

- Trust funds may be authorised by trust deed or by legislation or by other regulating act or by court authority → can come from multiple sources
- *\*\*\*In an exam – Where a duty issue, the first thing that you need to do is evaluate what the trust deed says (just by looking at the trustee provisions ss. 5-8, everything is qualified by what is set out in the trust deed). If you've got a specific obligation to invest, the primary authorisation will be from the trust deed. If the trust deed doesn't authorise anything, look to trust legislation and in that context, the primary authorisation is to invest to a standard of care, and looking to section 8 to determine what would be authorised*
  - If clear situation where trustee doesn't have a mandate to carry out the type of investment (because the trust deed is specific about the type of investments that can be made) and the transaction at issue clearly exceeds that, can be breach OR where the trust deed isn't specific about the type of investments that can be authorised, need to look to legislation
- Where trustee has an absolute discretion (i.e. no guidance in the deed) then will be in breach if do not 'invest' because that would not be exercising reasonable care
  - Must 'invest' i.e. '*...to apply money in the purchase of some property from which profit or interest is expected and which property is purchased in order to be held for the sake of the income which it will yield.*'
  - **Must exercise investment with reasonable care**
- Must follow guidance of the Trustee Act provisions ss5-8
- Must invest/ensure profits taken in even if you are a 'bare trustee': ***Byrnes v Kendle (2011) 243 CLR 253*** (where bare trustee had to get in the rent).

***Nestle v National Westminster Bank [1994] 1 All ER 118 TB 32.7.1***

**Facts:**

- A granddaughter and residuary beneficiary of the trusts established by William Nestle, who died in 1922 sued trustee for breach of duty to invest – *have they acted with authorisation AND if they've got a power to invest, have they exercised that power with reasonable care?*
- She argued that the trustee was authorised to invest trust monies in any securities or investments of the same or similar nature as Nestle held when he died and that the trustee had failed to invest in ordinary shares to obtain an enormous increase in the index prices.
- In 1922 the Nestle Estate had been worth 50,000 pounds. If it had of been invested in ordinary shares in 1922 it would have been worth 1.8 million (instead of 1 million) in 1988.
- Trustee bank argued that bank is not under a duty to achieve best financial results and that investment power must be exercised reasonably and cautiously to balance in this case the interests of the life tenant and the remainderman

**Held:**

- The English Court of Appeal claim arguing that whilst the trustee had *committed errors of judgement*, particularly in failing to consider the breadth of its powers of investments and to review the investments from time to time, it was not guilty of a breach of the duty to invest. Hoffman J examined the modern portfolio theory and stated:
  - *This is an extremely flexible standard capable of adaptation to current economic conditions and contemporary understanding of markets and investments. For example, investments which were imprudent in the days of the gold standard may be sound and sensible in times of high inflation. Modern trustees acting within their investment powers are entitled to be judged by the standards of current portfolio theory, which emphasise the risk level of the entire portfolio rather than the risk attaching to each investment taken in isolation...in revising the conduct of trustees over a period of more than 60 years, one must be careful not to endow the prudent trustee with prophetic vision or expect him to have ignored the received wisdom of his time.*
- **Invest carefully and cautiously** – Not a breach of a *duty to invest* but a breach of the obligation to invest with reasonable prudent where there has been an investment power conferred (unlike a case where the trustee must specifically invest, set out in trust deed)
- See further: *Harris v The Church Commissioners for England* [1993] 2 All ER 300 (charitable trustees must invest and cannot object on moral grounds); *Poseidon Ltd & Sellars v Adelaide Petroleum NL* (1994) 179 CLR 332 at 355, 367-368; *KCA Super Pty Ltd as Trustee of the Superannuation Fund known as 'KCA Super No 2* [2011] NSWSC 1301 at [44] per Brereton J.

#### Modern Portfolio Theory

- In essence modern portfolio theory demonstrates the advantages of diversification. The advantages include the minimisation of risk and administrative costs
- Risk is minimised because diversification averages profits and losses. Administrative costs are minimised because the efficient market hypothesis demonstrates that trustees cannot obtain better than average returns by making expensive enquiries in an attempt to forecast price movements.
- A portfolio that attempts to mirror the market as a whole is called 'index linked' or an 'index tracker.' It reflects rises and falls in the market it tracks but it cannot avoid systemic variations of value.
- Systemic variations are flattened by following a policy of holding the portfolio and of investing regularly
- Modern portfolio theory is highly persuasive and many financial services providers index link. This is not to say that trustees must index link rigidly. It is not appropriate for trustees to set a policy, in advance, that if changes in share prices have the effect that a portfolio in management ceases to reflect the list precisely, shares that have fallen

in value must be sold, and shares that have risen in value purchased, although some financial services providers do that.

### DUTY NOT TO PURCHASE TRUST PROPERTY

- A trustee must not purchase trust property – cannot act upon any benefit/knowledge that evolves from being a trustee
  - This would constitute a conflict of interest and a breach of the strict fiduciary duties set out in **Keech v Sandford**
- The obligation to avoid purchasing trust property is known as the ‘self-dealing’ rule.
- In the UK it has been held that in some exceptional circumstances a trustee may purchase trust property. This exception situation is known as the ‘fair dealing’ rule
- **Holder v Holder [1968] Ch 353 TB 32.8 – fair dealing rule**
  - **Facts:** Testator devised property (two farms) on trust equally for his widown, eight daughters and two sons. He appointed the widow, and one son and daughter as executors. The son who was appointed held one of the farms as a joint tenant and wanted to purchase it outright. Son carried out minimal executor duties (signed 9 cheques) before renouncing his executorship. Son purchased farms at auction. Other son subsequently objected on the basis of the self-dealing rule.
  - **Held:** Harman LJ that the very special circumstances of the case justified setting aside the self-dealing rule. Son had taken no part in the valuation of the farm and had never assumed formal duties of an executor and had never interfered with the administration of the trust. Danckwerts LJ agreed: beneficiaries never looked to the son for protection of their interests and they considered him to be a purchaser not a trustee.
- **Fair dealing rule rejected – Chewell v Excell [2009] NZLR 711** : Allan J stated at [43]: He was ‘*not satisfied that the approach in Holder v Holder has attracted any significant support. It cannot be said with confidence that the Court has a discretion to decline to enforce the rule against self-dealing.*
- **Fair dealing rule has not been followed in Australia either: Sleiman v Alwan [2009] NSWSC 484** - The court (quoting *Chewell*) concluded at [28]: ‘*There is a firm principle of equity that the sale by a trustee to himself is voidable at the suit of a beneficiary. The basal principle was laid down over the centuries. It matters not that the sale was for full value. The only defence appears to be acquiescence.*
- **Calvo v Sweeney [2009] NSWSC 719** - White J concluded that there is a distinction between the discretion of a judge to sanction the purchase of trust property ‘in advance’ and the discretion of a judge not to set aside a purchase once made. His Honour concluded at [236] court in *Holder v Holder* only intended to confer a discretion on a judge to sanction the purchase of trust property in advance and any further discretion was ‘*opposed to the policy of the law that where a trustee or other fiduciary, without the informed consent of his beneficiary or*

*principal, enters into an engagement in which his duty and interest conflict, the transaction is voidable without inquiry as to whether it is fair.* He agreed with the conclusions of Allan J in *Chellev v Excell* [2009] 1 NZLR 711 at [43]

- **Reader v Fried** [2001] VSC 495 - Pagone J noting that a breach of the self-dealing rule contravenes fiduciary principles and constitutes moral turpitude

#### **DUTY TO ALLOW BENEFICIARIES ACCESS TO TRUST DOCUMENTS**

- *Does your obligation to provide the beneficiary with trust documents stem from the fact that you're a trustee and a fiduciary OR does the obligation stem from the fact that the beneficiary owns the trust property in equity and T/F own the trust property*
- Trustee must provide beneficiaries with access to trust documents
- Trust documents are all those documents which relate to trust property
- Trust documents are not documents which relate to the exercise of trustee discretion
- There are two rationales underlying this rule: (1) Beneficiary has an equitable interest in the trust property (because the beneficiary owns the trust property in equity and T/F owns document) and (2) Trustee owes fiduciary duties towards beneficiaries to look after trust property and this process should be transparent
  - If you take second approach, applies to any trust (fixed or discretionary)
  - If you take first approach, could be problems with discretionary objects (under a discretionary trust) because they have an equitable chose in action (right) to be considered, but not a fixed interest, so if they don't have fixed interest they don't have interest in documents....

#### **Re Londonderry's Settlement** [1965] Ch 918 TB 32.10

- **Facts:** The trustees of a discretionary trust decided to exercise their discretion and distribute the entire fund, thereby bringing the trust to an end. One beneficiary, who was a member of the class of income and capital beneficiaries under the discretionary power, and who was also entitled to the income in default of appointment, object to this decision and sought copies of certain documents including the minutes of meetings of the trustees, the agenda and other papers prepared for the meetings and correspondence between the trustees relating to those meetings. The trustees objected to that demand.
- **Issue:** Can a discretionary object seek access to trust documents AND should they be trust documents?
- **Held:** The Court of Appeal held that the trustees were not obliged to disclose their reasons for exercising a discretion. As long as the trustees exercise their power that is, their absolute discretion to appoint (which they had done), bona fide with no improper motive, their exercise of that power cannot be challenged in the courts. Their reasons for acting as they decide are, accordingly, immaterial.

Trustees exercising a discretion are not obliged to disclose their reasons. The mere fact that those reasons are reduced to writing does not change that.

- Salmon LJ stated: *Nothing would be more likely to embitter family feelings and the relationship between trustees and members of the family, were trustees obliged to state their reasons for the exercise of the powers entrusted to them*.
- What are Trust Documents? Salmon LJ found that they had 3 characteristics:
  - 1) Documents in the possession of the trustees as trustees
  - 2) Documents which contain information about the trust which the beneficiaries are entitled to know (this would exclude documents relating to the discretion) and
  - 3) The beneficiaries have a proprietary interest in the documents and accordingly are entitled to see them.

**Privy Council rejected the ‘property’ foundation of Re Londonderry’s Settlement in: *Schmidt v Rosewood Trust Ltd* [2003] 2 AC 709 TB 32.10**

- *Rejected the argument that person only has a chose in action/right to be considered under a discretionary trust T/F you don’t own any trust document*
- **Facts:** Mr Schmidt senior had been one of several eligible beneficiaries to whom appointments of capital and income could be made under the terms of two trusts of which Rosewood was the trustee. Mr Schmidt senior had written to the trustees of both trusts expressing a wish that, if he were to die, his share of the trust property be held for Mr Schmidt Junior. Mr Schmidt Junior sought disclosure from Rosewood of documents relating to the trusts, both in his capacity as the administrator of the estate of Mr Schmidt senior, and personally. The trustee opposed providing the documents, on the basis that Mr Schmidt Junior in his personal capacity “was not a beneficiary in any sense of the word”, and that Mr Schmidt senior was “never more than “a mere object of a power who as such had no entitlement to trust documents or information. The argument in the Privy Council turned on whether Mr Schmidt Junior, in either of his capacities, had the kind of relationship to the trust that entitled him to disclosure of information concerning the activities of the trust. The contention of Rosewood was that neither Mr Schmidt senior nor Mr Schmidt Junior had a proprietary interest in the trust funds, and a proprietary interest was necessary for a potential beneficiary of a trust to have a right to access trust documents.
- **Held:** Lord Walker stated that he felt the *‘more principled and correct approach was to regard the right to seek disclosure of trust documents as one aspect of the court’s inherent jurisdiction to supervise, and if necessary to intervene in, the administration of trusts. The right to seek the court’s intervention does not depend on entitlement to a fixed and transmissible beneficial interest. The object of a discretion may also be entitled to protection from a court of equity, although the*