

SPEAKMAN LAW



Is your Trust still Needed?

Is it still effective?

*Are changes needed on account of
the new Trusts Act?*

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1 Overview

- The advantages offered by trusts are far reduced from what they used to be. For many, there is no longer any need for a trust at all. I encourage you to assess whether your trust is still needed and whether the need for its retention outweighs the steps involved in administering it under the new Trusts Act and making amendments to your trust to fit with that Act.
- The door has been opened for trust busting. Though creditors and ex-spouses might only bust open a trust in exceptional cases, it is advisable to test the effectiveness of your trust to overcome a challenge.
- The Trusts Act 2019 imposes obligations on trustees that include the obligation to write to the beneficiaries. For trusts that are to be retained, it is generally advisable to amend the trust deed so as to limit this obligation to immediate family members or other intended recipients. The Trusts Act also imposes obligations on trustees to hold a copy of all "core documents" for the trust. The list of core documents is longer than you might expect, see below.
- Recommended amendments to your trust deed to ensure it fits well with the new Trusts Act include an amendment to exclude some or all of the default duties imposed by the Trusts Act. This is particularly important to ensure limited liability is not lost by reason of gross negligence in failing to meet those duties.

2 Assessing whether to Retain your Trust

The two primary purposes for family trusts are:

- Sheltering assets from creditor and ex-spousal claims; and
- Providing for family members.

If in your business you are exposed to creditor claims, having assets held in a trust is definitely advisable. This does not afford absolute protection for those assets from third party claims but it will go a long way towards it. In this category are professional directors, sole traders and individuals who are directors of a trading company and who carry the risk of a claim against them for breach of directors duties. For many though, the risk of a creditor claim is small and is adequately covered by limited liability under a company or limited partnership structure.

Similarly, if you have assets from the period prior to your marriage, retaining those assets in a trust that was established prior to the marriage is advisable. Again, this will offer good protection against a claim by an ex-spouse in most cases. Equally, however a robust relationship property agreement that categorises pre-marital assets as separate property will achieve the same result.

Other advantages formerly made available by the use of a trust have all but disappeared. For example:

- a. the purpose of sheltering assets from estate duty disappeared with the abolition of estate duty and I see no real prospect of estate duty returning in my lifetime;
- b. the tax rate (33%) is set at a level considerably higher than that for companies (currently 28% and likely to lower if alignment with international norms is sought), hence a trust offers no tax advantage, as against a company, as a trading vehicle;

- c. income splitting via a trust is now severely curtailed by tax rules (as are arrangements to distribute trustee income via tax loss entities);
- d. means testing for various Government subsidies encompasses clawbacks that constrain use of a trust to assist accessing Government subsidies.

A material tax advantage of a trust does remain, however, in the form of the 33% trust tax rate sitting well below the top marginal income tax rate. This encourages use of a trust as a shareholder of privately owned companies in order that company earnings ultimately suffer only a 33% tax impost.

In summary, you should retain your trust where:

- a. the nature of your business exposes you personally (including as a director of a trading company) to creditor claims; or
- b. you are concerned that pre-marital assets are not protected by a relationship property agreement; or
- c. the trust achieves the purpose of providing for family members and your Will does not adequately facilitate that; or
- d. the trust serves a useful purpose as shareholder of a trading company in limiting the ultimate tax impost on company earnings to 33%.

If none of these circumstances apply to you, then likely your trust serves no further purpose and will entail administrative hassles that you can do without.

3 Is your Trust still effective?

If you regard the assets in your trust as being at your beck and call, then most likely your trust will be ineffective against a claim by a creditor or ex-spouse. This was the case in *Clayton v Clayton* where Mrs Clayton successfully pursued assets in a trust established by her ex-husband during the time of her marriage to him.

Mrs Clayton's successful claim recognised the near absolute powers that Mr Clayton had preserved for himself to control the trust. He had the power to hire and fire trustees (which is not unusual), the power to appoint and remove beneficiaries (also not unusual), the power to accelerate the date of distribution (likewise not unusual), the power to appoint himself as beneficiary to the exclusion of others, the power to do each of the above without peril of a self interest claim and most problematic of all, the ability to exercise these powers without the hindrance of fiduciary duties. A lesser combination of these elements may not have been problematic for Mr Clayton; their combination in total was fatal.

In short, a trust needs to ensure the powers retained by the settlor are appropriately balanced against beneficiaries' interests.

4 Obligations for trustees under the Trusts Act 2019

- a. There is a stated presumption that trustees must write to all beneficiaries to notify them of "basic trust information". This comprises the fact that the person is a beneficiary, who the trustee is, the trustee's contact details, and details of changes in trustees. The presumption also requires trustees to notify beneficiaries that they have the right to request a copy of the terms of the trust and other information about the trust.

Many trustees simply do not want to do this. What do they do?

Winding up the trust is one solution. Another is to insert into the trust deed a provision expressing the settlor's intention (assuming the settlor is still alive and this matches his or her intention) that only primary beneficiaries receive this information. Primary beneficiaries can be defined to suit and are often limited to immediate family members only.

- b. Each trustee is required to keep a copy of all core documents. The only exception here is where you know for certain that another of the trustees holds them and will make them available on request.

The core documents are:

- i. The trust deed and any and all variations to it;
- ii. Records of the trust assets, liabilities, income and expenses of the trust;
- iii. Records of trustee decisions during your trusteeship;
- iv. Written contracts for the trust during your trusteeship;
- v. Accounting records/financial statements during your trusteeship;
- vi. Documents appointing or removing trustees or beneficiaries;
- vii. Any letter or memorandum of wishes of the settlor;
- viii. Any other documents necessary for the administration of the trust;
- ix. Any of the above documents that were kept by a former trustee which have been passed onto you as trustee.

- c. Other obligations exist, including in the case of advisors the obligation to advise a settlor of the existence and meaning of a future limitation clause in the trust deed (if there is one, and there usually is) and exclusion of any default duties.

5 Recommended Changes to Trust Deed

- a. Exclusion of Default duties: Unless expressly excluded, each of the default duties in the Trusts Act will automatically apply. My recommendation is to negate them (bar one). If any others are wanted, these can be specifically inserted into the deed. The key ones are the duty:
 - i. Not to exercise any power for one's own benefit. Consider a family home owned by the trust and occupied by the trustee. This default duty makes that problematic;
 - ii. To invest prudently – depositing funds in a bank earning low interest as opposed to returns offered by managed funds might trigger "gross negligence" and, by extension, loss of limited liability;
 - iii. To act for no reward (a problem for professional trustees);
 - iv. To act unanimously – making it difficult to resolve disputes.
- b. Other recommended changes include:
 - i. Excluding gross negligence from a trustee's limitation of liability;
 - ii. Extending the life of the trust (to 125 years), subject to contrary provisions in the deed;

- iii. Modifying a trustee's powers of management of trust property and carry out the trust to suit your purposes. For example, consider whether you wish to empower the trust to make distributions to beneficiaries for their education, well being, maintenance or advancement on an unfettered basis, or subject to a monetary threshold, and if made in favour of one beneficiary, whether a "hotchpot" to apply to balance this up in favour of other beneficiaries.

6 What next?

My recommendation is to review your trust deed in light of these points. As a first stage, consider whether there remains a need for the trust. If there is such a need, you should then address the changes that are needed to it to fit with the Trusts Act 2019. So long as the deed grants the trustees the power to do so, this is relatively simple.

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