



Is your Trust Effective Against claims on You?

If you regard the assets in your trust as being at your disposal in the same way as the balance in your bank account, then most likely your trust will not be effective to shelter your assets. The assets held in trust may be attacked by:

- a. an ex-spouse;
- b. business creditors.

For many people these are the very two possible claimants that they wish to shelter their assets from by way of their trust. My pick is that one in four trusts would fail a challenge made on the trust assets by a disgruntled ex-spouse or creditor.

How can I ascertain whether my trust offers effective protection?

Trust deeds need to balance the flexibility that most people want to retain over the trust assets against the rights of the beneficiaries of the trust. The trust deed must not confer on you absolute disposing power over the assets in the trust. If it does, then potentially you do not have a trust at all. You can ascertain whether your trust appropriately achieves that balance by asking yourself the question whether your trust grants you power to do as you please with the trust assets without having to weigh the rights of others to those assets.

This needs to be done in the context of specific provisions in the trust deed that give you control over the identity of the trustees and beneficiaries, to accelerate the date of distribution and to exercise powers of distribution of capital and of income.

The Consequences

The determination of the Supreme Court in a case between Mr and Mrs Clayton a few years ago, was disastrous for Mr Clayton. The value of the assets that he had placed in trust was attributed to him. Consequently, matrimonial laws entitled his ex-wife to precisely 50% of the entire asset base of the trust. Mrs Clayton's reward from the matrimonial estate jumped from a paltry sum of \$30,000 awarded under the pre-nup agreement that she had entered into with her husband to a 50% share of trust assets of \$28m.

Equally, if it had been the Official Assignee attempting to bust open Mr Clayton's trust (had Mr Clayton become bankrupt – he didn't), likely the Official Assignee would have obtained 50% of the trust assets for recoupment of Mr Clayton's creditors (up to the amount owed to them, of course).

What can be done?

Most trust deeds contain a power of variation. For those that do, the trust can be varied to make it effective by restoring an appropriate balance between the interests of the settlor on the one hand and the rights of the beneficiaries on the other hand. For trusts that do not contain a power of variation, the same result can be achieved under the new Trusts Act upon that Act coming into force on 30 January 2021.

What should I do?

All trusts need to be reviewed to ensure their compliance/suitability with the new Trusts Act. I have previously written about the steps needed to do so. I suggest you combine a review of your trust deed that is demanded by the new Trusts Act with a review to ensure it has the necessary balance of rights and responsibilities to enable it to survive a trust busting challenge. I am happy to review your trust for both its suitability under the Trusts Act and to ascertain its effectiveness against a challenge by an ex-spouse or by a creditor and to make such changes as may be necessary for you on a fixed fee arrangement. Please see my details below in order to contact me.

Further Detail

For those readers who are interested, I offer a little more detail.

A valid question to ask is what were the offending provisions in the trust deed established by Mr Clayton that failed him? The question might also be asked whether those provisions were so unusual that in nearly all cases there is not in reality a problem.

Dealing with the second question first, it is true that the trust deed established by Mr Clayton was highly unusual. That deed was at the extreme end of the spectrum for trusts. Notably, rights were conferred on Mr Clayton as Principal Family Member, and not as trustee, thereby circumventing duties and obligations that apply only to trustees. Nevertheless, the Supreme Court decision established principles that will inevitably relate to many trusts and which may disavow them (in my view, as many as one in four trusts may well suffer that result).

The offending provisions are the amalgam of:

- a. the power to hire and fire trustees;
- b. the power to appoint and remove discretionary beneficiaries, including by appointing oneself in that capacity;
- c. the power to accelerate the date of distribution, thereby defeating the interests of the Final Beneficiaries, whose rights are predicated on the capital not being distributed before the Vesting Day;
- d. the power to change any provision in the trust deed relating to the management and administration of the trust;
- e. the power to resettlement the trust on a trust which includes any one or more of the discretionary beneficiaries;
- f. direction in the trust deed that it be interpreted in a manner broadening powers and restricting liability of the trustee;
- g. provision in the trust deed that entitled the trustee to exercise any power or discretion in the trustee's own favour without the need to consider the other beneficiaries.

This amalgam of powers entitled Mr Clayton at any time to appoint all or any of the trust capital and income to himself at the exclusion of and without consideration of the other discretionary beneficiaries. He was not

constrained by fiduciary duties, no fraud on exercise of a power could be made out and he had absolute disposing power. The Supreme Court determined that there were no limitations whatsoever on the powers vested in Mr Clayton by the trust. Their decision establishes that for a trust to be effective, the trust deed must contain appropriate limits on individual's powers.

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