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WHAT TO LEAVE OUT OF TRUST DEEDS

By David W Marks QC

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WARNING – THIS PAPER IS DELIBERATELY PROVOCATIVE, AND SHOULD BE REGARDED ONLY AS A WORK IN PROGRESS.

IT WAS PRESENTED FOR THE FIRST TIME (IN ADELAIDE) ON 7 MARCH 2018. ITS DEFICIENCIES IN NOT DEALING WITH SOUTH AUSTRALIAN STAMP DUTY LAW, AS REGARDS THE BENEFICIARIES ISSUES, WERE LAID BARE. THANKS ARE DUE TO THE WORKSHOP PARTICIPANTS.

IT WILL BE PRESENTED AGAIN IN BRISBANE TO TRIBUTUM CLUB ON 21 MARCH 2018, AND I SUPPOSE FURTHER LIVELY DEBATE WILL ENSUE.

DWM

1. The title is deliberately provocative.

2. Much of what we will discuss will need to be covered in a trust deed: but not in the way we see it done in some common clauses. Thus, when I say we should not have things like "beneficiaries", or even "words", in a trust deed, we are really looking for the right beneficiaries and the right words.

3. Two major areas where new thinking is necessary are:

   (a) Wide definitions of beneficiaries; and

   (b) Centralisation of substantial control in one person, as appointor.

4. But much else must be reconsidered.

1 Income

5. We must deal with income in the trust deed.

1.1 Income equalisation clause

6. But uncritical use of *income equalisation clauses* cannot continue.

7. Kessler & Flynn give us this old specimen for discussion (not as a recommendation):[1]

> ***"Income" in relation to an Accounting Period means the net income of the trust fund for the Accounting Period within the meaning of s 95 of the Income Tax Assessment Act 1936.***

8. The issues with that are known: draft ruling TR 2012/D1.

1.2 What to do

9. One approach is Kessler & Flynn's recommendation:[2]

> *"Income" in relation to an Accounting Period is such amount as the trustee determines, but if the trustee fails to make an effective determination it includes profits and gains of a capital nature.*

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1 Kessler & Flynn, *Drafting Trusts and Will Trusts in Australia* (2ed), p 229 para [12.25]

2 Kessler & Flynn, above, p 231 para [12.30]

10. Their discussion of this is nuanced.
11. Their recommended definition requires business-people to consider the trust's position in detail, possibly before 30 June.
12. This again would indicate that a trust is beyond the ken of less sophisticated businesses.
13. Kessler & Flynn discuss another approach, which attempts to cover the issues raised in the draft ruling. It lists out a treatment for each issue raised by the draft ruling.
14. That might, in my view, be more realistic for less sophisticated businesses in the first year.
15. But will detailed definitions ever be kept up to date, with changes in laws and in the Commissioner's views. Deeds would require constant maintenance.

1.3 Fixing existing issues

16. Most deeds allow the trustee flexibility to deciding "income". The issue can be managed year by year, by reviewing the income to date and prospective transactions. We are doing that, anyway, because of the requirements of dividend and capital gains streaming.
17. If there is no flexibility, but the deed seems outdated, amend same to substitute something flexible or at least workable. (We discussed amendment at my presentation in Adelaide in 2017.)

2 Exculpation clause

18. An exculpation clause should be considered. But simply inserting a broad clause no longer works, without considering the likely trustee and the places where the trust may travel.

2.1 Old form

19. The following is from a model deed in Grbich, Munn & Reicher *Modern Trusts and Taxation* (1978):

LIABILITY OF THE TRUSTEE

14.1 THE Trustee shall not be personally liable for the consequences of any error or forgetfulness whether of law or of fact on the part of the Trustee or its legal or other adviser or generally for any breach of duty or trust whatsoever unless it shall be proved to have been committed made or omitted in personal conscious fraudulent bad faith by the Trustee charged to be so liable, and accordingly all persons claiming any beneficial interest in over or upon the property subject to this settlement shall be deemed to take with notice of and subject to the protection hereby conferred on the Trustee.

2.2 Drafting choices

2.2.1 Whether wise at all

20. First the draftsmen certainly must consider whether to include an exculpation clause. I acknowledge the views of Mr Lee:

> *It will be submitted in this text that exemption from liability provisions can have disastrous consequences for the trust fund that have not been explored by or been before the courts and that the only prudent course for settlors and their advisers at the present time is to make sure that they are never used.*[3]

21. That is not the only view.

22. There are drafting decisions to be made. It is live whether an exculpation clause should be included.

2.2.2 Width

23. Secondly, in some cases a clause like the above example will be unsustainable.

24. Two instances suffice:

    (a) A professional trustee, such as a solicitor or accountant, who is charging a fee.[4]

    (b) Some jurisdictions positively prevent exclusion of anything more than mere negligence. Thus, such a clause will not travel well to New Zealand, assuming their *Trusts Bill* 2016 passes in its current form.

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3 Ford & Lee, *The Law of Trusts*, para 18.1110. That chapter is still edited by Mr Lee.

4 *Armitage v Nurse* [1998] Ch 241, 256.

2.2.3 Things to consider

25. If the trustee (or executor) is likely to be non-professional, and there are no foreign aspects requiring advice from overseas, a simple clause extending to conduct short of actual fraud may well be suitable.

26. Kessler & Flynn has an elegant example.[5]

> *A Trustee shall not be liable for a loss to the Trust Fund unless that loss or damage was caused by his own actual fraud.*

27. If it is known that the trust deed will have contact with overseas jurisdictions, think about the the foreign law.

28. The concept of "gross negligence" is now problematic under Scottish, Guernsey and Jersey systems of law, albeit for different reasons.[6]

29. The issue will become very live in New Zealand, shortly, I expect. I am increasingly impressed that Australia and New Zealand are effectively one market. I follow developments there, as our clients move freely across the border.

30. The *Trusts Bill 2017* (NZ),[7] clause 37, restricts exemption clauses limiting or excluding liability for a breach arising from the trustee's dishonesty, wilful misconduct or gross negligence. Clause 39 applies a "blue pencil" to such a clause.

31. Clause 40 of the NZ Bill requires the adviser to alert the settlor to the meaning and effect of an exclusion or indemnity clause. Failure to do so would void that clause as against the adviser – for example, as against an adviser who is proposing to act as trustee.

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5 *Drafting Trusts & Wills Trusts in Australia* (2nd Edition), paragraph 5.155:

6 Ford & Lee *The Law of Trusts*, paragraph 18.1120

7 The Bill has had its first reading, and is before the Justice Committee. Submissions to that committee close 5 March, and the committee's report is due on 5 June 2018: https://www.parliament.nz/en/pb/bills-and-laws/bills-proposed-laws/document/BILL_74746/trusts-bill (viewed 1 March 2018).

32. If there is to be a professional trustee, or professional executor, a balance must be struck in drafting an exculpation clause. (This is discussed at considerable length by Kessler & Flynn (2nd Edition), chapter 5.)

2.3 Exculpation – what to do

33. An exculpation clause may well be desirable.

34. Its form requires drafting decisions.

35. First, work out for whom you are drafting.

    (a) The New Zealand *Trusts Bill 2017* focuses on the person who is forming the trust. This is the person effectively making the gift. This is likely to be the correct focus.

    (b) But the demands and reasonable needs of trustees must also be considered.

36. Next, work out the systems of law with which the deed will have contact. Take local advice.

37. Changing an exculpation clause would be unusual – it is rarely seen as a priority.

38. But if a trust has contact with a foreign jurisdiction, local advice would be sought. The last thing a trustee needs is the uncertainty of a court, for example, "blue pencilling" a clause in an unpredictable way.

39. If there is a professional trustee, the trust fund will be larger, and the terms of the exculpation clause will be negotiated.

3 Trustee's lien

40. A trustee is commonly said to have a "lien" or "charge" over trust property in support of a right of indemnity or exoneration.

41. Occasionally you will see a clause, perhaps tacked to an express provision about the trustee's rights of indemnity and of exoneration, adding a provision as follows:

> ***… and the trustee shall have a lien over the Trust Assets for the purpose of securing to him the benefit of such rights of indemnity and exoneration.***

42. In many cases it may be anticipated that the trust fund will include personal property. The *Personal Property Securities Act 2009* (Cth) has caused some disquiet.

3.1 PPSA

43. This paper is not about the intricacies of the PPSA. However I should set out part of the problematic definition of "security interests" from section 12:

> *(1) A **security interest** means an interest in personal property provided for by a transaction that, in substance, secures payment or performance of an obligation (without regard to the form of the transaction or the identity of the person who has title to the property).*

44. There are then a number of express inclusions of interests in personal property provided by a transaction which, "in substance, secures payment or performance of an obligation" by way of various things including "a floating charge".

45. The point becomes particularly problematic in the case of a former trustee. One might think it difficult to conceive of a trustee having a right <u>against itself</u> to vindicate a payment obligation (such as a right of indemnity). But a former trustee, who has parted with the trust fund to the incoming trustee, is in a peculiar situation.

46. I do not wish to say that the argument has any merit. It is not an area in which I have expertise.

47. There are two seriously considered and lengthy articles now, dealing with the problem.[8]

48. While both of these heavy-hitting articles conclude on a generally positive note, it may be better for the time being to rely on rights conferred by equity, at least in relation to the proprietary interest.

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[8] D'Angelo & Busljeta, "The trustee's lien or charge over trust assets: A PPSA security interest or not?" (2011) 22 JBFLP 251;
Loxton, "In with the Old, Out with the New? The rights of a replaced trustee against its successor, and the characterisation of trustees' proprietary rights of indemnity" (2017) 45 ABLR 285.

3.2 Consequent recommendations

49. For the time being, I suggest omitting an express provision of the kind set out above.

50. One of the two articles in footnote 8 refers to discussion in the profession about whether even an express right of indemnity or exoneration (without mention of a "lien"), would offend. I think the balance of opinion from the two articles is against that further proposition.

4 Beneficiaries

51. For the next example, I will take the model discretionary trust deed in Grbich *et al*., and alter it fundamentally to reflect common definitions I have seen:

> ***1.1 "Primary Beneficiaries" means the children of [AB] living from time to time.***
>
> ***1.2 "General beneficiaries" means –***
>
> > ***(a) The Primary Beneficiaries, [AB] and any spouse, widow or widower or descendant of any of them alive from time to time.***
> >
> > ***(b) Any body corporate wherever incorporated or resident any share in which is beneficially owned or held by any Beneficiary, or by the trustee of any trust or settlement under which any Beneficiary has any interest whether absolute or contingent or by way of expectancy whether liable to be defeated by the exercise of any power of appointment or revocation or to be diminished by the increase of the class to which that Beneficiary belongs whether or not such corporation trust or settlement is in existence at the date of this Deed.***
> >
> > ***(c) The trustee (in his capacity as such) of any trust or settlement in which any Beneficiary has an interest whether absolute or contingent or by way of expectancy and whether liable to be defeated by the exercise of any power of appointment or revocation or to be diminished by the increase of the class to which that Beneficiary belongs … and whether or not such trust or settlement is in existence at the date of this Deed provided that the beneficial interest in property provided by such trust or settlement shall vest within the perpetuity period applicable to the trusts of this Deed.***
> >
> > ***(d) Any relative by blood or marriage of a Primary Beneficiary.***
>
> ***1.3 "Beneficiary" … means any one or more of the General Beneficiaries.***

52. The above clauses are in common circulation.

53. Wide classes of persons, including companies and trustees of trusts, are thus always objects of discretion.

54. Thinking of my own family, I know that one of my relatives spent years abroad. I never enquired about her immigration and citizenship status (which is the point to which I will come in a moment).

4.1 Recommendation

55. I deliberately corrupted the example clause given by *Grbich et al.*, to make my point.

56. However this corrupted version is the one I more commonly see in practice.

57. What *Grbich et al*. actually do in their subclauses 1.2(b), (c) and (d), is require written nomination by the Trustee of the body corporate, the trustee of the trust, or the relative as a "General Beneficiary", before that person falls within the definition of "General Beneficiary".

58. That is the course I suggest.

4.2 Reason for recommendation

59. I come to the importance of that now. I am not sure, looking back 40 years to the date of publication of *Grbich et al.*, what led those authors to include the requirement for written nomination. It is certainly something I have seen (though, as I say, more commonly there is no such requirement in the deeds I have seen).

60. One possible explanation is the sheer difficulty in doing something like appointing a new corporate trustee, and yet complying with New South Wales stamp duty concessions on change of trustee. The obvious promoters of the new corporate trustee would inevitably be family, and without the requirement that a corporation be nominated as a beneficiary first, the new corporation would automatically be a beneficiary, offending the longstanding New South Wales rule that a trustee of a private settlement cannot be a beneficiary if concessional treatment is to be gained: refer present section 54 *Duties Act* (NSW), and former section 73(2A) *Stamp Duties Act 1920* (NSW).

61. That part of the drafting is prescient.

62. Modern land tax, stamp duty, and foreign investment rules make it desirable that the trustee have more control over who is actually a beneficiary or object from time to time.

4.3 FIRB

63. I do not intend this to be a paper about all the difficulties with the current *Foreign Acquisitions and Takeovers Act*.

64. Suffice to notice that a simple transactions involving acquisition of established residential property in Australia cannot, without dealing with FIRB, be undertaken by a "foreign trust".[9]

65. The above follows from the interlocking definitions of "foreign person" in section 4, "substantial interest" or "aggregate substantial interest" and "associate" in section 6. You then turn to section 43 which makes the acquisition of an interest in Australian land by a foreign person a "significant action".

66. The most vexing aspects of this is that "substantial interest" and "aggregate substantial interest" are determined on an associate-inclusive basis, so that it would be a trivial matter to fall over the respective 20% and 40% thresholds without more. Worse, interlocking provisions commencing at section 17 tend to maximise the "interest". In terms of section 18(3):

> *For the purposes of this Act, if, under the terms of the trust, a trustee has a power or discretion to distribute the income or property of the trust to one or more beneficiaries, each beneficiary is taken to hold a beneficial interest in the maximum percentage of income or property of the trust that the trustee may distribute to that beneficiary.*

67. To take my simple example, of income beneficiaries defined by reference to a broad concept of "relative" – in many cases Australian citizens will have near relatives

[9] Under Regulation 52(1)(a), much residential land has no threshold for the purposes of section 52 of the Act. The actual treatment of a particular block of land must be considered carefully in light of this complex legislation, together with the foreign investment policy of the Commonwealth.

ordinarily resident abroad, such as their parents and grandparents, uncles and nephews, aunts and nieces.

68. The application fees and other administrative actions necessary to purchase in a relatively straightforward Australian discretionary trust would be unwanted. The consequences of not seeking exemption, of not notifying, or otherwise taking administrative action are beyond comprehension.

4.4 Queensland - AFAD

69. For example, under Queensland stamp duty law, the AFAD ("additional foreign acquirer duty") looks to a "foreign person". Under section 234(c), this includes the trustee of a foreign trust.

70. Under section 237, a foreign trust is one where "at least 50% of the trust interests in the trust are foreign interests". A "foreign interest" is defined as:

    (a) A trust interest of a foreign individual; or

    (b) A trust interest of a foreign corporation; or

    (c) A trust interest of a foreign trustee; or

    (d) A trust interest held by a related person of a person mentioned in the preceding three subparagraphs.

71. Given the broad definition of "related persons" in section 238 – which relies in part of a broad definition in section 61 – you need only have one member of the same family who is not an Australian citizen nor Australian permanent resident, for the entire trust to be tainted in many cases.

72. And this is without having to deal with the concepts of "foreign corporations" and "foreign trusts" potentially having interests in the subject trust.

4.5 South Australian "foreign ownership surcharge"

73. South Australia has followed in the footsteps of other States, and imposed a 7% surcharge on transactions qualifying for conveyance duty if, in outline, they involve acquisition of an interest in residential land by a foreign person: section 72 *Stamp Duties Act 1923* (SA).

74. Section 72(2) specifically includes a transaction by which a person "takes the interest as trustee for a foreign trust".

75. Under section 2(14) a "foreign trust" is defined depending upon whether interests are fixed. If beneficial interests are fixed, a trust will be a foreign trust if beneficial interests of 50% or more of the capital of the trust property is held by one or more foreign persons.[10]

76. If the trust is a discretionary trust, it will be a "foreign trust" if any of the following criteria are satisfied – that is to say that there is a foreign person who is:

    (a) a trustee;

    (b) a person who has the power to appoint under the trust;

    (c) an identified objection under the trust;

    (d) a person who takes capital in the trust property in default.

77. The Revenue SA website indicates that "identified" does not include somebody who might merely be identifiable by reference to a described class.

78. Thus if I made my "cousins" objects of a discretion as to income, apparently that would not, of itself, trigger the trust to be a foreign trust. However if I made my "cousins" default capital beneficiaries, and one of my cousins was a foreign person, the whole trust is deemed to be a foreign trust.

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[10] Essentially all natural persons are "foreign persons" in terms of section 2(14)(a) unless they are Australian citizens, holders of a permanent visa of a particular type, or New Zealand citizens who hold a special category visa. There is also a definition of "foreign person" to deal with a corporation.

4.6 Other revenue laws

79. This is not the occasion to explore the full range of State, Federal, and possibly local imposts on foreigners. We know that each State has its own way of dealing with this.

80. The point is dealt with, in practice by limiting actual objects or beneficiaries to a discrete group, whose movements you can monitor. This has to work in tandem with the "solution" under heading 4.7.

4.7 Ancillary or second-best solution

81. If it is nevertheless thought desirable automatically to include potentially diverse groups of people and entities as objects or beneficiaries, there should be a provision, for exclusion of a person from benefit, by a deed revocable or irrevocable made by the trustee (with or without approval of an appointor or like person).[11]

4.8 Summary

82. To emphasise the point, Australia remains very much a migrant society, and we are an increasingly global society. It is perfectly possible that a great number of your clients will have close relatives who are neither Australian citizens nor Australian permanent residents.

83. I have not dealt with other Australian stamp duty issues, the land tax issues in several States, nor potential FIRB issues.

5 Royal Lives Clauses

84. Trust deeds in Queensland often have some variation of the following as the definition of the vesting date:

> ***(a) The 80th anniversary of the date of this deed;***

[11] Kessler & Flynn, *Drafting Trusts and Will Trusts in Australia* (2ed), p 81 para [4.180]

(b) 21 years after the death of the last of the issue, of His Majesty, the late King George V, living at the date of this deed; and

(c) A date appointed by the [Trustee] in its absolute discretion,

whichever is the first to occur of the above.

85. Royal lives clauses take advantage of the historical ability to appoint that a trust vest no later than 21 years after the death, of a life in being at the commencement of the trust. In the example above, subparagraph (b) has the 21 years added to it, but for some reason we see deeds without that addition.

5.1 Queensland position

86. In Queensland, it is possible instead to appoint a fixed perpetuity period no greater than 80 years.[12] While, as a matter of statutory implication, if the vesting date is stated in the trust deed in Queensland, and it vests the trust in 80 years or less, that is taken as specifying the perpetuity period under the *Property Law Act 1974* (Qd).

5.2 Other States

87. What is best practice in other States really comes down to the experience of practitioners in those other States.

88. New South Wales adopts a completely different approach, specifying an 80 year perpetuity period for most private trusts (though of course leaving the draftsmen to specify for vesting in 80 years or less). As I understand it, it is possible to use a Royal lives clause in New South Wales, so long as it is used in combination with other provisions vesting the trust within the permitted maximum 80 years. Thus it would seem pointless in New South Wales to use a Royal lives clause, unless there was some particular view about use of the trust deed to invest in other jurisdictions.

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12 Section 209 *Property Law Act 1974* (Qd).

89. I am quite conscious that, for example, South Australian practitioners have some firm views about what to do about vesting periods. So long as the trust is wholly South Australian, I can see no reason for a vesting date to be specified. But then there is literature discussing what happens if, in particular, real property is acquired by the trustee.[13] I leave that literature to one side.

5.3 Recommendations

90. Do not use Royal lives clauses.[14]

91. One illustration will serve.

92. In *Clay v Karlson*,[15] in Western Australia, no one realised that the death of the late Duke of Gloucester, in 1974, brought about the vesting of the family trust concerned, until some years later. In the meantime the trustees had continued to make discretionary distributions.

93. This led to all sorts of complications.[16]

94. This cannot be an isolated incident. Material surrounding issue of draft ruling TR 2017/D10, about vesting of trusts, strongly suggests that ATO are seeing trusts which have been administered as discretionary vehicles, despite passing the vesting date.

95. I do not intend to speak today about the merits of that draft ruling, which goes into whether vesting dates can be extended after they have passed.

96. Rather, I mean to say only: that having the vesting of a trust depending upon careful study of *Burke's Peerage* and *Debretts* makes no sense in the modern era, when a lengthy perpetuity date can be specified as a term of years.

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13 See Michael Butler "Trusts – Extending the Vesting Date", The Tax Institute, 18th National Tax Intensive Retreat, 2010, at 7.5.

14 If the deed may have contact with a place without at least an 80 year perpetuity period, rethink this.

15 (1998) 19 WAR 287

16 *Clay v James* [2001] WASC 18

97. In each of the significant matters in recent years, where I have had to make application to the Queensland Supreme Court for sanction (on behalf of incapable beneficiaries) of an extension or removal of vesting dates, I have had the arduous process of actually tracing the lineage of Royal houses.

98. Ultimately, and perhaps significantly in this context, this has always led to a paragraph in the submissions which I call the "Royal minibus" submission – that is, that the future of a significant Australian business depends upon the quality of the driver of my mythical Royal minibus.

99. A final point coming out of the above is that the utmost vesting date could, without any difficulty, be inserted on the front page of a modern trust deed. This would tend to obviate some of the problems we are seeing at the moment, and is facilitated by the ability to specify a fixed period of years as the perpetuity period (in States like Queensland) and in any case the ability to specify a fixed period of years in Australia (80 or less in most States) as the ultimate vesting date.

6 Vesting dates

100. Far be it from me to suggest what should occur as a matter of South Australian practice. But the topic is obviously live. See paragraph 89.

101. In other places, it is either extremely desirable, or necessary to include a provision for the vesting of interests within the period selected as, or ordained as, the perpetuity period.

7 Winding up clauses

102. There should be <u>power</u> for the trustee to wind up affairs, on vesting.

103. Should there be an obligation? Will an obligation be implied?

104. In *Clay v James*[17] the gift over read:

[17] [2001] WASC 18

> *2. Subject to the trusts aforesaid the Trustees shall hold the Trust Fund on trust as to both capital and income for the member or members or the specified class living at the expiration of the Trust Period and if more than one in equal shares.*

105. Anderson J said of this clause:

> ***[6]*** *In my opinion, this means that on the vesting date, that is the expiration of the trust period, the trustees held the trust fund for the members of the specified class living at that date in equal shares and those members were entitled, as at that date, to immediate possession and if more than one, in equal shares. The duty of the trustees was to pay the amount of the trust fund in accordance with the settlement deed and otherwise to take all steps necessary to wind up the trust. The entitlement of the members of the specified class was to immediate possession of the whole of the interest in equal shares. In this sense, the property held under the settlement vested in both interest and in possession on the vesting date in the members of the specified class living at that date.*

106. When he released TR 2017/D10, the Commissioner also released the opinion of Messrs O'Sullivan QC & O'Meara. They discount this passage, saying:

> *72. Those instructing us have drawn attention to the reasons of Justice Anderson in Clay v. James [2001] WASCA [sic] 18 at [6] and [11]. In our respectful opinion those passages should be understood in the light of the particular trust deed before the court. ... In our opinion whilst that may (or may not) be the correct interpretation of clause 2 of the deed before the court, the decision is not authority that in a fact pattern of the kind currently being considered, there is usually an implied obligation on the trustee to distribute the trust fund or to otherwise wind up the trust once it has vested.*

107. Thus, if a trust deed properly excluded an obligation to wind up, it seems matters could drift along indefinitely.

108. The continued uncertainty about the meaning of "absolutely entitled", as exemplified by draft ruling TR 2004/D25, presents an opportunity.

109. If the assets, beneficiaries or both, are such that no one is absolutely entitled on the vesting date (absent appointment), it is possible that:

    (a) the same trust continues, albeit now "fixed" for the benefit of those who took in default of any appointment: *Clay v James.*[18]

    (b) no CGT event has occurred.[19]

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18 [2001] WASC 18

19 Draft ruling TR 2017/D10, para 14, *et seq.*

(c) the trustee would continue to administer the trust in the interests of the remaining, fixed beneficiaries.

110. This has favourable implications.

8 Words

111. Some words should never be used.

112. These words are known simply make trouble.

113. If troublesome words are going to be used, they should be defined.

114. Lots of words can be troublesome. I treat them in 2 groups:

(a) Family relationships; and

(b) Other bothersome expressions.

8.1 "Issue" & "heirs"

8.1.1 Issue

115. There is good discussion in Jarman *Treatise on Wills* (8th Edition).

116. Jarman says that "issue", properly, means descendants of every degree.[20]

117. However, the word "issue" "may be, and frequently is, explained by the context to bear the restricted sense of 'children'".[21]

118. The difficulty "often arises from the testator having used the words *issue* and *children* synonymously, rendering it necessary therefore, in order to avoid the failure of the gift for uncertainty, that the prevalency of one of those respective terms should be established".[22]

[20] Jarman, above, p 1581

[21] Jarman, above, p 1587

[22] Jarman, above, p 1593

119. Preferably do not use the word "issue". Sometimes it is a useful word, but then it should be defined as, for example, including "issue of every degree". If the draftsman means "children", use that term instead.

8.1.2 "Heirs"

120. In fact I could mention a number of uncertain expressions about family and relatives. The word "heirs" caused difficulty in *Clay v Karlson*.[23]

121. (However, pretty much everything caused a problem in that litigation, including use of the word "spouse": *Clay v Clay*.[24])

8.1.3 "Family", "relatives"

122. Fortunately, we rarely see these expressions undefined in professionally drawn documents.

8.2 Other annoying words

123. There are 171,476 words reputedly in the OED (2ed).[25]

124. There are therefore enough words for us to have some peeves.

125. As examples, only, I mention the following:

(a) "deem" –

(a) sometimes we say "deemed" only to emphasise some point as being "true", or found to be true. This meaning is colloquial, but troublesome if confused with the technical usage.

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23 (1998) 19 WAR 287

24 Unreported, BC9601043

25 Refer https://en.oxforddictionaries.com/explore/how-many-words-are-there-in-the-english-language

(b) true deemings cause difficulty.[26] No draftsman can remember, let alone tell you, how far something deemed to be something else for a particular purpose is meant to carry over to another clause.[27]

(b) "shall" – Piesse *The Elements of Drafting* (8th Edition) has a whole chapter on "shall". I like the word. But it must be used carefully. It should be made plain whether it is declaring the case or condition upon which something is to occur, or whether it is referring to something in the future, or both.

(c) "and/or" – This is the very work of the devil. Garner *A Dictionary of Modern Legal Usage* (2nd Edition) devotes one page to it, in an otherwise packed and succinct volume. Mr Garner says:

> *A legal and business expression dating from the mid-19th century, and/or has been vilified for most of its life – and rightly so. The upshot is that "the only safe rule to follow is not to use the expression in any legal writing, document or proceeding, under any circumstances." ...*

126. In a recent matter in which I was involved, I was encouraged by one party to look at findings seriously made by a previous decision maker, about the state of mind of a man who was criticised by that decision maker. The previous decision maker found, however, that the man had been "dishonest and/or reckless". I still have no idea what that previous decision maker's actual decision involved.

9 Appointors

127. The key to undoing 5 NZ trusts, recently, was the appointor.

128. I do not suggest abolishing appointors, guardians, protectors, and the like.

129. I suggest more care in conferring powers.

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26 Pearce & Geddes *Statutory Interpretation in Australia* (8th Edition) paragraphs 4.45-4.46.

27 See the article in Garner *A Dictionary of Modern Legal Usage* (2nd Edition), p 254

9.1 Pugachev

130. There has been debilitating litigation in England and New Zealand concerning New Zealand foreign trusts established by Mr Pugachev. Mr Pugachev is being pursued by someone in the position of a liquidator of Mr Pugachev's now-insolvent bank.

131. Precise details are difficult to discern, and doubtless this litigation has a way to run yet. I particularly mention that, because a number of the people involved, and particularly the New Zealand practitioners involved, are entitled to see the litigation play out.

132. In short, Mr Pugachev is married to (but estranged from) Ms Tolstoy, with whom he has children. It appears he nevertheless desired to make provision for them by setting up five New Zealand foreign trusts using the services of a well-known, small firm in Auckland. The assets in the trusts were largely foreign to New Zealand, and it is fair comment I think that Mr Pugachev was setting up those trusts following enormous difficulties he had faced with expropriation of assets in Russia.[28]

133. The English courts recognised a Russian judgment. They made a freezing order. After several other steps, it became clear that Mr Pugachev's NZ trusts were within the scope of the then orders.

134. Mr Pugachev found it convenient, by July 2017, to remain in France. But Ms Tolstoy carried the weight of the argument for the NZ trusts' viability, in the face of a claim that the trusts' property was simply Mr Pugachev's.

9.2 Structure

135. In essence, there were 5 discretionary trusts, each with a NZ company as trustee. The shares were held by 2 NZ solicitors. The directors included the solicitors, and certain others who might (I speculate) have been associates of the family. The discretionary

28 See the most recent case, *JSC Mezhdunarodniy Promyshlenniy Bank v Pugachev* [2017] EWHC 2426 (Ch).

beneficiaries included Mr Pugachev, Ms Tolstoy, and some children and named relatives (at various times).[29]

136. There was a protector clause. Mr Pugachev was first named protector, with provision for succession to a named relative.[30]

137. The NZ High Court had found that the powers of the protector were to be exercised in the best interests of the beneficiaries.[31] On different evidence, the High Court of England and Wales found that the powers were not fiduciary.[32]

138. The powers were (using one trust deed as an example):

> *"4 Protector*
>
> *4.1 The Protector shall be:*
>
> *(a) Sergei Victorovitch Pugachev while he is living and not Under a Disability and after death of Sergei Victorovitch Pugachev or while he is Under a Disability Victor Sergeyevitch Pugachev;*
>
> *(b) Subject as above such person as the Protector for the time being may appoint in writing, revocably or irrevocably;*
>
> *(c) If there is no Protector for the time being such person as the Trustee may appoint in writing, revocably or irrevocably.*
>
> *4.2 Resignation and Disability*
>
> *Any Protector may resign by notice in writing to the Trustee, If any Protector being a natural person is Under Disability or is bankrupt or being a body corporate is in receivership or liquidation, that Protector shall automatically and immediately cease to serve as a Protector.*
>
> *4.3 Information*
>
> *The Protector shall have the right to request information from the Trustee and such requests shall not be unreasonably refused.*
>
> *4.4 Remuneration*
>
> *The Protector shall be entitled to reimbursement of reasonable expenses incurred as part of their role as Protector and any such remuneration fir their services as may be reasonable having regard to their duties and responsibilities as Protector.*
>
> *4.5 Protector's Consent Required*
>
> *Notwithstanding any provision in this deed conferring an absolute or uncontrolled discretion on the Trustee, the following powers and discretions*

29 At [15]

30 At [15]

31 *Kea Trust Company v Pugachev* [2015] NZHC 2412, [51]

32 [2017] EWHC 2426 (Ch), [267]

which are vested in the Trustee by the provisions of this deed, shall only be exercisable after the Protector has been given fourteen (14) days prior written notice and the Trustee has received the prior written consent of the Protector:

(a) Specification of a Date of Distribution that is earlier than eighty (80) years (clause 1.1(b));

(b) Distribution of income and/or capital of the Trust Fund (clauses 5.2, 5.3, 5.4 and 5.5);

(c) Investment of the Trust Fund (clause 9);

(d) Declaring that any person shall cease to be a Discretionary Beneficiary and/or shall not be capable of being a Discretionary Beneficiary (clause 12);

(e) Variation of this trust deed (clause 13.1); and

(f) Releasing and revoking any power conferred on the Trustee by this deed (clause 14.1).

4.6 Power for Protector to direct sale of residential property

(a) The First Protector may by written instruction to the Trustee direct the Trustee to sell the residential property forming part of the Trust Fund on such terms and conditions as the Protector shall direct and the Trustee shall act in accordance with such direction. The net proceeds of sale shall then be held upon the trusts declared in clauses 5.2-5.5 of the Trust Deed (but with power thereafter with the written consent of the Protector to purchase a further residential property).

(b) If the First Protector has died or is Under a Disability the Protector for the time being may also instruct the Trustee in writing to sell the residential property PROVIDED

(i) such instruction may only be given if all the children born to Alexandra Tolstoy and the First Protector have attained the age of 21 years or subclause (d) applies; and

(ii) The Trustee has pursuant to clause 1.1(b) of the Trust Deed (with the written consent of the Protector) declared an earlier Date of Distribution of the Trust Fund TO THE INTENT that the net proceeds of sale of the residential property will be distributed pursuant to clause 5.5 of the Trust Deed.

(c) The Protector may also exercise the power conferred by clause 4.6(a) above if he is satisfied that Alexandra Tolstoy and her children are in financial distress and that it is desirable that the residential property be sold so that clauses 5.2-5.4 of the Trust Deed can take effect.

(d) The provisions of clause 4.6(b) also apply if more than two thirds of the trust beneficiaries (being those beneficiaries named or described in clause 1.1(c) of the Trust Deed) advise the Trustee in writing that they wish the residential property to be sold. If a trust beneficiary is under the age of 18 years the Trustee may accept written instruction signed on behalf of such beneficiary by its legal guardian."

139. Birss J, in a complex and lengthy judgment concluded:

453. Mr Pugachev is the settlor of all the trusts. All the assets in the trusts were his beneficially before they were transferred. That includes the assets transferred in Victor Pugachev's name. Victor was acting as Mr Pugachev's nominee.

> *454. None of the Protector's powers in the trust deeds in this case are fiduciary in nature. They are purely personal powers which may be exercised selfishly.*
>
> *455. When Mr Pugachev is Protector (and to the extent Mr Pugachev is under a disability, when Victor is Protector) the true effect of all the trust deeds in this case, properly construed, is to leave Mr Pugachev in control of the trust assets. Mr Pugachev is the beneficial owner. They amount to a bare trust for Mr Pugachev.*
>
> *456. Mr Pugachev's intention in setting up all five trusts was to retain control of the assets but use them as a pretence to mislead third parties by hiding his control. No other natural person involved in setting up the trusts (neither Mr Liechti, Ms Dozortseva, Ms Hopkins nor Mr Patterson) had an intention independent of Mr Pugachev's. Accordingly if the interpretation of the true effect of the deeds is wrong, such that they would have the effect in law of divesting Mr Pugachev of his beneficial ownership of the trust assets, then they are shams and should not be given effect to.*

9.3 Implications for Australian practice

140. How many trusts are in circulating where:

(a) The effective settlor is a beneficiary;

(b) The powers of appointor, even if not as extensive as here, nevertheless can be exercised selfishly, and to remove an unco-operative trustee; and

(c) The trustee is under the thrall of the effective settlor?

141. Birss J said:

> *268. The fundamental reason for why I reach this conclusion is having regard to the extensive nature of the Protector's powers combined with the fact that the First Protector is the settlor of all the trust assets and is also one of the named Discretionary Beneficiaries. If such extensive powers had been conferred on a third party as protector, with provisions barring that person from being a beneficiary, then I can see that a different result might follow but the fact it is a beneficiary on whom these powers are conferred militates against the idea of a limitation. One would expect a beneficiary ordinarily to be entitled to act in their own interests. Conversely if less extensive powers were conferred on a beneficiary/protector then again one might arrive at a different result but that is not this case.*
>
> *269. The fact that Mr Pugachev is also the settlor reinforces the conclusion. Another different case would be if the settlor did retain these powers as Protector but was excluded from being within the class of Discretionary Beneficiaries. The purpose of conferring those powers in that case could well be to allow the settlor to retain a watchdog role because they would be unable to benefit personally from the exercise of the powers. But that is a long way from the facts of this case.*

9.4 Drafting

142. Drafting and form (such as having an independently *owned* trustee company) evidently only get you so far.

143. But an immediate point is that the appointor should be denuded of some power:

    (a) The powers should be fiduciary;

    (b) If the kinds of extensive powers are held, as in *Pugachev*, they should be divided among different people. (But, fundamentally, Mr Pugachev should have trusted his trustees. You either have your foot on the stash, or off the stash.))

144. Amendments of deeds, to remove or alter appointor provisions have been problematic, depending on the width of the amendment power, and the purpose in making an amendment.

145. If the trust property actually belongs beneficially to the settlor, as in *Pugachev*, the revenue consequences, as well as estate planning consequences, do not bear thinking about.

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