

MEETINGS AND REVIEWS

Anthony Grant, Barrister

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Lindsay: I'm pleased to introduce Anthony Grant an Auckland based Barrister specialising in commercial law with a particular interest in the law of trusts. Anthony's a regular speaker on trusts and writes a two weekly column in New Zealand Lawyer magazine where he comments on topical matters relating to trusts.

Anthony Grant: Hi Lindsay. Thank you

Lindsay: Anthony, a number of lawyers and accountants have mentioned to me that it's often hard to get client co-trustees in to meet as trustees. In some cases meetings have stalled since gift duty was scrapped, in other cases it appears trustees seem reluctant to meet because of the perceived costs. Why do you think trustee meetings and regular trust reviews are important for trustees?

Anthony: I'll give you a couple of reasons why they are important.

The first one is that human trustees (as distinguished from corporate trustees), have full financial accountability for their actions, unlike companies where directors are less exposed financially. Many trustees have no idea of the exposure which they have as trustees. So for their own financial wellbeing, it's very desirable that their management of the trust assets should be regarded by the Courts as appropriate. That's the first reason to meet and it's about pure financial self-interest.

The second reason is that trustees may have various financial accountabilities in relation to the investment of trust assets. Section 13E of the Trustee Act refers, for example, to the desirability of maintaining the real value of the capital and income of a trust and it generally favours a diversified portfolio investment strategy. Now I suspect that most trustees have no knowledge of these things.

In one New Zealand case which has been reported all around the world, the trustees were prevailed upon to allow the assets to be invested with a focus on income for a wife beneficiary. By the time of her death some years later, the value of the investment assets had been depleted dramatically, mainly through the impact of inflation on what were mainly fixed interest assets.

One of the trustees was a professional corporation, which was ordered to pay a large amount of money to make up the deficit because it simply hadn't managed the investments adequately. That's the second reason to meet, that trustees actually do have real financial accountabilities in relation to the investment of trust assets.

Lindsay: So, regular trustee meetings and reviews are important for managing trustee risk and accountability. Your investment example shows the significant cost to the trustees if they get it wrong (in that case by not balancing the widow's needs against the needs of the beneficiaries who would eventually receive the capital on her death). Presumably there would have been plenty of opportunities for the trustees to not only review what was happening with the investments, but to make and implement the tough decisions that were actually required to be made...

Anthony: The widow in that case was entitled to income on the assets during her lifetime so she wanted maximum income. She prevailed upon a trustee to do that because she had a forceful personality. It came at very considerable expense for the trustee who was forced to make a substantial payment because the value of the trust assets had not been maintained properly. The final beneficiaries sued and succeeded in requiring the trustee to pay up the substantial shortfall in the value of the trust assets.

Lindsay: Let's expand a little more on investment reviews. I agree reviews are important, especially where active investment assets are held. It worries me when I see some trustees sign annual resolutions to say they've reviewed the investment strategy and decided it's still appropriate. When you look more closely, often the trustees haven't met, assessed investment performance and in some cases, there isn't an investment strategy for the trust. What are your thoughts?

Anthony: Section 13E of the Trustee Act which I mentioned at the outset, is concerned with the various principles of investment. New Zealand was ahead of the pack in creating this legislation and it's essentially a diversified portfolio investment strategy regime which effectively requires trustees to talk about their investments and assess whether they're meeting the criteria. Section 13E can be avoided in the drafting of a Trust Deed if the settlor isn't so fussed about it.

In general though, that section is there and trustees who just sign a piece of paper without discussing it, aren't actually participating in the investment process as the statute contemplates they ought to. While in most cases nothing will come of it, there do come times when something may well come of it. I've just been giving advice on one case where scores of millions are involved and claims are being made about the failure of the trustees to follow the diversified portfolio strategy. I'm not sure just how knowledgeable most trustees are about the criteria in Section 13E.

Lindsay: I'll include an appendix to this guide showing Section 13E for people to see the sorts of things that you are referring to (see **Appendix 2**).

Anthony: Yes, I agree.

Lindsay: Anthony, we've covered a few reasons why it's important for trustees to meet and review what's going on. I know trustee meetings were often tied to the annual gifting and now there is no gifting, some professionals are mentioning it is difficult to get clients in to hold a trustee meeting. What are your thoughts on how often trustees should meet or how they should structure their trustee meetings?

Anthony: My view is that trustees should meet at least annually. The fact that gifting is now free of tax is neither here nor there. Trustees have responsibilities.

They should meet at least annually and use a structured agenda. You have given me an example of the sorts of things trustees should consider in their annual meeting or review that I understand you will attach to your guide. I think what you've done is a very good job and it will help trustees focus on things that matter (see **Appendix 3**).

When they meet, trustees should also keep good records. They should prepare resolutions for any decisions they make and minutes of what they discussed and agreed at meetings. If beneficiaries inquire, they can be shown the trustees resolutions for decisions which have been made.

In that context, there's a question about whether trustees should give reasons for decisions. Trustees who include reasons as part of their resolutions can be held to account as to whether or not their reasons were sensible and justifiable and therefore it's not usually wise for trustees to tell beneficiaries what their reasons are.

However, it may well be useful for the trustees own benefit, to keep information and any advice received relating to particular decisions on the Trust File. In the event one of their trustee decisions was ever challenged in the future, the trustees would be able to refer back to their reasons for making the particular decision. It's sensible that they should do that.

Lindsay: You've mentioned that trustees "can be held to account". In the investment example you used earlier, the trustees had to make good the losses that the trust had suffered. Do you have any other examples you can share where trustees have been held to account for their performance?

Anthony: Well my next article in the NZ Lawyer magazine is about trustees in just that situation as it happens. It involves a Maori trust, a trust with thousands of beneficiaries, which was mismanaged badly and millions of dollars were lost. The final two trustees were removed by the Court. They appealed all the way to the Court of Appeal saying

that they ought not to have been removed because they didn't do anything personally wrong, they didn't misappropriate any money or anything.

But the Court has said they had to go because if they're going to accept appointments as trustees they are going to be held to account. They need to be competent and they simply didn't have the necessary skills for the job. The trustees in that case were potentially up for millions of dollars of damages and it was foolish of them to have accepted the role of trustee without understanding all that was involved.

Lindsay: That's a good example. It highlights the importance of trustees being competent and why trustees need to be trained and skilled as trustees.

Anthony: Basically you wouldn't want someone to be a trustee who didn't have a reasonable understanding of what the role required, because if they learn on the job, they may well make mistakes as those two trustees did. One of the trustees conceded that when she started her role as trustee she was reasonably ignorant of what was required of her and that she was out of her depth.

They said that as time had gone by they had understood far more and they were now competent people, so the fact that they had been less diligent or less knowledgeable at the outset should not be held against them. I was pleased that both the Maori Land Court and the Appellate Court within the Maori system, held against the two trustees saying that it simply was not good enough. They had to be competent and they had not shown sufficient competency.

Lindsay: Where else do you see trustees running into problems with managing their trusts?

Anthony: Well from a litigation perspective, New Zealand has a proliferation of family trusts where the husband and wife as trustees usually have very little knowledge of what a trust is. They think they don't really have to do anything and there are many cases, particularly in the family law area, where the trust is wholly mismanaged.

For example, there's no bank account for the trust, payments the trust is supposed to make are paid by the individuals, individuals claim as their own deductions payments which are the trust's deductions, there are no written minutes, there are no records of meetings, in fact there may have been no trust meetings.

The Courts tend to be dubious about trusts that are managed like this and try to find ways to circumvent them. When you consider trusts are created for the purpose of assisting parties to preserve trust assets, it

can all be quite counterproductive if the trusts are not run properly. This is because the Court can say “well this actually was never run as a trust and you guys never really intended to transfer the property to a trust. As far as you’re concerned it was still your property throughout and remained that way”.

It’s also important for trustees to have a good understanding of the main terms of a trust and know what the Trust Deed says. It is remarkable how often trustees don’t know who all the beneficiaries are or what rights people have in relation to trusts, even to the point where they distribute money to non-beneficiaries.

Lindsay: The problems you’ve just described reinforce your earlier point that trustees need to be skilled for the job and take responsibility for running their trusts properly. What then would you see as good practice for trustees around trust meetings and trust reviews?

Anthony: I think trustees should generally have an annual meeting as trustees and follow an agenda. It does depend upon the size of the trust and what its purpose is.

In trusts where the trust is just holding the family home and little else, there may be no need for meetings more often than once a year. If it’s just the home and nothing else is happening, you probably don’t need even to meet annually. However, in a trust where there are active investments and businesses being conducted, then trustees need to be on their guard to know exactly what is going on. For example, in a trust with larger assets, monthly meetings may be sensible.

A good practice would be for the trustees to get a better understanding of the settlor’s wishes for what is to happen if he or she were incapacitated, or were to die. While there can be a memorandum of wishes, it is my experience that people’s wishes often change as the years go by. It may be useful for trustees to meet with settlors to know what should happen if someone has, for example a heart attack, and how the settlors may wish for the trust is to be dealt with at that point.

It can also be sensible for trustees to meet with beneficiaries from time to time and try and include them in the process of decision-making to a degree so that they feel part of it instead of being alienated from it. My experience is that once trusts hit the second generation and certainly by the time they hit the third generation, there’s almost invariably one member of the family who hates the trust and hates the trustees. It all leads to difficulties.

One of the major problems with substantial trusts is that trust wealth demotivates beneficiaries and it’s actually harmful for them. Where a trust involves substantial wealth, it can be useful to provide beneficiaries with support for financial or business skills, counselling,

advice on hiring and firing people, etc. That way when the wealth does devolve in the future, it will be managed responsibly.

This goes another level beyond involving beneficiaries in a meeting, it is saying it's not good enough for you just to know about the trust, this wealth's very substantial and you guys all need to understand much, much more about wealth management so that it actually is productive rather than destructive.

Lindsay: Thanks Anthony. So to summarise, the size and nature of the assets of a trust will often drive the frequency of meetings and reviews. Next, trustees should be thinking about how they connect with settlors and beneficiaries and meetings are a way of doing that. Finally, trustees have accountabilities and risks, so regular trustee meetings and reviews should be seen as just part of the proper management and oversight of a trust, and its assets and liabilities.

Thank you for your recommendations and thoughts on managing trustee meetings and reviews. If people wish to contact you, they can do that through your website www.anthonygrant.com and I'd recommend trustees access your column online through the NZ Lawyer magazine as it provides good insights on topical trust issues and problems www.nzlawyermagazine.co.nz.

Anthony: Thanks Lindsay.