements are considered to date from the original settlement.

In the writer's view, the addition of clause 16A was probably unnecessary, except to remove the scope for parties to rely on a spurious argument.

As already noted, the concept of "initial settlor" has been added to new clause 36A (which is effectively the former clause 21). The Committee report states:

> We consider this clarification necessary to differentiate the duty that does not apply to parties to a trust who later settle property on to the trust.

It is unclear why the same concept was not added to clause 40(2). Both clause 36A(2) and clause 40(2) apply at the time "before creation of the trust".

Clause 31 is the default duty about trustee is not binding or committing trustees to future exercise of discretion. The Select Committee report recommends deletion of the reference to the exercise of discretion "relating to the distribution of trust property". This means that the duty is intended to be "quite broad".

The concept of "gross negligence" has been clarified by the recommended insertion of clause 40A. This addition was considered in part one of this paper.

Quite important change was made to the provisions governing the giving of information to beneficiaries. The requirement contained in the original Bill that reasons be provided has been deleted. The Justice Committee report tellingly states:

> We also consider [clause 50(3)(b)] to be an extension of the current law. We do not believe this is the bill's intent.

That language clearly implies that the provisions relating to the disclosure of information to beneficiaries are considered to be codification of existing (albeit recent) law.

An amendment to clause 63 has been recommended clarifying that a power of appointment (meaning a power to appoint a person as a beneficiary or to remove them) cannot be delegated.

Clause 76 applies where a party takes a disposition of trust property. The Committee's recommendation was to replace it with a version that was closer to the original section 22 of the Trustee Act 1956. The new provision states:

> **76 Protection of purchasers and mortgagees dealing with trustees**
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> (1) This section applies if a trustee purports to exercise a power (whether statutory, under the terms of a trust, or otherwise) to sell or mortgage trust property or an interest in trust property.

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[3] Oxford University Press, 2nd edn, 2012.

(2) The purchaser or mortgagee is under no obligation to inquire into whether the money received by the trustee as a result of the sale or mortgage is needed, or how that money is later dealt with, by the trustee.

(3) This section is subject to the Land Transfer Act 2017.

One of the reasons for the recommended change is the view of the Committee that the original bills provision was not consistent with the policy of deterring money-laundering.

Clause 78 of the Bill governs the situation where beneficiaries agree to use trust funds to indemnify a trustee for a breach of trust in circumstances where the usual indemnity of the trustee is not available. The Committee recommended substantial amendments which enable the court to consent to the proposed indemnification or dispense with the requirement for some beneficiaries to consent.

Clause 97 governs the process of removal of a trustee. The Select Committee's reported version of the bill replaces the former clause 97 with clauses 97, 97A and 97B. Under the new provisions, there is a clear distinction between a compulsory removal of a trustee (where clause 97A applies) and an optional removal (where clause 97B applies). The new clause 97 itself addresses issues of whether the appointer relies on a power in the trust document (terms of the trust) or the statutory provisions. This depends on the operation of clause 86 as well as ensuring that there is clarity as to which power is being relied on by the appointer.

The provisions relating to the vesting orders have been recommended to be transferred to provisions in the Property Law Act 2007. It is important to note that these provisions are different from the new vesting provisions contained in clause 108 of the Bill. The clause 108 provisions apply where a new trustee is appointed, or a trustee is removed. These provisions are likely to greatly simplify the issues that currently arise where a trustee loses capacity. The Property Law Act provisions apply in other contexts, particularly where there is a mortgagee sale or a judgement for specific performance.

A recommended new clause 136(6) will enable litigants in family court proceedings where trust law issues are raised to apply that the proceedings transferred to the High Court.

The alternative dispute resolution (ADR) provisions are to be amended to distinguish between arbitral awards and other ADR outcomes.

A variety of amendments to the Financial Markets Conduct Act 2013, the Financial Advisers Act 2008 and the Retirement Villages Act 2003 have been recommended.

Part Three – Practical Steps for Advisers

There are two elements to be considered for law firms (including sole practitioners) when transitioning to the new trust law regime, after enactment of the Trusts Bill 2017. The first relates to informing clients as to the new rules and the implications for their particular trusts. The second involves modifying trust practices within the firm to mitigate future risks.

Informing clients about the new legislation will probably involve two different stages. The first will be general publicity about the new legislation and the need to conduct a

review of the trusts. That review of each trust, on a trust by trust basis, is the second stage.

It may be convenient to identify trusts that have powers of amendment in those (generally older) trusts that do not have powers of amendment. Where there is no power of amendment, the partial invalidity of exculpatory provisions will be automatic from the effective date of the Trusts Bill. The Bill does not contain specificity about how an exemption provision is made partially invalid by virtue of it omitting a reference to "gross negligence". The following example may be of assistance. An exemption provision from an old trust deed specifies:

> TO the extent permitted by law no Trustee of the trusts of this Deed shall be subject to any duties except the duty to act honestly and the duty not to commit wilfully any act known by such Trustee to be a breach of trust and the duty not to omit wilfully any act when the omission is known by such Trustee to be a breach of trust AND no such Trustee shall be liable for the consequences of any act or omission or for any loss not attributable to such Trustee's own dishonesty or to the wilful commission by such Trustee of any act known by such Trustee to be a breach of trust or to the wilful omission of such Trustee of any act when that omission is known by such Trustee to be a breach of trust nor shall any Trustee be bound to take any proceedings against a co-trustee for any breach or alleged breach of trust by that co-trustee.

It is somewhat difficult to "strike out" the language of this exemption provision in order to make it comply with the "gross negligence" standard. In one sense, addition of the words "gross negligence" is the way in which the provision needs to be re-drafted if there is a power of amendment. However, without a power of amendment, it is less clear how the cited provision should operate. This is, in some respects, similar to the problem that has arisen in relation to section 61B of the Charitable Trusts Act 1957. In **Re Beckbessinger,** Tipping J referred to the difficulty of deleting provisions with a "blue pencil" rather than "appropriate modification of the testator's words". That problem was accentuated in several High Court cases when the charities regulator refused registration or revoked registration under the Charities Act 2005.

For clients and for law firms, the accumulation of the core trust documents specified in clause 41 of the Bill is likely to be difficult. Document retention and destruction policies of most law firms will generally mean that it is difficult to locate documents falling into the following categories listed in clause 41:

> (e) any written contracts entered into during that trustee's trusteeship:
>
> (f) any accounting records and financial statements prepared during that trustee's trusteeship:
>
> (i) any other documents necessary for the administration of the trust
>
> (j) any documents referred to in paragraphs (a) to (i) that were kept by a former trustee during that person's trusteeship and passed on to the current trustee.

In relation to the reference to financial statements, contained in clause 41(f), the writer's experience is that law firms generally retain financial statements for a greater period than do the accounting firms that prepare such financial statements. In addition,

retention of "accounting records" for the entire duration of a trust is unlikely to be achievable in relation to pre-commencement date records.

Trustees and law firms should, in the writer's recommendation, commence steps to identify, locate and retain core trust documents that are listed in clause 41. Preservation of records today, rather than in 20 months' time, is desirable.

The foregoing suggestions are interim ones. It is likely that over the coming months, law firms are likely to develop additional practices in order to cope with the significant changes that will be imposed on trusts once the Bill comes into full force. Although it is difficult to be precise, because of the apparent low ranking on the Parliamentary Order Paper of the Bill, the writer's expectation is that the new trusts law will apply from about April 2021.

Conclusion

The timing of any possible Capital Gains Tax coming into force concurrently with the trusts law may make for an interesting time for lawyers. The adage "may you live in interesting times" has been suggested to be a Chinese curse and has been attributed to Sir Austen Chamberlain in 1936 (who was a supporter of Churchill's campaign for rearmament in the 1930s although a half-brother of Neville Chamberlain).[4]

This paper commenced with an expression of the opinion that the Trusts Bill was a glacier. The initial impetus for that characterisation was the slow and almost imperceptible progress of the reform process that commenced in 2008, or even earlier in 2001-02 when the late Donald Dugdale led the Law Commission's initial project with the title of "Some Problems in the Law of Trusts".[5] The major changes to the landscape that are made by glaciers are more significant than their apparent slow progress. The writer suggests that these changes need to be studied closely and appropriate changes made to legal practice to reflect the oncoming commencement of the Trusts Bill.

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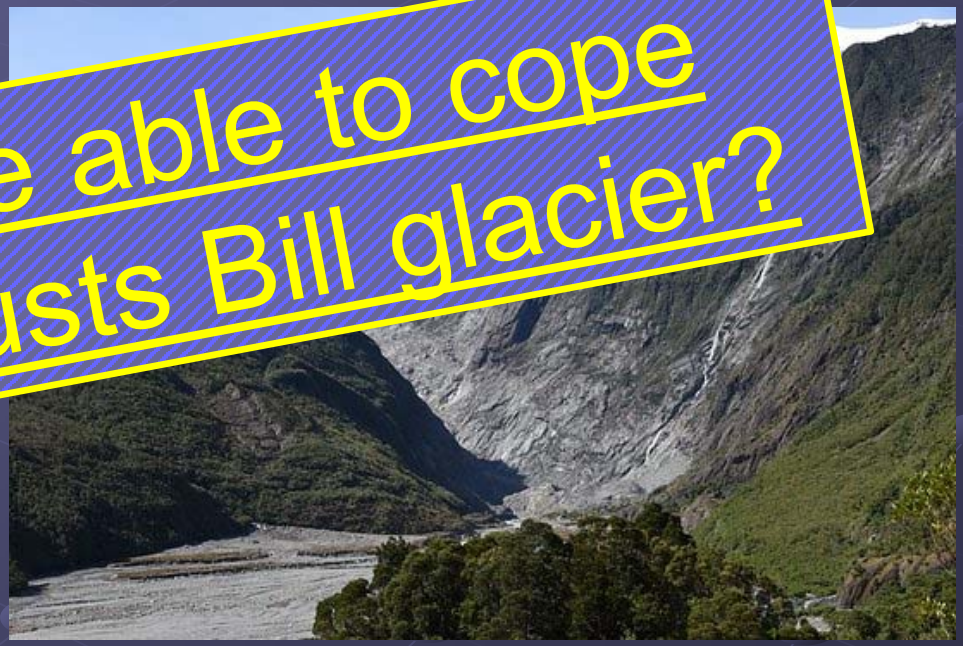
[4] "May You Live In Interesting Times" **accessed at** https://quoteinvestigator.com/2015/12/18/live/ on 21 February 2019.

[5] Law Commission, **Preliminary Paper 49** (January 2002) and **Report 79** (April 2002).

Glaciers

- Slow
- Powerful
- Land-changing



Will you be able to cope with the Trusts Bill glacier?

Clause 49

49 Procedure for deciding whether presumption applies

The factors that the trustee must consider (for the purposes of sections 47(2)(a) and 48(2)(a)) are the following:

(a) the nature of the interests in the trust held by the beneficiary and the other beneficiaries of the trust, including the degree and extent of the beneficiary's interest in the trust and the likelihood of the beneficiary 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 (if known) as to whether the beneficiaries as a whole and the beneficiary in particular would be given information:

(d) the age and circumstances of the beneficiary:

(e) the age and circumstances of the other beneficiaries of the trust:

(f) the effect on the beneficiary of giving the information:

(g) the effect on the trustees, other beneficiaries of the trust, and third parties of giving the information:

(h) in the case of a family trust, the effect of giving 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:

(i) in a trust that has a large number of beneficiaries or unascertainable beneficiaries, the practicality of giving information to all beneficiaries or all members of a class of beneficiaries:

(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):

(k) the practicality of giving some or all of the information to the beneficiary in redacted form:

(l) if a beneficiary has requested information, the nature and context of the request:

(m) any other factor that the trustee reasonably considers is relevant to determining whether the presumption applies.