

# THE QUALITIES OF A TRUSTEE

Alasdair McBeth, DLA Phillips Fox

Notes...

**Lindsay:** I'm pleased to introduce Alasdair McBeth a Partner of DLA Phillips Fox in Wellington. Alasdair provides legal advice to trustee companies, financial organisations, Government agencies and Crown entities. He's has always maintained a strong interest in trust work and he's a trustee for private and international clients.

Alasdair, we're going to be looking at the qualities of a good trustee. Before we do that, when we last caught up, we talked about today's environment for trustees and the changing demands of society. Do you want to start with a few comments on what changes you're seeing?

**Alasdair McBeth:** We go through cycles every 30 years or so where you see significant financial losses, the most recent being the Global Financial Crisis. People try and recover their loss which leads to litigation, litigation leads to new law and trust law always features quite prominently. Particularly when you think of some of the finance company situations where directors who have been made bankrupt are still living in expensive homes and driving flash cars because they've had their money or wealth tied up in trusts.

In these situations liquidators or regulators who have suffered these losses, litigate to try and attack the assets held in trust. Judges respond and we're seeing a lot of old equitable trust principles see the light of day. When this happens we see trusts found to be shams or invalid and in some cases it's enabled trusts to be attacked and the assets used to meet the debts owing to creditors or investors.

We're also seeing trust assets attacked in the relationship property area as a result of changes to the law giving Judges greater discretionary powers. Also, Judges are being quite proactive I suppose in trying to find ways to attack trust assets on equitable grounds. In some very acrimonious relationship breakdowns we are seeing trust assets being divided in ways that weren't ever contemplated to bring about an equal division of property. This is a significant development and has meant a lot more care is needed in planning and managing trusts because of what I'd call the desire by the Courts to use old principles and bring fairness and equality to bear on their decision to attack assets and trusts, if possible.

It's important people understand that the roles and responsibilities of a trustee are well entrenched. They're not something new. The principles for trusts are very old and really haven't changed a lot so knowing these is quite fundamental. Unless you know them, you shouldn't be a trustee.

**Lindsay:** I think trusts have often been seen as very private arrangements and if trustees are likely to be under more scrutiny, it's more likely they'll have to be more transparent and accountable for the job they do. Alasdair, take us through what you see as the qualities of a good trustee?

**Alasdair:** I think the first quality of a trustee must be around having sound judgement. For a trustee, that's about being able to weigh up the pro's and con's, consider all relevant factors and information and come to a decision that's in the best interests of the beneficiaries of the trust.

The starting point is they must know the terms of their trust deed. They must understand what the terms of the trust deed allow them to do and it surprises me that some trustees I talk to have never even seen the trust deed that they're trustee of, that's a problem.

**Lindsay:** Those trustees are just leaving themselves wide open.

**Alasdair:** Yes, but they must be able to understand. I think it's important they understand the family and the family dynamics, the settlor's wishes, etc. I think trustees need some financial acumen as well to understand the assets of the trust and the liabilities and potential liabilities. We're talking about how trustees critically assess their responsibilities so they understand. All this really comes under judgment and no one of sound judgment would ever accept a trusteeship unless they understood what their role and duties were and what the terms of the trust deed were.

**Lindsay:** So let's capture these qualities, you've mentioned qualities like sound judgement, being able to reason or interpret information, there's understanding and financial acumen. Trustees also have to manage relationships as well, between themselves as trustees, between trustees and beneficiaries and between trustees and settlors. What's important there?

**Alasdair:** Well if you put the financial crisis aside, I think the biggest problem I'm often faced with is when what I would call a "dominant settlor" dies. That's because when that type of settlor dies, the settlor (who is normally a husband, a trustee and the person who has probably set up and broadly controlled the direction of the trust), has been the key figure in the trust and the family to that point in time. When he dies, that control on not just the trust, but the family, ends as well.

It's a time when as an independent trustee you can get all sorts of reactions from family members, particularly if some of the decisions that may have been made have not been decisions that the family or the widow have agreed with or knew about. So, when that control

comes off, it can be a bit like letting the steam out of a valve and there can be all sorts of trouble. It's very important if you are a co-trustee with a person like the settlor/co-trustee I've just described, that you are aware of what could potentially happen. As a trustee, you need to be thinking about and planning for what could happen if that person was to die tomorrow and you're left holding the baby, so to speak. You need to take control immediately.

**Lindsay:** The qualities in those situations would be around being sensitive to needs, maybe a good listener and there's also a quality around planning. You've just described a situation where an independent trustee could be "the last person standing" left facing the family and their questions. What are your thoughts on how trustees should manage their relationships with the next generation or start involving them with the trust?

**Alasdair:** Lindsay, I'm a great believer in two things. One, I'm a great believer in a letter or memorandum of wishes which is revisited frequently, I'd suggest at least every two years. That way, if that settlor dies tomorrow, as the last person standing to use your phrase, you would know exactly what the settlor would have wanted. I think it's crucial that a letter or memorandum of wishes is in place and kept up to date as part of good trustee planning.

The second thing that's important is the point in time the next generation should start to become involved. It can be done in different ways – for example, they could be invited to an annual trustee meeting to ask questions, maybe they could be given a copy of the annual accounts for the trust and have the opportunity to ask questions. It's a healthy process which can be undertaken when the next generation is of an age and maturity to get involved and come on board.

Normally I'd suggest a first step being an initial meeting between the trustees and the beneficiaries and then having a general discussion about what the trust is and how it works, what its assets are and what its intentions are. In some cases it may lead in time to one or more of the children becoming a trustee.

**Lindsay:** So you're describing trustee qualities here around leadership, engagement and consultation by providing information to make the trust arrangement more transparent.

**Alasdair:** And it's very difficult because you are going to have some settlor/co-trustees that will have no intention of telling their children anything which can make it difficult for the independent trustee. There's no "one size fits all" approach, it's a matter of what we talked before about understanding the family dynamics. It's totally different

in each trust and each family. A good trustee will recognise and acknowledge that and act accordingly.

**Lindsay:** It can be hard to find one person with all the skills and qualities you're describing. That's where having complimentary skills and qualities within a team of trustees can be helpful.

**Alasdair:** You're quite right. There's no doubt that the best trust trusteeships I'm involved in are those where there are three or four trustees who bring different skills and perspectives to the table. Now these trusts are generally larger trusts where we would meet at least twice a year, with an agenda that is flexible enough to allow a free and frank discussion between all trustees.

Take an example of a farm trust where I'm one of four trustees. Each trustee brings different skills and knowledge – I bring legal skills, there's an accounting person, one has a farming history and knowledge and then there's the settlor/co-trustee who values the input of all the trustees. There's mutual respect, trust and confidence for what each person brings to the table.

**Lindsay:** So in that farm trust example, one of the qualities in that situation was having specific specialist knowledge relevant to farming. That must be an advantage...

**Alasdair:** Yes that is right. Another example would be in a trust owning shares in a private company involved in property development. While the trust is not the property developer in an operational sense, it's important for the trustees to know and understand what the company is up to if the trust is the sole shareholder. This is fundamental. Having a trustee with a knowledge or background in property development adds hugely to the discussion around the table.

It's common in many trusts for the main trust asset to be shareholding in private companies. You used the word transparency before. It's about the trustees getting transparency about what's going on in a company, what it's up to, what deals it's looking at, what commitments and liabilities that it's getting into. It's the sort of transparency that also reinforces to the people running the company that the trustees have got very, very close eyes on it...

**Lindsay:** So, in that case you're describing qualities around good inquiry to know what's happening. That's about asking questions, sometimes the hard questions, and challenging constructively.

**Alasdair:** Exactly, and it can be a good thing. It can sometimes be useful for a director/trustee to say "well look, my co-trustees don't agree with what's proposed". The directors have an out and can say to the other side "unfortunately the trustees who own the company

don't agree so we won't be able to go ahead". It can be quite a good escape hatch if the other side know that it's just not one person's decision but four trustees have to agree. That's about trustees being of independent mind and collaborative.

Trustees owning shares in private companies have to make all sorts of decisions so having people with a strong finance, accounting or legal sense can help when decisions are required like whether a dividend should be declared (or not), how to take money out of the company in a tax effective way or having a security interest over the company to secure any advances made from the trust. They're all really important things from an asset protection perspective.

**Lindsay:** That reinforces qualities around keeping things under review or being able to take advice...

**Alasdair:** Yes, and while trustees aren't expected to know everything, they certainly should know when they have a need to get advice and what sort of advice they should get.

**Lindsay:** Alasdair, thanks for setting out some very good qualities for trustees. What then would you regard as some good practices that go along with the qualities that we've been discussing?

**Alasdair:** Well I'll set out a few things that I think are important and while they might sound obvious, in my experience I've found that in many cases they're just not there. Things like:

- Having a minute book with all trust decisions noted and signed by all the trustees. Most trust deeds require unanimous decision-making, so it's important to be able to show in those situations that all trustees were unanimous when a decision was made.
- Next would be to understand what the trust assets are. I see a lot of mixing up of trust assets with the settlors' private assets. For example, dividend cheques for the trust get paid into the settlor's or beneficiaries' bank account rather than the trust bank account.
- Making sure the trust has its own trust bank account. This should be a separate bank account and closely monitored by all trustees.
- Proper financial accounts should be prepared each year.
- The trust should have an Inland Revenue Department (IRD) number if it is earning income. Trustees need to make sure tax returns are prepared and filed each year and any tax paid.
- Trustees having a proper understanding of investment and actively monitoring the on-going performance of the investments.

These things are all very fundamental. It's all about proper process and record keeping.

I'd also like to make a final point on delegation between trustees. Sometimes one trustee may be authorised to do certain things on behalf of the trust and on occasions this is sensible and appropriate. For example, where an investment strategy is approved by all trustees and one trustee is tasked with overseeing the implementation of the strategy with the investment adviser or broker.

This makes sense in these situations because all they're doing is implementing an agreed plan. However, the decision to allow that trustee to act on behalf of the trust should be recorded in writing together with what the agreed parameters are. It really all comes down to just proper process and no unilateral decision making.

**Lindsay:** Thanks Alasdair for a great overview of the qualities for a good trustee and your suggestions for good trustee practice. Alasdair, I know if someone wants to contact you, they can do that through your website at [www.dlapf.com](http://www.dlapf.com).

**Alasdair:** My pleasure.