

ATTACKS ON TRUSTS

Vanessa Bruton, TGT Legal

Notes...

Lindsay: I'm pleased to introduce Vanessa Bruton who is a Partner of TGT Legal a boutique trust firm in Auckland. Vanessa heads up the litigation team with a focus almost exclusively on trusts and estates disputes. She's also a regular speaker on trust matters, particularly around her area of speciality relating to litigation associated with trusts and estates.

Vanessa, you're going to give some insights into what trustees can do to best manage a situation where they or their trust becomes involved in a dispute. I know you represent a lot of people who are either trustees being challenged, or people challenging trustees. Can you please firstly take us through how disputes arise with trusts?

Vanessa Bruton: Thanks Lindsay. Disputes arise in relation to what I call the three D's – Death, Divorce and Dementia. The settlor/trustee's death is a time that is ripe for a dispute, next would be when the settlor/trustee or a major beneficiary divorces. The third area of dispute I am seeing is around dementia and that's associated with an aging population and instances of Alzheimer or aged related diseases which seem to be on the increase as people live longer.

Examples of dementia-related disputes include situations where a trustee no longer has the requisite mental capacity to do the job as a trustee properly, or where the children are looking to obtain "their" inheritance early as a result of their father or mother no longer having full mental capacity.

Lindsay: Mental illness is a really tough one because there are different degrees of mental capacity. Dementia can set in over a long period of time or you can have a situation strike quite quickly (for example, as a result of a stroke). And under the law, I think there are different rules relating to will or trust situations.

Vanessa: Yes, that's absolutely right. I think dementia is an emerging area of the law. There really isn't much authority in terms of how these cases should be dealt with or what the legal tests are in relation to the requisite capacity when acting as a trustee, for example, as compared to making a will. So, watch this space.

Lindsay: You touched on the death of a settlor/trustee as being a difficult time. I'd imagine that if the settlor/trustee had been a very strong-minded personality with firm views on how the trust was to be run in their lifetime, it could be difficult for any surviving trustees left to face tough questioning from beneficiaries who may be disgruntled about the way the trust had been run.

Vanessa: Look, it really can be. A really interesting decision in that very area where I was counsel for the plaintiff trying to remove two trustees (which we successfully did), is a decision in the High Court at Auckland which came out in July 2013. It was one of those on death situations where there's often a contest between the second or third wife of the settlor and the children of the settlor's first marriage. This was one of those classic cases where, in his prime, the deceased settlor/trustee had been very directive and very astute.

When he passed away, there was a dispute between his widow and the son of his first marriage. The trustees were the widow, her lawyer (who had also been the deceased's lawyer) and two other trustees appointed by the deceased when the trust was settled.

The widow and the lawyer had been appointed more recently, after the deceased suffered a major stroke. So you had a situation with four trustees where the widow and the lawyer always took one point of view on pretty much every matter and the other two independent trustees took a different view.

We had a situation where the trustees were effectively deadlocked on all the major issues in the trust. The High Court's way of resolving that was to agree with my client's application that the widow and the lawyer trustee should be removed as trustees.

Lindsay: You hear of trustees being deadlocked and not able to agree on anything. It can't be an easy time to be a trustee, especially if you can't reach unanimous decisions or get things done...

Vanessa: Exactly, and the trust ends up being exposed to potential losses when appropriate decisions can't be made. That then paves the way for claims to be made against the trustees for breach of trust.

Lindsay: So what happens when trustees start being challenged on their stewardship of a trust, can you give us a picture of what's involved and what things come under review?

Vanessa: I think really there are three main areas of challenge if you're acting for a plaintiff or advising a beneficiary who is not happy with the way the trust affairs are being conducted.

Firstly there's what I call the structural issues, secondly, there's the trust administration issues and, thirdly the trustee behaviour issues.

Dealing first of all with the structural issues (and they've really been under the microscope as a result of the recent decision of the High Court in a case called Clayton). The question there is whether there is a real trust or whether the settlor trustee has reserved such extensive

powers of control that he (and it's usually a he) could say "well I'm going to end this trust right now and distribute everything to myself".

In the Clayton case, the Court held that no real trust existed. If I'm acting for the plaintiff, the first thing I'm going to do is have a really, really careful look at the trust deed from that perspective.

The second area is around the administration issues. This means looking at whether the trust has been managed and administered properly. So the things I would look at are whether there have been regular trustee meetings, whether resolutions have been passed for trustee decisions and whether the independent trustees are actively involved. Do they stand up and say "no" sometimes to the settlor/trustee? Do they just sign off on whatever the settlor/trustee puts in front of them? Is the so called "independent trustee" really just a puppet of the settlor/trustee?

The third area is the trustee behaviour area. We've already touched on capacity and so we look at things like whether this trustee really did have capacity to make that decision and if not (and if the trust deed requires all decisions to be unanimous), have we actually got a decision that is valid? So, I think capacity issues have to be taken really, really seriously. You can't just assume that they won't be raised if an unhappy beneficiary comes on the scene.

Also on the trustee behaviour issue, there are generally questions around whether the trustees have exercised their powers appropriately, whether they are impartial as between beneficiaries, whether they act independently and objectively and do consider the needs and interests of all beneficiaries. Or, are they partisan, and just go along with whatever, say, the dominant settlor/trustee wants?

Lindsay: So on that last point, some trust deeds do state that trustees are to give preference or priority to certain beneficiaries (for example, the husband and wife who established the trust), whereas many trust deeds give no direction on how beneficiaries should be treated or prioritised.

Even so, I think it's still important for trustees to undertake inquiry to understand the needs and circumstances of all beneficiaries so they can at least consider their interests, especially if there are beneficiaries with special needs who potentially could be supported by the trustees. Often there can be too much focus by the trustees on just one or two beneficiaries.

Vanessa: Yes, absolutely right.

Lindsay: Vanessa, I've heard it said that for trustees, protection lies in the "process" used to manage a trust and that the paper trail is an

important part of any defence. What are your views?

Vanessa: Yes. Although we are increasingly seeing cases where the paper trail is good but that more investigation is then required into seeing whether the paper trail genuinely reflects what's really been going on. So, if the trustees have simply gone through the motion of saying "yes, we've carefully considered the interests of all beneficiaries and resolved XYZ" and as trustees they actually haven't considered the interests of all the beneficiaries, we would look to pick that up.

That said, I think you're right Lindsay, if there's a good paper trail, it goes a long way to protecting the trustees from attack, but it's got to be a genuinely considered paper trail.

Lindsay: So from what we've discussed, a trust has got to be a genuine arrangement and run properly as a trust by trustees who behave and act responsibly using good process.

Vanessa: Exactly.

Lindsay: So, let's look at a situation where the trustees are locked in a dispute either between themselves as trustees, or with their beneficiaries. Often each side will have entrenched positions and there may be lawyers representing each side. What is the impact that you're seeing on some of the trustees or trusts involved? I'd imagine when a dispute gets to that stage, it could be quite a long time before anything gets resolved or gets to Court.

Vanessa: Well yes, and it's a question of degree because sadly we are increasingly seeing in trust disputes a whole lot of money being paid to a whole host of lawyers in legal fees that could otherwise more usefully have been spent on the beneficiaries of the trust.

Of course we have some trusts where the main asset may only be the family home and there's simply not sufficient cash available to pay the lawyers a lot of money. The unhappy situation may just continue on.

For my part, I do think that trustees need to take their obligations seriously, be really clear about what the trust deed says, know what their job is and understand their duty is to all beneficiaries (not just the settlor or settlor/co-trustee). If they do that it will greatly increase the chances of the trust and the trustees surviving unscathed and mean less money needing to be spent on legal fees, money which could be far better spent on the beneficiaries of the trust.

Lindsay: You've referred to the scrutiny trustees come under, the time it takes and the legal costs but there's also the emotional toll on the parties in a protracted dispute. It can become quite draining emotionally having to defend your actions as a trustee...

Vanessa: Yes, and not only that. We are increasingly seeing that when trustees defend their actions unsuccessfully, they can be ordered to pay the other side's costs (or at least a proportion of them) and be denied their right of indemnity from the trust fund.

A good example of that is the costs decision of Justice Gilbert in *Carmine v Ritchie*. It would obviously be very, very draining and stressful for a trustee to have to defend one's professional actions, but then to actually have to put your hand in your own pocket and pay costs is pretty serious.

Lindsay: When you think of the large number of trusts in New Zealand, a lot of trustees will be thinking that what we've been talking about will never happen to them. While it may not happen, it could happen and hopefully it may influence them to implement good practices as trustees.

Vanessa: Exactly. Trustees have got to do their job properly or else they shouldn't be doing it at all. I think if trustees do their job properly, when disputes arise, then trustees (and especially independent trustees) have an extremely important part to play in guiding the family through troubled waters, assisting the trust structure to survive and in minimising the cost and turmoil of achieving a resolution.

Lindsay: I'm pleased you've referred to that Vanessa as we don't hear enough of the positive aspects of trusteeship. There's no doubt the role can be onerous, but it can also be very rewarding. In a nut shell then, what would you say are good practices for trustees if they do come under attack? What are the things they immediately need to be thinking about?

Vanessa: I think the first point is to actually step back and take some independent objective advice, especially in situations where someone's been a trustee for many, many years very close to the family (or at least some members of the family).

Sometimes trustees can take great personal affront, perhaps rightly so, when their actions are challenged and they in effect get personally caught up in the scrap to their own detriment. I think in those situations it can be very helpful if they get good independent advice from someone who hasn't been so intimately involved with the family.

Another aspect I think that trustees always need to remember is their role is as a trustee charged with acting in the best interests of the beneficiaries as a whole. So for independent trustees, it's not for them to embark on a personal crusade or blindly support the position taken by one particular trustee or beneficiary or the settlor.

Independent trustees have got to be able to always stand back and remain impartial. If they can't do that, that's where we're seeing them running into trouble and being removed by the Courts (and in some cases found liable for breach of trust and ordered to pay compensation to the trust fund).

Lindsay: Vanessa, thank you for your overview into what happens in a trust dispute and your suggestions on the steps trustees can take to put themselves in the best position if a challenge to their trusteeship arises. I know your contact details are best found through your website www.tgtlegal.com.

Vanessa: Thanks Lindsay.