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STRUCTURING TRUSTS TO DEFLECT ATTACK

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INTRODUCTION

In the early 20th century, Pierre Lepaulle, a civilian lawyer and specialist in comparative law, made a comment about use of trusts by English lawyers with which many of you will be familiar. He said:¹

The trust is the guardian angel of the Anglo-Saxon, which accompanies him everywhere from the cradle to the grave. It is at his school and his athletics alike. It follows him mornings to his office and evenings to his club. It is by his side on Sunday at church or in a committee meeting of his political group. It will support his old age until his last day, and then it will watch at the foot of [his] tomb and extend over his grandchildren the light shadow of its wings.

Never has that comment been truer than it is today. It is true not only for Anglo-Saxons but for all persons living in common law jurisdictions. It is particularly true for New Zealanders as we have a distinct fondness for the modern domestic discretionary trust.

If we look at the form and nature of the trust over its 300 or so year history, we can see that the trust has changed almost beyond recognition. As Donovan Waters explained in his paper at the STEP Conference in March², we have seen the settled land trust and the trust for sale. From the middle of the 20th century, we have seen the rise of the modern discretionary trust, which evolved initially through English case law.³

From those early days, practitioners have responded to the economic and social needs of their clients and have, in various jurisdictions, through case law and often with the aid of legislation, extended the boundaries of the trusts and powers in settlements to an extraordinary extent and we, probably, have not reached the end. Indeed, it has said that 'the future development of new and

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¹ Pierre Lepaulle *Traite Theorique et Pratique des Trusts* (1932).

² Donovan Waters "Using Discretionary Trusts in Estate Planning" (paper presented to the New Zealand Trust Conference 2012, Auckland, March 2012).

³ Francis Barlow QC of the English Bar commented recently that, in his view, *Re Manisty's Settlement* [1974] Ch 17 had a profound effect on the development of the modern discretionary trust, particularly forms of offshore settlements. In that case, Templeman J (as he was then) upheld as valid a power vested in trustees to add any person (other than the settlor, his wife or the trustees) to a class of beneficiaries ie a hybrid power vested in trustees. Other significant early developments include the expansion of dispositive powers (eg *Re Gestetner* [1953] Ch 672, *Re Gulbenkian* [1970] AC 424 and *Re Baden's Deed Trusts* (No 1) [1971] AC 424 in relation to certainty of objects for powers and discretionary trusts) and delegation of dispositive powers (*Re Pilkington* [1964] AC 612, *Re Clore's Settlement* [1966] 1 WLR 955 and *Re Hampden Settlement Trusts* [1977] TR 177. *Re Pilkington* established that a power to apply trust capital for the benefit of a beneficiary would authorise the settlement of such capital on trusts for the benefit of the beneficiary even though other persons might incidentally benefit. *Re Hampden* held that an application of capital by trustee will be valid if objectively it can be regarded as for the beneficiary's benefit and subjectively they believe so. Of course, it is usual now to include express power to delegate dispositive discretions.

innovative uses of trusts in commercial applications is limited only by the imagination of the lawyers ...⁴

In *Schmidt v Rosewood Trust Ltd* [2003] AC 709 at [34], Lord Walker commented on this transfiguration of the trust. He said:

It is appropriate to reflect that during the long period covered by these authorities (but especially during the second half of the 20th century) the forms and functions of settlements have changed to a degree that would have astonished Lord Eldon.

As you will know, *Schmidt* is one of the intriguing Russian/East European cases that are so generously helping to support the legal profession in London. Indeed, I read recently in an English legal magazine, *The Lawyer*, that 60% of the current litigation in the High Court in the Strand was of Russian origin. Recently, the *Guardian* newspaper (on 4 September 2012) ran a story entitled 'Top London law firms profit from feuding Russian oligarchs'. Apart from that pecuniary aspect, these cases are contributing some new and exciting case law in Equity and trusts. For example, in the *JSC BTA Bank* and *Ablyazov* litigation, the English Court of Appeal has reviewed aspects of the law of contempt and the consequences of breaching freezing orders.⁵

Of course, because of the vast amounts of wealth at stake in these cases, there are always trusts involved. I recently read an advertisement for a London conference on International Trust Disputes which stated:

Since the recession, legal disputes over trusts containing assets including property jumped 238% according to City law firms.

It would be nice to have some of that activity down here.

We know that, worldwide, there has been a huge expansion in the number of jurisdictions offering offshore financial services and New Zealand is now firmly in the mix. Trusts obviously play a central part in those services. Hopefully, the work New Zealand attracts in this area will continue to develop and grow.

Involvement in this type of work may bring with it a little controversy. New Zealand may increasingly be drawn into the on-going global debate and concern about the use of trusts eg the piece on New Zealand foreign trusts on '60 minutes' on 7 October 2012.

Certainly, in the last year, there have been a number of reports from various international bodies regarding the use of trusts:

- On 16 February 2012, the Internal Revenue Service released its annual 'dirty dozen' ranking of tax scams. One of the dozen was, of course, the trust, though it only ranked at number 12.⁶

⁴ Randell Krebs "Flexible Friend" (2008) 16(2) STEP J 17.

⁵ *JSC BTA Bank v Ablyazov* [2012] EWCA CIV 639 [*Ablyazov*].

⁶ See <http://www.irs.gov/uac/IRS-Releases-the-Dirty-Dozen-Tax-Scams-for-2012>.

- In February 2012, the Financial Action Task Force (FATF) re-issued its recommendations with revised guidance which indicate that the core area of concern in relation to money-laundering and terrorist financing relates to transparency and beneficial ownership.⁷
- In July 2012, the Tax Justice Network released a report which concluded that the global elite are hiding up to \$32 trillion in assets in offshore tax havens.⁸
- In November 2011, the World Bank published a report entitled 'The Puppet Masters' which (in part 3) discusses how investigators find trusts such a hurdle to investigate that they often do not prioritise them in corruption investigations. I should add, however, that trusts are seen, certainly by the World Bank, as less of a danger at the moment than other complex arrangements involving bearer shares or the misuse of shell companies. This is largely because of the fiduciary nature of trusteeship.⁹

Conversely using trusts to conceal assets does have some potential drawbacks, which may contribute to its low incidence. Professional trustees (who are required to follow standard financial compliance practice) tend to be more inquisitive about the source of funds to be vested in a trust than if they would be establishing a company. They are inquisitive because they face the risk of exposure to legal action, either by outside parties arguing claims against the trust or trust assets, or by settlors and beneficiaries for breach of fiduciary duties. Defending the trust from a suit can prove a costly undertaking for a trustee. Consequently, professional trustees may have a stronger incentive than a company service provider to avoid suspicious clients and ensure that the assets to be placed in trust are indeed owned by the settlor and are of legitimate origin. Furthermore, most service providers nowadays request proof of the source of the funds (for example, a copy of a will or a letter from an attorney for an inheritance, a receipt of sale for funds derived from property or shares, or pay slips.)

What we need to keep clearly in mind is that there are many perfectly acceptable reasons why people or organisations decide to use trust structures. As Pierre Lepaulle made clear, trusts are intricately woven into our domestic and business lives to such an extent that it is doubtful whether we could function without them. There are specific and historical uses in the New Zealand context such as avoiding the impact of the relationship property regime, misalignment of tax rates and social assistance policies. There are also uses that we share or may come to share with other jurisdictions. These include:

- **Commercial uses of trust** eg forms of collective investment such as unit trusts and pensions, loan syndication, holding of assets of a joint venture, voting trusts, various types of bonds etc.
- **Legitimate tax minimisation or mitigation** eg where a foreign settlor is immigrating to a common law country with high taxation.
- **Succession** eg as one English practitioner has put it 'protecting the family from their inheritance or the inheritance from the family'. Wealthy settlors, particularly those who are self-made, often do not have confidence that those who survive them will be proper and

⁷ <http://www.fatf-gafi.org/media/fatf/documents/recommendations/pdfs/FATF%20Recommendations%20%28approved%20February%202012%29%20reprint%20May%202012%20web%20version.pdf>. See in particular recommendations 24 and 25.

⁸ http://www.taxjustice.net/cms/upload/pdf/Price_of_Offshore_Revisited_120722.pdf.

⁹ http://www1.worldbank.org/finance/star_site/documents/Puppet%20Masters.pdf at page 46-47.

effective caretakers of the fortune the settlor had created and they want a mechanism to control what can be done with that fortune.

- **Succession** eg relief from the ‘forced heirship’ rules of many civil law jurisdictions and imposed by Sharia law. Typically forced heirship rules allocate to the surviving spouse and children an inalienable portion of the deceased estate. For example, under Swiss law, the surviving spouse is entitled to one quarter (¼) and the children to three-eighths (3/8) with three-eighths being available for free disposal. Some jurisdictions, the forerunner being The Cayman Islands (Cayman Trusts (Foreign Element) Law 1987), have enacted legislation seeking to thwart the claims of forced heirs. Other offshore jurisdictions have followed eg Guernsey.
- **Political risk** eg you may have a non-domiciled settlor from a country where the rule of law is not well observed or who has a singular lack of trust in his or her country’s political system or constitutional protections.
- **Creditor protection** eg transferring assets into trusts may provide a layer of protection for the settlor and the settlor’s heirs from a settlor’s creditors, not all of whom might have genuine claims. And, of course, we have a certain degree of protection for creditors in the Insolvency Act 2006 and Property Law Act 2007, which we will look later.
- **Charitable purposes** eg private schools and other charities.

As discussion and debate grows about the use of trusts, I think those of us who are protagonists or supporters of trusts need to be prepared to respond to criticisms of them. It is important that people understand that the trust is not a villain – it is simply a device to help us do the things we want to do and to structure and regulate our lives. If trusts are put to certain uses that are considered to be unacceptable or objectionable then we need to deal with those specific uses and problems eg the use of trusts to avoid the relationship property regime.

Professor Paul Matthews, a practitioner and Visiting Professor at Kings College London recently commented that:¹⁰

[T]here are a few people who seek to use trust for improper or even unlawful purposes. But so equally do some people seek to use motor cars and hypodermic syringes for such purposes. We do not ban the use generally of motor cars and syringes just because people use them to rob banks and the latter to shoot up illegal drugs. We have to separate the good uses from the bad, just as we do in all other aspects of life. Trusts are no different from contracts or other legal institutions in this respect.

At the very least, this is an appropriate first step in responding to criticism.

We are looking today at structuring trusts to deflect attack. There are a number of way that trusts can be ‘busted’ or ‘cracked’ or ‘looked through’. We will focus on a couple of the most commonly used methods and consider ways to minimise the success of such attacks.

¹⁰ Paul Matthews “The Place of the Trust in English Law and in English Life” (paper presented to the Future of Trusts Conference, London, April 2012).

SHAM TRUSTS

Perhaps the most controversial and long-running argument in New Zealand in relation to cracking or looking through trusts have been over the applicable rules for determining whether or not a trust is a sham. It is not uncommon to hear lawyers in New Zealand saying that a significant proportion of domestic trusts might be 'shams'.

If a trust is found to be ineffective because the trust documentation is a sham, then third parties, such as creditors, estranged spouses or partners or the tax authorities, may be able to treat the trust fund as still belonging in equity to the settlor. To allege that a trust is a sham involves impugning the transfer of equitable title of the trust fund to the beneficiaries (see, for example, *Minwalla v Minwalla*).¹¹ If a trust is found to be a sham, then the trustees would generally hold the trust fund on resulting trust for the settlor.¹²

The classic definition of a sham is given by Diplock LJ (as he was then) in *Snook v London West Riding Developments Ltd*.¹³ This case involved allegations that a hire purchase arrangement was a sham. Diplock LJ said of the term 'sham':

[I]t means acts done or documents executed by the parties to the "sham" which are intended by them to give to third parties or to the court the appearance of creating between the parties legal rights and obligations different from the actual legal rights and obligations (if any) which the parties intend to create.

... all parties [to acts or documents] must have a **common intention** that the acts or documents are not to create the legal rights and obligations which they give the appearance of creating. **No unexpressed intentions of a "shammer" affect the rights of a party whom he deceived.**' (emphasis added)

In the context of a trust, a helpful description can be found in Underhill & Hayton:¹⁴

... the rights and obligations apparently created within the four corners of the trust instrument were intended to create a misleading smokescreen.

There are two basic arguments as to the applicable rules for determining whether a trust is a sham:

- The first¹⁵ is that for a trust to be found to be a sham there must be a common intention of pretence or sham between the settlor and the trustees. So, the settlor and trustees must intend to mislead (*Official Assignee v Wilson*¹⁶ and *Midland Bank v Wyatt*¹⁷). If the same person is the settlor and sole trustee (ie there is a self-declaration of trust), the requirement for common intention is satisfied by the unilateral intention of the single holder of both roles.¹⁸ Common intention can include conduct where the trustee simply goes along with the shamming settlor and behaves recklessly or ignorantly (see, for example, *Midland Bank*

¹¹ *Minwalla v Minwalla* [2004] EWHC 2823 (Fam) [*Minwalla*].

¹² Or perhaps a bare trust, see *Official Assignee v Wilson* [2008] 3 NZLR 45 (CA) at [116] [*Wilson*]. For the position where there is a common intention between the settlor and beneficiaries see [121].

¹³ *Snook v London West Riding Developments Ltd* [1967] 2 QB 786 at 802.

¹⁴ David Hayton *Underhill & Hayton Law of Trusts and Trustees* (18th ed, LexisNexis, London, 2010) at [4.7].

¹⁵ See Matthew Conaglen "Sham Trusts" [2008] CLJ 176 and Matthew Conaglen "Shams, Trusts and Mutual Intention" [2008] NZLJ 227.

¹⁶ *Wilson* above n 12, at [26] – [54].

¹⁷ *Midland Bank v Wyatt* [1995] FLR 696 [*Midland Bank*].

¹⁸ *Wilson* above n 12, at [51]

where the wife signed trust documents but had no knowledge of the effect or nature of the declaration that she signed as a trustee).¹⁹

- The second²⁰ is that for a trust to be found to be a sham, common intention is not required. Rather, it is solely the settlor's intention to mislead that is relevant.

As you are all no doubt aware, the Court of Appeal in *Wilson*²¹ very clearly supported the first argument that a common intention between the settlor and trustees is required. In a joint judgment, Robertson and O'Regan JJ, stated that the court must look behind the objective appearance of a trust to ascertain the true nature of the transaction. In doing so, the court looks at the position at the inception of the alleged trust, because if a trust is validly created it cannot later become a sham. The court will search for the subjective intention of the parties to an alleged sham.²² However, the court will only look at the subjective intention if there is a 'good reason' to do so and because there is a premium on commercial certainty. Finding 'good reason' will require a high threshold to be met.²³ Indeed, Robertson J describes finding a trust to be a sham to be an 'extreme finding' because of the effect it has on the effect of beneficiaries.²⁴

Glazebrook J took a similar position.²⁵

This argument is generally accepted in other major common law jurisdictions such as England (*Shalson v Russo*²⁶), Canada (*Minister of National Revenue v Cameron*²⁷) and Australia (*Sharriment Pty Ltd v Official Trustee in Bankruptcy*²⁸) and *Sonenco (No 87) Pty Ltd v Commissioner of Taxation*²⁹, and also in Jersey *Abacus (CI) Ltd and Grupo Torras SA v al Sabah*³⁰ known as *In Re Esteem Settlement*. The second argument, on the other hand, has little judicial support. However, the Law Commission, in its Second Issues paper,³¹ does dwell on the second argument.

One of the strongest arguments in favour of having a rule that requires common intention is that it protects the security of transactions. The need to protect the security of transactions is something that English courts often emphasise in judgments when considering the ambit of legal rules. Hazel Genn, an English academic, has explained why this is so. She states that:³²

'The civil courts contribute quietly and significantly to social and economic well-being ... They promote social order and facilitate the peaceful resolution of disputes ... Most importantly, the civil courts support economic

¹⁹ At [37] - [38].

²⁰ Jessica Palmer "Dealing with the Emerging Popularity of Sham Trusts" [2007] NZ L Rev 81 (this was written before *Official Assignee v Wilson*) and Jessica Palmer "What Makes a Trust a Sham" [2008] NZLJ 319.

²¹ *Wilson* above n 12.

²² At [50] - [54] and [108].

²³ At [52].

²⁴ At [77].

²⁵ At [113] - [115].

²⁶ *Shalson v Russo* [2005] Ch 281.

²⁷ *Minister of National Revenue v Cameron* [1974] SCR 1062 at 1068.

²⁸ *Sharriment Pty Ltd v Official Trustee in Bankruptcy* (1988) 18 FCR 449 (FC).

²⁹ *Sonenco (No 87) Pty Ltd v Commissioner of Taxation* (1992) 38 FCR 555 (FC).

³⁰ *Abacus (CI) Ltd and Grupo Torras SA v al Sabah* [2003] JLR 188 [*Re Esteem*].

³¹ Law Commission "Some Issues with the Use of Trusts in New Zealand" Issues Paper 20, December 2010, Wellington at 42.

³² Hazel Genn "What is Civil Justice for? Reform, ADR, and Access to Justice" (2012) 24 Yale LJ & Human 397.

activity. Law is pivotal to the functioning of markets. Contracts between strangers are possible because rights are fairly allocated within a known legal framework and are enforceable through the courts if they are breached. **Thriving economies depend on a strong state that will secure property rights and investments.'**

If a contract is made or a trust is established, third parties need to be able to rely on those events and any resulting property rights in order to conduct business.

The Court of Appeal in *Wilson* made its support for this justification very clear stating that the courts 'will not wantonly interfere in ostensibly valid commercial transactions'.³³ As a result, it is in fact quite difficult to have a trust set aside as a 'sham'.³⁴

Another advantage of the current rule it is clear and relatively simple to apply. As a result, practitioners can more easily advise clients as to their legal position.

As I mentioned above, trusts are woven into the fabric of our domestic and business lives and a significant part of our wealth is held in trust. A rule that enables trusts to found to be ineffective with relative ease, by only requiring an examination of the settlor's intention when establishing the trust (the second argument), is likely to be commercially unworkable because the trust would become an 'unreliable' as a mechanism to hold wealth. There would be greater uncertainty as to beneficial ownership. Even if you argue that the application of such a rule could be controlled by estoppel or constructive trust arguments, determining such arguments would be complicated and costly, and would not necessarily alleviate uncertainty.

One of the strengths of Equity over the centuries has been its ability to create workable, efficient rules to regulate conduct which operate to assist and not undermine our market-based economy. We can look to such cases as *Keech v Sandford*,³⁵ which regulates the conduct of fiduciaries and is still assisting us today.³⁶

A more modern example might be the rule in England and Wales for determining liability for knowing receipt. In *Bank of Credit and Commerce International (Overseas) Ltd (in liq) v Akindele*,³⁷ Nourse LJ said that the test for determining liability should be whether the defendant's knowledge makes it unconscionable for the defendant to retain the benefit of the receipt. He considered that that rule would enable the courts to make common sense decisions in commercial contexts. In doing so, he rejected suggestions that strict liability should be imposed, subject to a change of position defence. That proposition, he considered to be commercially unworkable because it would make receipts unsafe.

In relation then to comments that a significant proportion of domestic trusts might be shams, in my view, this is unlikely. For a finding of sham trust, you need to show an intention to mislead by both the settlor and the trustees ie deceitful conduct. It might be true that a number of trusts in New Zealand are mismanaged and that some settlors and trustees do not fully understand the nature and

³³ *Wilson* above n 12, at [52].

³⁴ *Wilson* above n 12, at [53].

³⁵ *Keech v Sandford* (1726) 2 Eq Cas Abr 741.

³⁶ See for example *Guinness plc v Saunders* [1990] 2 AC 663.

³⁷ *Bank of Credit and Commerce International (Overseas) Ltd (in liq) v Akindele* [1999] BCC 669, affd [2001] Ch 437.

effect of their trusts or that trustees do not fully understand the nature and extent of their obligations, but those things alone, without some element of misleading conduct or deceit, will not make a trust a sham. Such scenarios might support an argument of equitable mistake if a settlor has absolutely no idea of the nature and effect of what he or she has done so that the trust instrument is set aside (or rectified) or might support claims of breach of trust or of fiduciary duty, or the rare liability as a trustee *de son tort*,³⁸ but they are different legal arguments.

Warning signs of sham

In *Wilson*, the Court of Appeal said that in ascertaining whether a trust was a sham from inception, it would look at the subjective intention at the time a trust is set up or at the time of an impugned transfer of an asset into the trust. As evidence of that intent, it would also look at conduct at that time, but also at subsequent conduct that might show that the trust was not genuine.

The types of conduct that should alert a practitioner to a possible claim that a trust is a sham, include:

- A trust executed in haste and secrecy from beneficiaries.
- A settlor who is not interested in taking professional advice.
- False statements in recitals to a trust instrument.
- Transfers to a trust shortly before a settlor enters a hazardous transaction.
- A settlor continuing to exercise dominion over trust property and treating it as his or her own.
- The trust that is not acted upon.
- A trustee who does not appear to be exercising any independent discretion.
- Evidence, such as paperwork, indicating the trustee feels bound to do what the settlor wants.
- A general lack of paperwork justifying trustee decisions.
- Powers reserved to the settlor or, perhaps, a protector close to the settlor, to appoint, add or remove trustees and beneficiaries or to appoint capital or income to the settlor in whole or in part or revoke vary or amend the trust.
- The settlor being made the sole trustee of the trust.

It is perfectly proper for settlors to reserve certain powers to themselves in the trust instrument, unless those powers are so great that it is considered that the trust is no longer for the benefit of the beneficiaries, but rather the assets are for the settlor's enjoyment ie on resulting trust for the settlor. Where that line will be drawn will depend on a particular factual situation and can be difficult to determine.

It is also perfectly proper for the settlor to consult with the trustees and for the trustees to do what the settlor has suggested, provided that the trustees properly exercise their independent judgment and discretionary powers.³⁹ Trustees and settlors have to aware of the types of conduct that may

³⁸ See *Williams-Ashman v Price and Williams* [1942] Ch 219 at 228 and *Mara v Browne* [1986] 1 Ch 199.

³⁹ See *Charman v Charman* [2006] EWCA Civ 1606 and *Kain v Hutton* [2007] NZCA 199 at [272]. See also *Spread Trustee Co Ltd v Hutcheson* [2011] UKPC 13

leave them open to attack. For example, informal arrangements between the settlor and trustee as to how things will operate can create difficulties and it is generally better to draft clear reservations of power for directions or veto by settlors (say in relation to investments) or requirements for written consent of a settlor before a trustee exercises certain discretionary powers.

If we look at the three well-known cases where trusts have been found to be shams, they all contain a number of our warning signs:

- *Minwalla*⁴⁰ - The settlor treated underlying assets of the trust as his own (dealing with bank accounts). The trustee passively allowed the settlor to treat the assets as his own and regarded him as the client. The trustee acted as the husband's tool, for example, he tried to evict the wife from possession of a trust property at the husband's request and wrote misleading letters to secure the release of funds frozen by a Mareva injunction. Also, the husband wrote two inconsistent letters of wishes saying how he wanted the trust fund to be dealt with on his death. The letters were both dated the same date. One named his wife as a beneficiary and the other did not.
- *Midland Bank*⁴¹ - Mr and Mrs Wyatt were joint legal owners of their home. They signed a declaration of trust (dated 17 June 1987) over the home in favour of Mrs Wyatt and their children as beneficiaries. It was not intended to be acted on and was put into a safe 'for a rainy day.' Loans for Mr Wyatt's business were secured against the interest in the home. The bank was unaware of the declaration of trust. The declaration was only produced once the business went into receivership.
- *Rahman v Chase Bank (CI) Trust Co Ltd*⁴² - The settlor retained a power to appoint capital of the trust to anyone including himself (with the consent of the trustee). The settlor also had a power to appoint one-third of the capital to himself without the consent of the trustee. The trustee could appoint all the capital to the settlor and in exercising the power was to have regard 'exclusively to the interests of the settlor'. The main administrative powers (such as investment) were exercisable only with consent of the settlor. The settlor, in fact, acted beyond those extensive powers and treated the trust property as his own and treated the trustee as a mere agent.

We have a recent New Zealand example of what factors can be relied to mount a sham trust claim and have it survive a strike-out application in *KA No 4 Trustee Ltd v Financial Markets Authority*⁴³ and in the earlier High Court decision *Financial Markets Authority v Hotchin*.⁴⁴

These cases relate to investigations by the Financial Markets Authority (FMA) into suspected breaches of the Securities Act 1978 by Mark Hotchin in his capacity as director of companies within

⁴⁰ *Minwalla*, above n 11.

⁴¹ *Midland Bank* above n 17..

⁴² *Rahman v Chase Bank (CI) Trust Co Ltd* [1991] JLR 103 [*Rahman*]. *Rahman* has however been criticised and distinguished by the Royal Court of Jersey in *Re Esteem*. The court in *Re Esteem* said that *Rahman* was really concerned with a now redundant principle of Jersey law (*donner et retenir ne vaut*) and the applicable rules on sham trusts were not fully considered.

⁴³ *KA No 4 Trustee Ltd v Financial Markets Authority* [2012] NZCA 370 [*KA 4 Trustee Ltd*].

⁴⁴ *Financial Markets Authority v Hotchin* [2012] NZHC 323 [*Hotchin*].

the Hanover Finance Group. The suspected breaches relate to the accuracy of representations as to the financial status of companies contained in certain offer documents.

Proceedings were issued by FMA seeking various orders preserving assets, including an order under s 60H(1)(a) of the Securities Act 1978 prohibiting any dealing with the property of a trust called the Kelly-Ashley 4 Trust, but known as KA 4 Trust on the basis that the property was 'controlled' by Mr Hotchin.

The KA 4 Trust was established by Deed dated 1 May 2003. Mark Hotchin, a former director of companies in the Hanover Group, was settlor and also, initially, sole trustee. Two years later, a Mr Radley was added as a trustee. In 2009, a company KA 4 Trustee Limited became the sole trustee of the trust. The sole shareholder and director of this company was an accountant, Mr Thomas, who had acted for Mr Hotchin and interests associated with Mr Hotchin for some time.

The trust was constituted with \$10 and assets were later transferred to the trust from other entities including another trust known as the KA 3 Trust. The discretionary beneficiaries of the KA 4 Trust included Mr Hotchin's children, but not Mr Hotchin himself. The children were also the final beneficiaries of the trust. There were no fixed beneficiaries.

The FMA, in its pleadings, alleged that this trust was a 'sham'.

The pleadings survived a strike-out application in the High Court, although a similar pleading in relation to another trust, the KA 3 Trust, did not.⁴⁵ The trustee of the KA 4 Trust appealed arguing that the claim was insufficiently particularised and untenable. This appeal was unsuccessful. In its judgment, the Court of Appeal made two important points.

First, they stated that in considering whether a trust was a sham at inception, evidence of transactions subsequent to the settlement of the trust could support the allegation of sham. They noted that where the same person was settlor and sole trustee, that person's 'unilateral intention' was critical in establishing the sham allegation. Without an admission by the settlor/trustee, the person alleging the sham would have to point to subsequent conduct to demonstrate the implementation of the sham ie personal control of assets ostensibly in trust. That is clearly right. There is generally a strong reason for entering into a sham transaction and the transaction operates over a period of time. It is clear that subsequent conduct should be considered, as well as conduct at inception of an alleged trust.

Secondly, the Court of Appeal cast doubt on dicta of Munby J in *A v A*⁴⁶ that a sham trust could become a genuine trust if a new 'untainted' trustee was appointed in place of a trustee who was in on the sham. For ease of reference, I have set out the full quotation from *A v A* below:

Can a trust which is initially a sham subsequently lose that character? I see no reason in principle why that should not be possible. The situation is best explained by an example. S has purportedly vested property in T1 as trustee

⁴⁵ A claim that another trust, the KA 3 Trust was void as a sham was struck out in the High Court because there were insufficient particulars to support an arguable case. The KA 3 Trust had initial trustees other than Mr Hotchin and there was no evidence to suggest that those trustees were party to any intention to set up the trust as a sham. See *Financial Markets Authority v Hotchin* n 44, at [54].

⁴⁶ *A v A* [2007] EWHC 99 at [45] – [47] [*A v A*].

of a trust which is in fact, consistently with their common intention, a sham from the outset. T1 now wishes to retire as "trustee." S, executing all the appropriate documents, purports to appoint T2 as T1's successor and to transfer the "trust property" into T2's name. Now if T2 knows that the "trust" is a sham and accepts appointment

as "trustee" intending to perpetuate the sham, then nothing has changed. The "trust" was a sham whilst T1 was the "trustee" and remains a sham even though T1 has been replaced by T2. But what if T2 does not know that the "trust" was a sham, and accepts appointment believing the "trust" to be entirely genuine and intending to perform his fiduciary duties conscientiously and strictly in accordance with what he believes to be a genuine trust deed? I cannot see any reason why, in that situation, what was previously a sham should not become, even if only for the future, a genuine trust.

On the contrary, principle argues compellingly that in such circumstances there is indeed, for the future, a valid and enforceable trust. After all, in the circumstances I have postulated, the trust property has been vested in someone who accepts that he holds the property as trustee on the trusts of a document which he believes to be a genuine instrument. He has no intention that the arrangement should be a sham. Conceptually, as it seems to me, the situation is, in reality, no different from that which was considered by Rimer J in the passage in *Shalson and others v Russo and others (Mimran and another, Part 20 claimants)* [2003] EWHC 1637 (Ch), [2005] Ch 281, at para [190] that I have already quoted.'

Mr Wagstaffe, who appeared before me on behalf of the interveners, and for whose lucid and compelling submissions in relation to sham I am particularly grateful, put the point quite neatly when he submitted that, even if the earlier trustee was party to a sham, a new trustee cannot become an unknowing party to the sham. Once the new trustee becomes legal owner of the trust property, provided he exercises his powers and fulfils his duties in accordance with the terms of the trust instrument, the trust cannot be regarded as a sham, no matter what may have passed before. I agree.

The Court of Appeal deliberately left the point open for future debate, but stated that if the KA 4 Trust was a sham when it was created it was not clear to the Court that subsequent conduct could convert it to the valid trust.⁴⁷ They considered that it could be argued that only a fresh declaration of trust, not tainted by the settlor's sham intention, would be required. In my view, this is certainly an issue that needs further consideration.⁴⁸ Theoretically, if a trust is found to be a sham, the trustee holds the trust property on resulting trust for the settlor ie the settlor holds the whole equitable proprietary interest.⁴⁹ In *Timpson's Executors v Yerbury*⁵⁰, the court set out the ways in which an equitable proprietary interest could be disposed of. It said:

'Now the equitable interest in property in the hands of a trustee can be disposed of by the person entitled to it in favour of a third party in any one of four different ways. The person entitled to it (1.) can assign it to the third party directly; (2.) can direct the trustees to hold the property in trust for the third party (see per Sargant J. in *In re Chrimes*); (3.) can contract for valuable consideration to assign the equitable interest to him; or (4.) can declare himself to be a trustee for him of such interest.

One issue could be whether a settlor's act, in appointing a new trustee not in on the sham, amounts to a direction to hold the trust property on trust on the same terms as those set out in sham trust documentation ie a valid method 2 under *Timpson*. If it can be so construed, then it would validly dispose of the beneficial interest.⁵¹ If another person (other than the settlor) had the power to appoint a new trustee, the issue becomes more complicated and would probably lead to estoppel arguments.

⁴⁷ *KA 4 Trustee Ltd*, above n 43, at [48] – [50].

⁴⁸ See the discussion in *Underhill & Hayton* above n 14, at [4.10] regarding the effect of a finding of sham trust where an illegal purpose has been wholly or partly achieved

⁴⁹ As above.

⁵⁰ *Timpson's Executors v Yerbury* [1936] 1 KB 645 at 664 [*Timpson*].

⁵¹ There are some similarities with cases dealing with s 53(1)(c) of the Law of Property Act 1925 (UK) such as *Grey v IRC* [1960] AC 1.

The factors that the Court of Appeal considered could possibly support the claim of sham, include the following:⁵²

- That Mr Hotchin was both settlor of the trust and, initially, the sole trustee, so only Mr Hotchin's intention was relevant.
- That Mr Hotchin, as settlor, had power to appoint and remove both trustees and beneficiaries (though since 14 June 2011, he jointly held the power to appoint and remove trustees with his mother).
- While the Deed restricted the exercise of trustee powers by prohibiting a sole trustee from exercising any power of discretion other than the appointment of a new trustee, Mr Hotchin disregarded this restriction for the first two years after establishment of the trust ie until the appointment of another trustee.

In addition, Winkelmann J mentioned another relevant factor, namely that aspects of how the KA 4 Trust operated suggested that trust assets have been, and been allowed to be, treated as Mr Hotchin's own. She referred particularly to dealings involving a property in Paritai Drive. These dealings are not set out in detail in the above judgment but some factual information about dealings between Mr Hotchin and the KA 4 Trust can be found in an earlier judgment, *FMA v Hotchin*.⁵³ These include that, although the property was a trust asset, Mr Hotchin had contributed over \$12 million to the construction of a house on the land, that when construction began there were discussions about the ownership of the house but these were inconclusive, and that there was an agreement between KA 3 Trust and KA 4 Trust to provide funds of \$2.5 million and any further funds required for construction in return for which Mr Hotchin and his family would be granted a 10-year lease of the Paritai Drive property with two 10-year rights of renewal.

I also want to mention briefly a recent decision of the English Court of Appeal, *North Shore Ventures Ltd v Anstead Holdings Inc*.⁵⁴ In this case, North Shore Ventures Ltd had loaned some \$50 million to Anstead Holdings Inc and the debt was guaranteed by two gentlemen, Messrs Fomichev and Peganov. The debt was not repaid and judgment was entered against Fomichev and Peganov, and worldwide freezing orders were obtained. In affidavits required under the freezing orders, both men averred that they had no assets and that their respective assets had been transferred to two settlements in March 2008. Those transfers took place less than a month after the two men received a letter for North Shore Venture's solicitors setting out the amount of the debt and two months before formal demand for repayment was made. The two men were ordered to produce certain trust documents and appealed that order. During the appeal process, they stated that they had been removed as discretionary beneficiaries of their respective family trusts and that the trustees had obtained injunctions preventing them from answering questions about the trusts.

⁵² *KA 4 Trustee Ltd*, above n 43, at [52]

⁵³ *FMA v Hotchin* [2011] 3 NZLR 469 [*FMA v Hotchin*].

⁵⁴ *North Shore Ventures Ltd v Anstead Holdings Inc* [2012] EWCA Civ 11 [*North Shore Ventures*].

Their appeals failed and they were ordered to produce the relevant documents. What is interesting about this case from our perspective is a comment of Toulson J in the Court of Appeal. He stated:⁵⁵

The circumstances surrounding the appointment and behaviour of the trustees were undoubtedly suspicious. For a wealthy man (or in this case two wealthy men acting simultaneously) to make himself a pauper, with the genuine intention of disposing of his money down to his last dollar irrevocably and with no ability to control what was to happen to it, is an unlikely scenario. Family trusts are a well known (sic) possible device for trying to place assets ostensibly beyond the reach of creditors, and the timing of the simultaneous creation of the trusts fits such a pattern. Suspicion that these were not entirely arm's length arrangements is heightened by the later steps taken by the trustees, for example, in seeking to prevent cross-examination of the appellants in the English proceedings and in apparently removing the appellants from even being discretionary beneficiaries for reasons and in circumstances which are unexplained. The circumstantial evidence gave reasonable ground to infer that there was in truth some understanding or arrangement between the appellants and the trustees by which they were to shelter the appellants' assets, consistent with the appellants' real aim, and the nature of that understanding and arrangement was such that the trustees would take whatever steps the appellants wished in the administration of the trusts.

Just as reservation of too much control by a settlor might be evidence to support an argument of sham trust (ie a common intention to mislead) so too can too little control. Really, in sham trust cases much will come down to the particular facts of each case.

It is quite clear that considerable care needs to be taken when settling up a trust for a client and acting as a trustee to a trust. So what general lessons can we take from these various cases?

Some thoughts

Here are some thoughts:

- Right from the start, make sure that the client/settlor know precisely what he or she is doing in setting up a trust and fully understand the consequences of creating a trust and transferring property that he or she owns absolutely into trust. In particular, a client should specifically be made aware that settling property into a trust may take it out the ambit of Property (Relationships) Act 1976.⁵⁶
- Make sure that a client understand the nature of trusteeship, the nature of fiduciary duties and responsibilities of trustees and that the settlor can express wishes, but it is the trustees who will have control over trust assets, not the settlor.
- In relation to these first two points, extra care needs to be taken when a client/settlor does not have English as a first language or is from non-common law jurisdictions. You may need the services of a translator or even translations of relevant documents. You may want to ask a client/settlor to sign an undertaking that they understand the terms of the trust.
- You need to think very carefully about what powers are reserved to a settlor. In particular, you need to think very carefully about reserving powers of investment or disposition for the settlor that are greater than those of the trustee. We know from *Rahman* that the greater

⁵⁵ At [38]

⁵⁶ See in particular the article by Nicola Peart, Mark Henaghan and Greg Kelly "Trusts and Relationship Property in New Zealand" (2011) 17 Trusts & Trustees 866.

the control that is given to the settlor, the greater the risk that the trust will be found to be void as a sham, particularly if settlors can appoint capital to themselves or trustees can appoint capital to settlors having regard exclusively to their interests. If we look at the *Hotchin* decisions, even powers to appoint and remove trustees and beneficiaries (even though a Deed may prohibit self-dealing) can help to support a sham claim and help avoid it being struck out. You may want to use a co-appointer, who has a degree of independence.

- In appropriate circumstances, you may need to advise a settlor/client about how a court might perceive the settlor reserving **no** powers, particularly if the settlor is not a trustee or beneficiary.
- You need to advise clients about the dangers of being the settlor and also sole trustee of a settlement. As we have seen from the *Hotchin* decisions, it is easier to mount a claim that a trust is void as a sham.
- Make sure that clients understand that trustees can refuse or refuse in part a request from a settlor if they properly consider that that is the right thing to do. Clients also need to understand that trustees should avoid patterns of behaviour that seem to show that they are simply doing what they are told by a settlor.
- If a settlor wants to retain a significant degree of control then it is better to draft clear reservations of power for direction or veto by a settlor (say in relation to sale or purchase of investments) or requirements for written consent of the settlor before a trustee can exercise certain discretionary powers, than to have some informal arrangement between the trustee and settlor as to how things are to operate. Such informal arrangements can leave the way open to allegations of sham.
- Make sure that clients understand the need for trustees to administer trusts properly, hold regular meetings and keep accurate records of transactions and decisions reached. Such records can provide documentary evidence that the trustees are making independent decisions and not blindly following the wishes of settlors.

Often, when debtors use trusts to shelter assets, the intention of the debtor/settlor is to create a valid trust. This can make it difficult to argue that a trust is a sham. Of course, this is not always the case. Debtors can give the pretence that a trust has been set up, put assets into trust using a pliant trustee and later, when the coast is clear and creditors have given up, have trust assets transferred back to the debtor. It will be worth watching the *North Shore Ventures* litigation to see if that is how the actions of Messrs Fomichev and Peganov are construed.

Where it is difficult to prove that a trust is a sham, the next best route for a creditor will often be to see if a transfer to a trust can be set aside under statute.

SETTING ASIDE DISPOSITIONS THAT PREJUDICE CREDITORS

Utilising trusts to shield assets from creditors is a practice almost as old as the trust, as are methods to set aside transactions designed or intended to defeat creditors and others. The earliest statute I have seen is an Act of Edward III in 1376⁵⁷ which deals with fraudulent conveyances but the statute from which our modern statutory rules derives is the Fraudulent Conveyances Act 1571 which states:⁵⁸

[f]or the avoiding and abolishing of feigned covinous and fraudulent feoffments, gifts, grants, alienations, conveyances, bonds, suits, judgments and executions, as well of lands and of tenements and chattels . . . devised and contrived of malice, fraud, covin, collusion, or guile, to the end, purpose and intent, to delay, hinder or defraud creditors and others . . . [they] . . . shall be utterly void . . . and of no effect . . .

This section was law in New Zealand until it was replaced by s 60 of the Property Law Act 1952. The latest manifestation in New Zealand of the 1571 Act is subpart 6 of the Property Law Act 2007 (ss 344 – 350). Sections 344 – 350 of the Act set out a code to enable ‘prejudicial dispositions’ made by a debtor to be restored for the benefit of the creditors.

Pursuant to s 346, to be caught by subpart 6, ‘prejudicial dispositions’ must fall within two conditions:

- First, they must be made after 30 December 2007 by a debtor who:
 - was insolvent at the time, or became insolvent as a result, of making the disposition; or
 - was engaged, or was about to engage, in a business or transaction for which the remaining assets of the debtor were, given the nature of the business or transaction, unreasonably small; or
 - intended to incur, or believed, or reasonably should have believed, that the debtor would incur, debts beyond the debtor’s ability to pay
- Secondly, they must be made with intent to prejudice a creditor, or by way of gift, or without receiving reasonably equivalent value in exchange.

These latter phrases are specifically defined in s 345. So, a disposition of property prejudices a creditor ‘if it hinders, delays, or defeats the creditor in the exercise of any right of recourse of the creditor in respect of the property’ but does not include dispositions preferring one creditor over another.

A gift includes ‘a disposition made at an undervalue with the intention of making a gift of the difference between the value of the consideration for the disposition and the value of the property comprised in the disposition’. S 345 also states that a debtor is to be treated

⁵⁷ 50 Edw III c 6. This statute was aimed at debtors who, to avoid creditors, gave up their tenements and chattels to trusted associates (who would agree to pass to the debtor any profits) and then could seek sanctuary in the “Franchise of Westminster of St Martin le Grand of London and other such privileged place”.

⁵⁸ 13 Eliz 1, c 5

as insolvent if the debtor is unable to pay all his or her debts as they fall due from assets other than the property disposed of.

Ss 347 – 350 cover matters such as who can apply for orders (a creditor who claims to be prejudiced or a liquidator) and what orders the court can make. They also provide protection for certain persons receiving property, which include a person who acquired the property for valuable consideration and bona fide and also a person who received the property bona fide without knowledge and who has had a change in circumstances.

There is little case law on these sections, but cases in relation to s 60 Property Act 1952 will still be relevant in certain respects. For example, we are likely to turn to *Regal Castings Ltd v Lightbody*⁵⁹ when determining the meaning of the term ‘intent’.

In *Regal Castings*, the court was considering the meaning in s 60 of the phrase ‘intent to defraud’ and it held that it meant ‘intent to hinder, delay or defeat a creditor’. The Supreme Court stated⁶⁰ that ‘intent’ did not mean ‘purpose’ and it was not necessary to show that a debtor intended to cause loss to creditors. What you do have to show is that the debtor, in fulfilling his or her own purpose (for example, preserving assets for the family), has hindered, delayed or defeated creditors ie denied creditors access to the assets disposed of or alienated. In particular, Blanchard J stated:⁶¹

Whenever the circumstances are such that the debtor must have known that in alienating property, and thereby hindering, delaying or defeating creditors’ recourse to that property, he or she was exposing them to a significantly enhanced risk of not recovering the amounts owing to them, then the debtor must be taken to have intended this consequence, even if it was not actually the debtor’s wish to cause them loss. We respectfully agree with the opinion of Gaudron J in *Cannane (DM) v J Cannane Pty Ltd (in liq)* [(1998) 192 CLR 557 at 572] that an intent to defraud:

“involves the notion of detrimentally affecting *or risking* the property of others, their rights or interests in property, or an opportunity or advantage which the law accords them with respect to property.”

The most simple case is one in which an insolvent debtor has gifted a substantial asset to a relative or friend or to trustees of a family trust, thereby subtracting from an already insufficient quantum of assets.

There are certain types of conduct from which an intention to prejudice creditors can be readily inferred. They are often called ‘badges of fraudulent intent’ and include such things as a debtor giving away property say to a family trust, but retaining the benefit or use of the property,⁶² or secretly transferring property away or giving misleading explanations of it (*Twyne’s Case*).⁶³

The first significant case to follow *Regal Castings* is the Court of Appeal’s decision in *Taylor v Official Assignee*⁶⁴. If you are acting for clients whose assets have been placed in trust, this case will give you some comfort. From an academic point of view, however, the Court of Appeal decision is not without difficulty.

⁵⁹ *Regal Castings Ltd v Lightbody* [2009] 2 NZLR 433 (SC) [*Regal Castings*].

⁶⁰ Above at [53] – [54].

⁶¹ Above at [54] – [55].

⁶² Above at [6].

⁶³ *Twyne’s Case* (1602) 3 Co Rep 80.

⁶⁴ *Taylor v Official Assignee* [2011] NZCA 630 [*Taylor*].

The case concerns an appeal by trustees of a family trust against a decision by Heath J to uphold the setting aside of various dispositions made over a period of six years to a family trust by a bankrupt, Mrs Taylor, under s 60, and s 54 of the Insolvency Act 1967. The original determination required the family trust to pay \$227,000 to the Official Assignee.

Briefly, the facts are that Mrs Taylor ran a business as a tax agent. In 1999, her husband set up a new business and, on advice, in October 2000 the couple set up a family trust. They gave evidence that the trust was set up as asset protection in the light of Mr Taylor's new business. The family home was transferred to the trust in December 2000 in return for a debt secured by a 30 year second mortgage. A gifting programme was undertaken. In late 2000, Mrs Taylor was not well and in April 2001 was diagnosed with 'major depression'⁶⁵ and was medicated with prozac. She ceased paying proper attention to her business to such an extent that her accounts had to be reconstructed from 2001 to 2005. She was eventually made bankrupt in 2006, owing over \$200,000 to the Inland Revenue and to her own company.

The Court of Appeal allowed the appeal after analysing each disposition. In my view, the main difficulty with the judgment is that the court focusses on 'intent to defraud' without differentiating between the purpose of setting up the trust and making the dispositions, and the intent 'to hinder, delay or defeat creditors'. They focus on whether Mrs Taylor was insolvent at the time of each disposition, but fail to discuss the fact that a debtor does not have to be insolvent if they are about to enter a risky venture or might be incurring debts that they could not pay.

Some thoughts

- It is important to obtain full information from a client at the time they are setting up the trust as to their financial position and any plans to engage in new possibly risky business activities, as these can make the trust more vulnerable to attack if the client falls into financial difficulties.
- If a client is setting up a family trust in order to protect assets and transferring substantial assets to it, then the transaction should have a commercial element. In *Taylor*, the Court of Appeal heard evidence from the solicitor who set up the trust that the transaction was 'standard'.⁶⁶ The property was transferred at market value, the loan from the trust to the settlors was secured by a mortgage pursuant to which interest at commercial rates could be charged, and if interest was demanded and not paid, principal and interest could be called up, notwithstanding that the debt was not repayable for 30 years. This certainly provided some protection for Mrs Taylor.

⁶⁵ Above at [66].

⁶⁶ Above at [43] – [44].

Insolvency Act 2006

There are also provisions under the Insolvency Act 2006 to set aside transactions made before bankruptcy. These include ss 204 – 210 (gifts within two years of adjudication), s 205 (gifts made between two and five years in certain circumstances), and ss 194 and 195 (insolvent transactions within two years of adjudication). The Companies Act 1993 also has an almost identical regime.

‘BUNDLE OF RIGHTS’ CASES

No discussion in New Zealand of cracking or looking through trusts would be complete without, at least, a mention of this line of cases. The very least you can say about this line of cases is that they are unorthodox and are not aligned with trust law principles.

Traditionally, powers in a trusts’ context refer to an authority or mandate to deal with and dispose of property which the donee of the power does not own. They are an entirely separate concept from the ‘dominion’ that a person has over property that he or she owns.⁶⁷

The distinction between property and powers is a fundamental legal principle. In *Re Armstrong ex P Gilchrist*⁶⁸, Fry LJ described the distinction in the following terms:

No two ideas can well be more distinct the one from the other than those of ‘property’ and ‘power’. A ‘power’ is an individual personal capacity of the donee of the power to do something. That it may result in property becoming vested in him is immaterial; the general nature of the power does not make it property. The power of a person to appoint an estate to himself is, in my judgment, no more his ‘property’ than the power to write a book or sing a song. The exercise of any one of those three powers may result in property, but in no sense which the law recognises are they ‘property’ ... Not only in law but in equity the distinction between ‘power’ and ‘property’ is perfectly familiar, and I am also ashamed to deal with such an elementary proposition ... That being so, have the courts ever said that such ‘powers’ are “property”? If they have, it would be our duty to follow their decision. But no such imputation can with propriety be cast on the Courts of Law or Equity; they have always recognised the distinction between ‘power’ and ‘property’.

There has been some erosion, in equity and in various statutes,⁶⁹ of that stark position. There are a line of older cases dealing with general powers of appointment⁷⁰ and, recently, the Privy Council in *Tasarruf Mevduati Sigorta Fonu v Merrill Lynch Bank and Trust Co (Cayman) Ltd*⁷¹ has treated a general power of revocation as a right ‘tantamount to ownership’ and as property so that the equitable remedy of a receiver by way of equitable execution was available to a judgment creditor.

However, both these groups of cases deal with wide general powers⁷² of revocation and appointment which are entirely different from the powers included in ‘bundle of rights’ arguments. In *TMSF*, for example, the power of revocation enabled the settlor of the trust, Mr Demirel, to take

⁶⁷ Geraint Thomas *Thomas on Powers* (2nd edition, OUP, Oxford, 2012) at [1.04]

⁶⁸ *Re Armstrong ex P Gilchrist* (1886) 17 QBD 521 at 531

⁶⁹ See, eg, ss 101-102 Insolvency Act 2006.

⁷⁰ See Tony Molloy “The Vulnerability of Asset Protection Trust Revocable by the Settlor: ‘Equity’s Tenderness for Creditors’ “ (2011) 17 *Trusts and Trustees* 784.

⁷¹ *Tasarruf Mevduati Sigorta Fonu v Merrill Lynch Bank and Trust Co (Cayman) Ltd* [2011] UKPC 17 [*TMSF*].

⁷² In *Re Triffitt’s Settlement* [1958] Ch 852 at 861, Upjohn LJ stated ‘where there is a completely general power in the widest sense, that is tantamount to ownership.’

ownership of the trust assets entirely. He had ‘absolute disposing power over the property’⁷³ and there is no obligation to consider the interests of others.

In the bundle of rights cases, the relevant powers usually relied on by the courts are to appoint and remove trustees and any new trustee would be subject to fiduciary duties.⁷⁴

In *FMA v Hotchin*, Winkelmann J stated:⁷⁵

Powers of appointment of trustees, even of discretionary beneficiaries, are not sufficient to give Mr Hotchin control over the assets of the Trusts, because that control rests, at law, with the trustee once appointed.

We shall have to see if this dicta proves terminal to the ‘bundle of rights’ cases or whether a superior court determination is necessary.

This argument has been well put in Nicola Peart, Mark Henaghan and Greg Kelly’s recent article in the periodical, *Trusts and Trustees*.⁷⁶ The fault really lies with limitations in our relationship property regime. That is something which can be easily remedied by legislation and we can look either to the United Kingdom⁷⁷ or Australia for examples.

Undue Influence and Equitable Mistake

Finally, it is always important to remember that trusts can be set aside for undue influence and equitable mistake.⁷⁸

Other options

The usual alternatives to trusts include the following:

- Contractual solutions
- Foundations
- Limited partnership structures
- Companies with preferential share classes
- Offshore companies
- Offshore wrappers

Traditionally in the UK, foundations are encountered reasonably often especially with clients from civil law jurisdictions.

⁷³ *TMSF*, above n 70 at [43].

⁷⁴ See eg *JG v JBG FC North Shore* FAM-2007-044-591, 13 July 2012 and see also above n 56, 12.

⁷⁵ Above n 53 at [131].

⁷⁶ Above n 56.

⁷⁷ In the UK, see ss 24 and 25 of the Matrimonial Causes Act 1973. Trusts are relevant in ancillary relief/financial remedy proceedings as an ante-nuptial or post-nuptial settlements under s 24, or as a financial resource under s 25.

⁷⁸ See *Pitt v Holt* [2011] EWCA Civ 197. This case is currently on appeal to the United Kingdom Supreme Court. See also *Bullock v Lloyds Bank Ltd* [1954] 1 Ch 317

They are available in a number of jurisdictions including Panama, Malta, Liechtenstein, the Netherlands, the Bahamas, Seychelles, Nevis, Cyprus, Jersey and most recently the Cook Islands. In July of this year, the Cook Islands' Government enacted the Cook Islands' Foundations Act 2012.

The basic attraction of a foundation is that it has legal personality and also is better understood by those from civil law jurisdictions who are unfamiliar with equitable proprietary ownership and interests and often have difficulty understanding the trust as a 'relationship' between settlor, trustee and beneficiaries.

Foundations are similar to companies, although foundations do not have shareholders. They are generally managed by a board or council and a client, who is the founder and endows the foundation, can often sit on those bodies. They can have beneficiaries but the beneficiaries have only contractual rights rather than proprietary rights. Some foundations do not have beneficiaries and exist for charitable purposes. The founders can also have powers reserved to them such as powers over investments or appointment and removal of beneficiaries.

More recently, in the UK, limited partnerships have begun to be used. This is because of changes to inheritance tax regulation in 2006 which made it almost impossible for someone domiciled in the UK for inheritance tax purposes to create a trust without incurring ten year and exit charges.⁷⁹ Foreigners who have live in the UK are deemed to be domiciled in the UK for inheritance tax purposes if they live for 17 out of the last 20 years there.

The advantage of limited partnerships is that they can enable a wealthy parent to keep some control over partnership assets. The parent can be made the General Partner and retain responsibility for management of assets and distribution of profits, whilst other family members are limited partners. There are disadvantages which limit their usefulness. These include that the partnership has to have a business and 'view to profit'. It is not just for co-ownership of assets. And, the partnership interest is within the person's estate for tax and creditor purposes.

And, of course, there is a plethora of other types of trusts, both private express and purpose trusts, in various offshore jurisdictions, should a client wish to move funds offshore. Discussion of those, alas, will have to wait for another day.

⁷⁹ Finance Act 2006 (UK)