

The Problematic Role of the Trustee Services Companies

A recent eConnect article focused on the cases of *Selkirk v McIntyre* and *Church Property Trustees v Attorney-General and The Great Christchurch Buildings Trust*. We will not traverse those cases again suffice to say that, in each of those cases, the independent trustee was exposed to significant personal liability. In the *Selkirk* case, the liability was in respect of a tax debt. In the *Church Property Trustees* case, it was for liability incurred by the trustees as a result of actions outside the scope of the Trust.

Given such cases, who would now want to act as an independent trustee of any trust?

Although most trust deeds contain provision for a trustee (whether they are independent or not) to be indemnified from the assets of the trust, that indemnity will be of little value if there are no assets in the trust to call upon.

Accordingly, many professionals are now far less willing to accept appointments as independent trustees. Many are, however, happy to continue to provide services as an independent trustee by way of a corporate trusteeship. That involves a company acting as the trustee with the professional or a firm of professionals being the directors and shareholders of the company.

Before reviewing the different models of corporate trusteeship, it is important to recognise the benefits that the involvement of an independent trustee can bring. Just because potential liability may attach to an independent trustee does not necessarily mean that the concept should be discarded.

Most trust deeds require the unanimous consent of all trustees before any actions can be undertaken on behalf of the trust. The involvement of an independent trustee can therefore bring a reality check to the actions of other trustees who may not otherwise be acting in the best interests of a trust's beneficiaries. An independent trustee will of course need to make sufficient enquiry of any proposals. They will add little value if they are simply regarded as a rubber stamp to the actions of the trustees that are not so independent.

Traditionally, many lawyers or accountants have acted as independent trustees. As trustee decisions usually need to be unanimous, such professionals have often been involved at an early stage of a transaction undertaken by a trust in a dual capacity as professional and trustee. Such advice and input can add significant value and prevent costly mistakes. Advice from an accountant or a lawyer prior to the commencement of a subdivision is a classic example.

As mentioned, there are different models of corporate trusteeship. Some organisations that provide corporate trustee services form a company which acts as a trustee for a number of its clients.

The case of the *Commissioner of Inland Revenue v Newmarket Trustees Limited* has clearly shown that this is not good practice.

In that case a firm of lawyers had formed a single company to act as an independent trustee to its clients. The company was a trustee of over 100 trusts.

One of these trusts owed money to the Inland Revenue Department. The trust had no funds to pay the debt. Similarly, the co-trustee could not meet the liability so the Department turned to the corporate trustee for payment. As the corporate trustee could not meet the payment, the Department submitted that the corporate trustee should be put into liquidation. The Court of Appeal agreed and the company was put into liquidation. As that corporate trustee was also the trustee of over 100 other trusts, the firm of solicitors was therefore left with the administrative nightmare of having to remove the liquidated company from its role as trustee of all of the other trusts.

To avoid the problems as were encountered in the *Newmarket* case, many organisations that offer trustee services now incorporate a new company to act as a corporate trustee for each trust. Some question marks, however, still remain around the extent of a director's personal liability even when this model is used.

There are a number of duties imposed upon directors under the Companies Act 1993 (and for that matter under other legislation) such as the duty to act in good faith and to act in the best interests of the company, the duty to not engage in reckless trading or whilst trading insolvent and the duty to exercise the care, diligence and skill that a reasonable director would exercise. Directors could face personal liability if they breach those duties.

The Court of Appeal in the *Newmarket* case also suggested that the liquidator should examine the actions of the directors of the corporate trustee and stated that the directors would 'still have the opportunity to persuade the liquidator not to apply to the Court for an enquiry into their conduct'. The conclusion that can be drawn from those comments is that the directors should face personal liability should the circumstances warrant it.

The Law Commission has also examined the issue in its *Review of the Law of Trusts: Preferred Approach*. That paper is the sixth paper in Stage 1 of its wide ranging review of trusts.

The paper calls for an amendment to the Companies Act. It recommends adopting Australian legislation, specifically section 197 of the Corporations Act 2001 (CTH), to ensure that directors of corporate trustees are liable to discharge liabilities incurred by the company acting in its capacity as trustee. Although there are only specific circumstances when such a trustee would be liable, the recommendation if adopted further dilutes the protections that would otherwise be available to a corporate trustee.

The paper also addresses the issue of when a corporate trustee is in breach of its obligations to a trust's beneficiaries. The Commission's preference is to 'introduce a direct look-through with directors of companies acting as trustees being directly accountable to beneficiaries.' This would therefore allow beneficiaries of an insolvent trust to claim personally against the directors of the corporate trustee.

The Commission is to release its final recommendations on Stage 1 in the third quarter of the year. Anyone who is a director of a corporate trustee will no doubt await the recommendations with interest.

Another option for consideration when appointing trustees is the use of a statutory trustee corporation.

The Trustee Companies Act 1967 governs the conduct and status of trustee companies but there is a difference between companies that are trustees and trustee companies or corporations. Section 2 defines what companies qualify as a trustee company and section 3 states that every trustee company shall be deemed to be a trustee corporation for the purposes of the Trustee Act 1956. The Act does not apply to companies that are set up by lawyers or accountants to act as an independent trustee for the trusts of their clients.

Section 2 of the Trustee Act 1956 states that a 'trustee corporation means Public Trust or the Māori Trustee or any corporation authorised by any Act of the Parliament of New Zealand to administer the estates of deceased persons and other trust estates'. The Act provides some advantages to trustee corporations that are not available to individual trustees or companies acting as a trustee.

The Act also places controls and restrictions on statutory trustee companies as to how they charge fees and how they conduct their business.

Beyond the statutory area there are other advantages of involving a statutory trustee company as a trustee of a trust. Statutory trustee companies are truly independent: they are not a family member or a professional acting in another capacity for the family. They are impartial as they have no hidden agenda or 'family politics' to align to. Statutory trustee companies simply fulfil their role as trustee. They have also been in business for a considerable time and offer significant experience. They can also take a long-term view which is important as

many trusts are in existence for generations.

It is interesting to note however that the Law Commission considers 'that the reforms [that they propose] should also generally apply to the statutory trustee corporations, unless they are expressly exempted.' No doubt the Commission's final recommendations will provide further detail as to how they are to be treated.

Given all of the above, and the various options which are available, careful thought will need to be given as to who is to be appointed a trustee. A secondary, but just as important question is what type of trustee will be appointed? The decision is becoming increasingly complex.

The information contained here is of a general nature and should be used as a guide only. Any reference to law and legislation is to New Zealand law and legislation. We recommend that before acting on it, you consult your nearest Lawlink firm.