

## HOW TO MAKE YOUR TRUST STRONGER

This paper offers a few thoughts on how you may make your family trust stronger.

### Focussed terms may mean that you can relax some control

The Achilles heel of the modern trust is the extensive control settlors often exercise over its administration. In some cases, this control is derived from powers reserved to the settlor by the trust instrument. In other cases, control is asserted irrespective of the trust deed. In both cases the settlors treat the trust assets as their own. The courts frequently refer to the incidents of control whereby the settlor retains power. This list is included to enable you to consider whether your trust may be stronger if you relinquish some of the powers that may have been retained until now.

Releasing control to others may indeed make the trust appear stronger but this must always translate into an administration which accords with the terms of the trust. It is important that the terms of the trust also reflect closely the duties and discretions and priorities that the trustees will be asked to exercise.

Everyone associated with the trust administration must be supremely careful not to allow (either by conduct, or by word or by neglect) any unintended expectation to arise or develop on the part of any relative, any beneficiary, or any person associated in any way with the trust property. Failure to take such care risks trust property becoming vulnerable to claims disaffected spouses or partners.

### Settlors as Primary Beneficiaries

Inevitably the settlors will also be discretionary beneficiaries of the trust. The settlors' entitlements as beneficiaries will be made more certain if the trust deed describes them as "primary beneficiaries". This directs the trustees to exercise their discretion principally in their favour. The effect of this is to convert the *spes* (i.e., a mere hope of benefiting from the trust assets) enjoyed by the usual discretionary beneficiary into a something approaching a *res* (i.e., a property right in respect of the assets). This can have far-reaching consequences if the trust is challenged, especially by other discretionary beneficiaries. Although the possibility of a dispute with the settlor may be remote, the appointment of children as primary beneficiaries could render the trust vulnerable to constructive trust claims. See *below for more comment on primary beneficiaries*.

### Settlors as Trustees

The settlors may also be trustees of the trust. This entitles them to make all of the decisions relating to the trust's administration. There may be an independent trustee, but this safeguard is largely illusory if (as is generally the case) the settlor has the power to appoint and remove trustees, and the independent trustee can be shown not to have fully participated in decision making.

### Settlors as Trustees and Beneficiaries

Settlor Trustees often have wide discretion in regard to both the income and capital of the trust. They may even have the power to vest all of the income and capital in the settlors as primary or eligible beneficiaries.

## Primary Beneficiaries

Your trust will be more likely to achieve its purpose if primary beneficiaries are carefully chosen and recorded. Primary beneficiaries are people who will usually be entitled to undistributed capital and income on winding up of the trust and, in most discretionary trusts, will include the immediate family of those for whom the trust is being set up. There are also general discretionary beneficiaries, who usually include the primary beneficiaries as well as other people set out in the trust deed (including related companies and trusts). Equity is equality. To dispel this presumption, it is important to choose the primary beneficiaries carefully, and, to administer the trust accordingly.

In modern trust deeds, there will often be two classes of beneficiaries: primary beneficiaries and general beneficiaries. Primary (or named) beneficiaries will usually have an aggregated equitable proprietary interest in the trust assets (often termed "beneficial ownership" of trust assets). General beneficiaries will often be within a specified "class" of wide and indeterminate scope (i.e. such as issue, extended family members, etc). The trustee will have discretion as to whether to distribute to general beneficiaries. Such beneficiaries have no legal or equitable right to the trust property; rather they have a mere expectation or a hope that the trustee exercises their discretion in their favour. Put another way, they have no more than the equal right to be considered as a potential recipient of distributions from, and an equal right to the due administration of, each relevant trust.

## Confidentiality and the Memorandum of Wishes

The principle advantage of recording your wishes in a separate memorandum is that it may be retained by the trustees as a confidential document. If the wishes need not remain confidential, then consideration should be given to giving them stronger force by recording them in the actual trust document.<sup>1</sup>

## Are your trustees doing the job?

To those who have a settlor couple as the sole trustees, there are succession issues to be considered. Who takes over when one person dies? The immediate appointment of an additional trustee in an honorary capacity will not help. But provision can be made for a later appointment to take effect, or for the naming of "appointors" who can exercise certain trustee discretionary functions so that the trust does not risk failing by being left with a single trustee who is also a discretionary beneficiary.

In trusts which already have an additional or a professional trustee, it is now not just good practice but essential to require that all trustees be actively involved in trust management. In this way it will be clear that the trust property is not managed by one person as if it were his own.

## Which Beneficiaries should have the most rights?

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<sup>1</sup> Lord Rodger, in the House of Lords judgement on legal advice privilege spoke eloquently on the subject of confidentiality: *Three Rivers District Council & Ors v. Bank of England* [2004] UKHL 48, [2004] 3 WLR 1274, [2005] AC 610 [55] Despite its long pedigree the Court of Appeal in this case appear to have been less than enthusiastic about the very notion of legal advice privilege. In particular, they thought that it was not clear why it should attach to matters such as the conveyance of real property or the drawing up of a will: [2004] QB 916, 935, para 39 per Lord Phillips of Worth Matravers MR. I do not share these doubts. A client's financial or tax position, or the financial or tax position of members of his family, may well be relevant to the way in which he asks his solicitor to structure a property transaction. Or else, for example, the client may have private worries about his son's ability to fend for himself which explain why he conveys a more valuable property to his son than to his more able daughter. People have a legitimate interest in keeping such matters private. The case for confidentiality is, if anything, even more obvious when it comes to the preparation of a will. Rightly or wrongly, the provisions are often shaped by past relationships, indiscretions, experiences, impressions and mistakes, as well as by jealousies, slights, animosities and affections, which the testator would not wish to have revealed but which he must nevertheless explain if the solicitor is to carry out his wishes. Divulging the provisions during the testator's lifetime or disclosing the reasons for them after the testator's death could often cause incalculable harm and misery. The public interest lies in minimising the risk of that happening. In these circumstances it is, in the words of Sir George Mackenzie, Works vol 2, p 45, the interest of the commonwealth "not to unseal the Secrets of private Persons and thereby to render all Trust and Commerce suspect."

Most discretionary beneficiaries are unable to compel a trustee to exercise discretion in their favour because that would be contrary to the notion that “discretion” exists. This does not mean that beneficiaries under discretionary trusts lack rights, but the nature of the trust instrument and the description of the classes of beneficiaries will provide parameters to the rights and relief available.

As set out elsewhere in these papers, a person who may not be even a remote discretionary beneficiary may acquire constructive trust rights against the trust property, especially where they have some relationship with some trust property or with a settlor or trustee or other person associated with the trust.

It is important to ensure that your trust deed spells out what you expect to be provided to the primary beneficiaries, even although the actual benefits remain within the trustees’ discretion.

#### **WHAT SHOULD YOU DO?**

You should consider whether any of the above considerations apply to your family and whether the trust you may already have effectively safeguards your family property.

Varying an existing trust can often be achieved within the terms of the original settlement without application to the court. Often a resettlement provision is already included in the trust instrument. At other times the discretion to change beneficiary rights may be exercised to vary entitlements. The extent of the variation that is possible will be limited by the terms of the present trust, and may be affected its indebtedness to settlors, banks and beneficiaries.

If you would like more information on anything here, if you would like to discuss forming a trust, or if you think that your present family trust may no longer be set up to achieve what you want, please call us

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