<u>Trusts</u>
Fall Term 2017

Lecture Notes – No. 12

<u>Administration of Trusts (II)</u>

<u>4. Delegation of Duties (well, really, Delegation of Powers)</u>

→ **See Trustee Act, ss. 20, 27.1.**

Traditionally, and in the absence of express authority in the trust instrument or Will, trustees are expected to perform personally on their obligations that involve such important matters as exercising discretionary powers or making distributions. The difficulty is where the draw the line and whether to begin from a position allowing or disallowing delegation. Equity firmly comes down on an attitude disfavouring delegation consistent with the rather ominous sounding maxim, *delegatus non potest delegare* (a delegate may not delegate).

Trust administration is ultimately a practical business and the law has coalesced doctrine that disallows delegation of ***dispositive duties*** (eg. to distribute the trust property to those entitled to it under the trust) or the exercise of ***fiduciary discretions***. It is a breach of trust for trustees to delegate such discretionary functions and they are liable for any consequent loss.

The prohibition on the delegation of their fiduciary powers does not however preclude the delegation by them of powers to do acts **'merely ministerial'**. Although this distinction between fiduciary powers and ministerial acts is easily stated, the dividing line between those functions which only a trustee may perform and those which may be delegated is not easily drawn. In general, one can say that the trustee may delegate as permitted by the trust instrument or the statute as is reasonable, but must still act personally in matters that are at the core of trusteeship. Judicial supervision of the exercise of discretionary powers divorced from obligations is considered below.

Speight v Gaunt
(1883), 9 App Cas 1 (H.L.), cb, p. 951

The beneficiaries suggested to the trustee that he invest in stocks. The trustee agreed and employed a stockbroker. £15,000 was provided to the stockbroker to effect an agreed-upon investment. The stockbroker misappropriated the funds rather than closing the transaction. The trustee complained but the stockbroker was declared bankrupt. The beneficiaries argued that the trustee should have completed the trade directly with the vendor rather than using the services of the stockbroker as an agent.

In the CA, Lindley LJ observed that:

> [a] trustee has no business to cast upon brokers or solicitors or anybody else the duty of performing those trusts and exercising that judgment and discretion which he is bound to perform and exercise himself.

Thus, the trustee may appoint an agent to do a ministerial act – the trustee is only liable for the acts of the agent based on the trustee's own "willful default". In the House of Lords, the appeal was dismissed accepting the principle a trustee investing trust funds is justified in employing a broker to procure securities authorized by the trust and in paying the purchase-money to the broker, if he follows the usual and regular course of business adopted by ordinary prudent men in making such investments.

[***Does this distinction really make any sense nowadays?*** Indeed, given the complexities of managing money, should we not encourage delegation of many tasks to licensed and insured professionals. Compare to the law in England and Wales under the Trustee Act 2000:

11. - (1) Subject to the provisions of this Part, the trustees of a trust may authorise any person to exercise any or all of their delegable functions as their agent.

(2) In the case of a trust other than a charitable trust, the trustees' delegable functions consist of <u>any function other than</u>-

(a) [power of distribution] any function relating to whether or in what way any assets of the trust should be distributed,

(b) [power to deduct payments from income or capital] any power to decide whether any fees or other payment due to be made out of the trust funds should be made out of income or capital,

(c) [power to appoint trustees] any power to appoint a person to be a trustee of the trust, or

(d) [power to appoint further nominees] any power conferred by any other enactment or the trust instrument which permits the trustees to delegate any of their functions or to appoint a person to act as a nominee or custodian.]

5. The Duty to Invest and the Power to Select Investments

→ **See Trustee Act, s.27**

27.

(1) In investing trust property, a trustee must exercise the care, skill, diligence and judgment that a prudent investor would exercise in making investments.

(2) A trustee may invest trust property in any form of property in which a prudent investor might invest.

The first two sub-sections of s.27 set out above reflect the traditional position that it is of the utmost importance for the trustee to select investments that meet the standard of a 'prudent investor'. In some jurisdictions, the governing statute only permits trustees to select investments approved in the trust instrument or as set out in statute and regulation (a so-called 'legal list' regime); **Ontario uses the 'prudent investor' rule** as do most jurisdictions. Note, however, that **the trust instrument remains paramount and the settlor may fetter the trustee's discretion in selecting investments. Thus, the basic rule is that '…a trustee is not a surety, nor is he an insurer; he is only liable for some wrong done by himself, and loss of trust money is not per se proof of such wrong;'** ***Re Chapman*** **[1896] 2 Ch 763, 775 per Lindley LJ.**

Impartiality: The 'Even-Hand' Principle

The trustee must *select investments prudently*, but must also *deal with the trust property fairly*; that is to say, the trustee must accommodate the differing needs of different classes of beneficiaries. Key to fairness is

(i) inquiring into the differing interests of different classes of beneficiaries, including obtaining advice;

(ii) considering the effect of any proposed course of action on different classes of beneficiaries;

(iii) acting to maintain 'an even hand' and not favouring one class of beneficiaries over another. This is easier said than done, as the interests of these various parties may conflict and one must also keep in mind the intentions expressed by the settlor in respect of preference of interests (and the settlor should be encouraged to guide the trustee in the instrument).

Thus, such matters as diversification of investments raise questions respecting prudent investment but are difficult to review as a matter of ascertaining whether prudence requires diversification.

Re Smith
[1971] 1 OR 584 (HC); varied, 18 DLR (3d) 405 (Ont C.A.); cb, p.990

Here the father left shares in a trust for the son. The son created a trust of part of the shares' income for his mother for life, remainder to the son (but if the son pre-deceased the mother, she would attain his share and vice-versa). The trustee refused to diversify the portfolio to increase income to the mother in preference to leaving the trust property as it was upon the original inheritance. The trustee was inordinately deferential to the remainderman at the expense of his mother and was replaced.

Apportionment Between Capital and Income as Between Beneficiaries

Where the trust property is stock dividends and other corporate-income related assets, they are normally treated in the absence of directions in the settlement as capital (to be used to the benefit of life tenants and remaindermen both) rather than income (for the benefit of life tenants alone); see **Re Waters [1956] SCR 889; cb, p.1002.**

Lottman v Stanford
[1980] 1 SCR 1605; cb, p.994

Background: 'The Rule in Howe v Lord Dartmouth' (1802), 32 ER 56 (Ch)

> There are actually two rules from this case:
>
> (a) where a testator gives his or her residuary personal estate in trust for persons in succession without imposing a sale of the assets of the trust, and the trust property is comprised of wasting or unauthorized investments, then those assets <u>must be converted into authorized investments unless the testator intended that the assets were to remain unsold</u>;
>
> (b) Where such investments as should have been sold are not sold, the investments are treated as if they had been sold – that is, the life tenant is entitled to a fair equivalent of the income that he or she would attained if the investments had been sold.
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> Thus, where there is a *testamentary* trust in respect of *personalty* with a *reversionary interest to successive beneficiaries*, the trustee should normally convert unauthorized investments (eg. high income but risky securities) into authorized investments (eg. a diversified portfolio balancing the needs of the life tenant for income and the remainderman for preservation of the capital) unless the life tenant can show that the testator intended otherwise. Until the property is sold, the life tenant is entitled to a share of income (unless the settlement provides otherwise). Thereafter, the proceeds of the sale are apportioned between capital and income accounts.

In **Lottman v Stanford** the extension of the rule to real property was refused. Per McIntyre J.:

> **The question then arises whether new ground should be broken here and whether the operation of the rule in *Howe v. Lord Dartmouth* should be extended to real property.** Wilson J.A.'s views are expressed in her judgment and reproduced above. I am not, however persuaded that we should on this point venture into the field of judicial legislation so boldly. **To begin with, the restriction of the rule in Howe v. Lord Dartmouth to personal property is itself a rule of long standing. It must be presumed that those engaged in the preparation of wills and the settlement of trusts under wills know and understand, and have known and understood, its operation and effect and have planned and set in motion many trusts under wills upon the premise that the rule will continue to apply in relation to personal estate but not real estate. Great inconvenience could be caused to many existing trust arrangements by a sudden extension and, in my view, this is not a step which should be taken in this fashion.** This is not to say that old rules may never be changed, but rules dealing with estate administration of this nature should not be changed unless there is a positive reason for so doing. In such case, it should be done by the legislature which at the same time has the power to enact the necessary transition and protective provisions to avoid interference with existing trusts and with rights and obligations acquired and undertaken upon the reasonable expectation that there would be some degree of certainty in the law.
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> Furthermore, it should be borne in mind that we are here dealing with equitable rules relating to estate administration and not with dependents' relief legislation which enables a court to alter testamentary provisions in order to do justice between the testator and members of his family. Other legislative provisions deal with such matters and in Ontario may be found in the Succession Law Reform Act, S.O. 1977, c. 40, particularly ss. 64 to 88. **Courts must not twist rules such as that expressed in the case of *Howe v. Lord Dartmouth* to interfere with testamentary dispositions for the purpose of remedying supposed injustice. I would not extend the rule beyond its present limits. Such a step should be left to the legislature when and if it should consider it advisable.**

The point here is to allow the settlor to plan based on advice (especially in respect of a testamentary disposition) and not to bend the rules when other remedies are available.

Canada Trust Company v. Russell Browne
2012 ONCA 862 (Ont. C.A.)

The issue respecting whether the trustee of a family trust breached the duty to maintain an even hand presented itself somewhat atypically in this case. The trust was settled in 1980 by the settlor who created a trust in favour of his grandchildren and great-grandchildren as part of an estate freeze. In essence, the capital of the trust would be reserved for the great-grandchildren and the income for their parents. In 1984, the settlor died. The trust was varied in 1988, on consent, to allow the income beneficiaries access to capital to assist their children in planning their lives before inheriting large sums through a power of encroachment exercisable in favour of the various family units. The trust continued to grow and was varied again in 1997. Through a complicated formula, the trust became a unit-trust under which the 'income beneficiaries' (grandchildren) would receive a minimum income from the trust but without explicit provisions in the settlement allowing the trustees to encroach on capital to make the minimum payments should present income be insufficient. As it happens, the market dropped and a dispute arose as to whether the capital beneficiaries' interests (that is, the great-grandchildren) were susceptible to 'obliteration' (as they argued) depending on continuing market conditions that effectively required a continuing encroachment on capital. At the end of the day, the variation of the trust and its conversion from a conventional family trust to a unit trust was decisive in allowing the trustee to invest with few restrictions.

Feldman J.A.:

> [101] The appellant submits that the application judge erred in his interpretation of the Trust Deed as Varied by failing to recognize and give effect to the duty of the trustee to maintain an even hand between the interests of the income and capital beneficiaries. The obligation of a trustee to treat different classes of beneficiaries fairly and impartially can only be displaced, contends the appellant, by an express intention to the contrary in the trust deed. In the appellant's submission, the 1997 variation did not displace the duty to maintain an even hand in managing distributions.
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> [102] It is trite law that executors and trustees have a duty to maintain an even hand between the interests of the income and the capital beneficiaries, unless that duty is ousted explicitly or implicitly by the words of the instrument. Justice Middleton described this duty in the following way in *Armstrong (Re)*, [1924] O.L.R. 639 (C.A.), at p. 8:
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> [I]t must be borne in mind by trustees that they are trustees not for the remaindermen alone in disregard of the rights of the life-tenant, nor for the life-tenant disregarding the interests of the remaindermen. Trustees must preserve an even hand as between these two conflicting interests. The duty towards the capital is to preserve it intact. The duty towards the tenant for life is to obtain as large a yield as is consistent with safety and the observance of the law under the instrument of trust as to the class of investment made; and, furthermore, so to adjust the investments that the life-tenant will receive annually his due proportion.
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> [103] However, in a percentage trust, the trustee's duty is not to obtain a large income yield while preserving the capital but, instead, to increase the size of the entire trust for the benefit of both classes of beneficiaries. This includes increasing the capital rather than preserving it, and therefore involves an investment strategy that may include more risk. Because in a percentage trust the trustee is investing to increase the entire value of the trust to benefit all, the issue is not whether the trustee's even hand duty is ousted in respect of the management of the trust's investments. What is disputed is whether the duty has been ousted in respect of the obligation of the trustee to make distributions to the beneficiaries.
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> [104] The role of the even hand duty in the administration of a percentage trust was addressed in the Law Reform Commission's Report on the Law of Trusts. That Report recommends that when trustees administer a percentage trust,

they continue to maintain an even hand in the periodic valuation of the trust and when making the distributions. Specifically, the Report states at p. 303:

> We therefore recommend that the revised [Trustee] Act should contain a provision to the effect that, where trustees are expressly directed by the trust instrument to hold trust assets "on percentage trusts", they shall value the assets periodically and, instead of any income arising from the assets, pay to the person who would otherwise be the income beneficiary a percentage of that valuation in each year of the valuation period. In so doing, trustees should be required to maintain an even hand between income and capital beneficiaries.

This recommendation has not been incorporated into the *Trustee Act, R.S.O. 1990*, c. T.23

[105] There is no clear explanation as to what the Commission means when it says that the trustees should maintain an even hand when valuing the assets and making the annual percentage payment to the income beneficiaries. My interpretation is that the Commission contemplates a periodic review and, if necessary, a re-set of the percentage payable to income beneficiaries, based on the value of the trust assets and on the even hand rule.

[106] The problem here is that in the Trust Deed as Varied, the percentage payable to the income beneficiaries is based on a fixed formula for determining the "Applicable Percentage" and the amount to be paid can never go below the highest amount previously paid in a year. That is why the trustee continues to be obliged to cause the Holding Company to sell assets, if necessary, to meet the obligation to the income beneficiaries, despite the effect on the Trust corpus.

[107] To the extent the Trust Deed as Varied sets forth a minimum annual payment to the income beneficiaries, the even hand duty on the trustee has been ousted, implicitly, by the words and intended operation of the Trust Deed as Varied. The application judge made no error in making that finding.

6. The Duty to Account and Maintain Statements of Account

It is important to distinguish between two words, “accounts” and “an accounting”. Conventionally, “accounts” (or perhaps more properly “Statements of Account”) refer to the creation and development of standard accounting statements. Typical “trustee accounts” include the following statements: Statements of Original Assets, Capital Receipts and Capital Disbursements, Revenue Receipts and Revenue Disbursements, Investment Account, Schedules of Current Assets, Liabilities, and Investment; Schedule of Compensation. An “accounting” conventionally refers to a type of proceeding; that is, the application by the trustee or a beneficiary to have the Court approve the trustee’s accounts as accurate. The proceeding is called a “Passing of Accounts” and is conventional litigation (although usually in the way of a summary trial) with the full application of the costs rules. A “Passing of Accounts” usually arises after the trustee presents his or her statements of account to the beneficiaries together with a “Release” whereby the beneficiaries agree that the accounts are accurate (particularly with respect to the trustee’s actual or claimed indemnification for proper trust expenses) and release the trustee from liability for taking his or her compensation for the relevant period. Where the beneficiaries disagree with the accounts, the matter must be brought into Court for decision. In terms of process, the trustee will usually serve a Notice of Application to pass the accounts, the parties in disagreement will serve and file Objections, and the judge will decide whether each objection is valid. Such a proceeding can be expensive and trustees and beneficiaries alike strive to avoid this sort of litigation.

A trustee must maintain accounts of the trust property and all actions taken in relation to that property. Upon reasonable notice and as far as practicable (in the sense of maintaining the reasons for the trustees acting as they chose to do as confidential), the beneficiaries have a right to inspect the accounts. Not all information needs to be disclosed and the trend is for the courts to consider carefully the nature of the documents held by trustees that are sought by persons interested in the trust on matters such as confidentiality.

Sandford v Porter
(1889), 16 O.A.R. 565 (Ont. C.A.)

MACLENNAN JA:

> It seems to have been thought by the solicitors of the plaintiffs that it was the duty of a trustee, upon demand for an account, to lay aside everything else, and to sit down and make out an account for them, at the peril of a suit for an account and costs. But the law is not so unreasonable.
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> The duty of a trustee or other accounting party is to have his accounts always ready, to afford all reasonable facilities for inspection and examination, and to give full information whenever required; but as a general rule he is not obliged to prepare copies of his accounts for the parties interested. Cases may be imagined where it would be reasonable to require, and when it might be the duty of the trustee to furnish, statements of account, as, for example, when the *cestui que trust* or the principal lives at a distance from where the trust affairs are being carried on, or in a foreign country. In such a case it would be the duty of a trustee to give all reasonable information and explanation's by letter; and even, if requested,

> but of course at the expense of the *cestui que trust*, to prepare and transmit accounts and statements. But every case must depend on its own circumstances, and must be governed by reason and common sense...
>
> The true rule, as I understand it, is laid down by Mr. Lewin, *Law of Trusts*, 8th ed., p. 691, where he says: 'The *cestui que trust* has a right to call upon the trustee for accurate information as to the state of the trust. Thus in a trust for sale and payment of debts, the party entitled subject to the trust may say to the trustees, What estates have you sold? What is the amount of the moneys raised? What debts have been paid? etc. It is, therefore, the bounden duty of the trustee to keep clear and distinct accounts of the property he administers and he exposes himself to great risks by the omission. It is the first duty of an accounting party ... to be constantly ready with his accounts.'

[Thus the beneficiaries may obtain information respecting the existence of the trust, the accounts, but generally have no rights to the decision-making memoranda of the trustees (except where breach of trust is alleged).]

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The Ontario statute is representative of the statutory obligation of the trustee to account:

Trustee Act, R.S.O. 1990, c.T.23, ss. 23, 23.1:

> 23. (1) A trustee desiring to pass the accounts of dealings with the trust estate may file the accounts in the office of the Superior Court of Justice, and the proceedings and practice upon the passing of such accounts shall be the same and have the like effect as the passing of executors' or administrators' accounts in the court.

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Despite the formal process of a judicial audit of trustee accounts through a "Passing of Accounts" such proceedings are relatively uncommon. Most administrations will feature the presentation of informal accounts and reasonable adjustments being made based upon queries and objections. Often, the Passing of Accounts proceedings are not really about a conventional accounting but rather as a timely and efficient manner to bring into Court complaints about trustee misconduct, and the application for accounts to be passed may be brought together with an application to remove and replace trustees and a claim against the trustees for breach of trust and breach of fiduciary duty.

Duty To Inform

In most cases, trustees do their utmost to keep beneficiaries apprised of the developments in the management of the trust particularly as relates to investment and distribution of trust property. In this way, beneficiary complaints are kept to a minimum and trustees may do a better job of administering the trust. At other times, requests for information and documents can be rather more burdensome.

A trustee who administers a trust is sometimes in the unenviable position of having to satisfy beneficiaries who would rather be trustees. In such cases, it seems unfair to the trustee and costly to other beneficiaries for the trustee to constantly face demands for information from a beneficiary seeking ammunition to apply to have the trustee removed. At other times, a trustee has been provided with the discretion to appoint property or encroach on capital and the settlor has provided a non-compulsory “letter of wishes” that he or she wished to be treated as confidential and not have provided to the beneficiaries. In the past, the jurisprudence has been most unhelpful looking at such technical issues as which beneficiaries are entitled to which assets. In *Schmidt v Rosewood Trust Inc.*, a new more principle approach was outlined.

Schmidt v Rosewood Trust Inc.
[2003] AC 709 (Privy Council)

An application for disclosure was brought relating to two settlements of which the applicant’s father had been a co-settlor and under which the applicant claimed discretionary interests both personally and as the administrator of his father's estate. The trustees opposed disclosure on the ground that the petitioner was not a beneficiary under the settlements, and that his father was never more than an object of a power under the settlements and as such had no entitlement to trust documents or information. The Privy Council held that the nature of the right to disclosure of information was not strictly a proprietary interest in the subject-matter of the trust, but rather the inherent jurisdiction of the court to control administration of the trust. Merely by asserting a claim of breach of trust, the beneficiary could not have unrestricted access to documents; similarly, the lack of a proprietary interest in one particular aspect of the trust will not prevent access to information where the interests of justice dictate.

Lord Walker:

> Their Lordships have already indicated their view that a beneficiary's right to seek disclosure of trust documents, although sometimes not inappropriately described as a proprietary right, is best approached as one aspect of the court's inherent jurisdiction to supervise, and where appropriate intervene in, the administration of trusts. There is therefore in their Lordships' view no reason to draw any bright dividing line either between transmissible and non-transmissible (that is, discretionary) interests, or between the rights of an object of a discretionary trust and those of the object of a mere power (of a fiduciary character). The differences in this context between trusts and powers are (as Lord Wilberforce demonstrated in *In re Baden* [1971] AC 424, 448-449) a good deal less significant than the similarities. The tide of Commonwealth authority, although not entirely uniform, appears to be flowing in that direction.
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> However, the recent cases also confirm (as had been stated as long ago as *In re Cowin* 33 Ch D 179 in 1886) that no beneficiary (and least of all a discretionary object) has any entitlement as of right to disclosure of anything which can plausibly be described as a trust document. Especially when there are issues as to personal or commercial confidentiality, the court may have to balance the competing interests of different beneficiaries, the trustees themselves, and third parties. Disclosure may have to be limited and

safeguards may have to be put in place. Evaluation of the claims of a beneficiary (and especially of a discretionary object) may be an important part of the balancing exercise which the court has to perform on the materials placed before it. In many cases the court may have no difficulty in concluding that an applicant with no more than a theoretical possibility of benefit ought not to be granted any relief.