

# An important case on constructive trusts and settlor control

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In *Murrell v Hamilton* [2014] NZCA 377, the Court of Appeal approved the notion that a constructive trust can be imposed over the assets of an express trust.

Professor Rickett has been highly critical of this development, saying that a trust's assets are owned for the benefit of the beneficiaries and a trustee has no right to allow the assets to be given to a third party.

In *Vervoort v Forrest & Others* [2016] NZCA 375 (4 August 2016), the Court of Appeal has rejected these criticisms. It says:

"... the reality of a trustee's ability to give a third party expectations ... over trust property ... must be recognised. There is no misappropriation of property in that the beneficiaries of the express Trust have no claim in conscience to the increases in value resulting from the contributions. Beneficiaries cannot expect trustees to retain for them an unearned benefit, extracted by expectations engendered by the trustees." [70]

The facts of the *Vervoort* case are simple enough. Ms A lived with Mr B for 12 years. He had formed a trust before he met her and the trust bought a property while they were together. Ms A said she helped to find it, to decorate it, to maintain it, to maintain its garden, and to do other such things so as to preserve or enhance its value. When the relationship ended she made a claim of a constructive trust against the property.

The Court of Appeal has held that:

- The trust was not a sham even though Mr B "intended to control it." [28]
- "[Mr B] undoubtedly exercised de facto control of the Trust ..." [36]
- The trust was not an illusory trust.
- The fact that a stooge trustee "in breach of his obligations as a trustee, left the management of the Trust to [Mr B] did not make the Trust expire." [39]

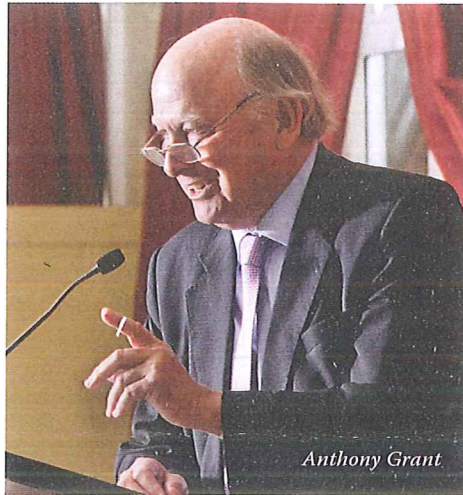
In such circumstances, the Court held (at para [39]) that Ms A could make:

- a claim for breach of trust;
- a claim of negligence; and
- a claim based on constructive trust.

The judgment is important not only for the fact that it cements the notion that a constructive trust can be imposed over the assets of an express trust, but also for the Court's toleration of what trust lawyers call "effective control".

These are some of the passages from the judgment that indicate a toleration for effective control:

"Where one partner has de facto control of the trust and ... contributions and expectations have



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arisen, the noncontrolling partner may be forced to claim against the trust ..." [48]

"The Judge was quite right in acknowledging the traditional trust principles of unanimity and nondelegation but those principles must bend to the practical realities when one trustee is in absolute control of all trust activities and the other trustees have effectively abdicated their trustee responsibilities." [62]

"[The] controlling partner cannot avoid equitable constructive trust obligations by relying on the prohibition on delegation and the lack of consent from the other trustee, whom that controlling partner has deliberately isolated from trustee functions. To allow that would be to allow a Trust principle to operate as a weapon for inequity. The deliberate exclusion of other

trustees from a role in managing the trust cannot be invoked to create an injustice." [64]

In *Vervoort*, the Court of Appeal has firmly established that, notwithstanding criticisms to the contrary, a constructive trust can and should be imposed over the assets of an express trust if equity requires it and that it is not necessary that all trustees must have known of the facts that have given rise to a constructive trust over the trust's assets.

As for "effective control", the toleration of a state of affairs where one trustee "has de facto control of the trust" or "absolute control of all trust activities" is concerning.

The tax havens spend much time creating laws by which settlors can retain extensive controls over trusts and statutes are passed that deem the controls not to be in a breach of the "effective control" rubric.

But this is not the law of equity. This is what the Royal Court of Jersey said in *Rahman v Chase Bank Trust* (1991) JLR 103:

"We were unanimously satisfied that the oral evidence, together with the documentation placed before us, established clearly that from the date on which [Mr Rahman] purported to constitute the settlement he exercised dominion and control over the trustee in the management and the administration of the settlement ... he treated the assets comprised in the trust fund as his own ... There was a retention by [Mr Rahman]. We are unanimously of the opinion that the settlement was a sham on the facts, in the sense that it was made to appear a genuine gift when it was not."

And in the Australian case of *Re Stephen Moor Ex Parte* [1989] FCA 59, it was said:

"I think that this bankrupt is in effective control of the trust ... This means that the deed, and possibly the trust instrument, may have amounted to one or more shams ..."

And in the case of *Ashton* [1986] FamCA 20 (also an Australian case), Strauss J said:

"The powers which the husband has in the Ashton Family Settlement have given him control of the trust either as trustee or through a trustee which is his creature, and at the same time he is able to apply the income and property of the trust for his own benefit ... this Court is not bound by formalities designed to obtain advantages and protection for the husband who stands in reality in the position of the owner."

Such "trusts" were disregarded in Jersey and Australia. There is not space in this article to provide similar illustrations from other jurisdictions.

Although these cases are not identical to the facts in *Vervoort*, they are close enough to cause a reader to wonder whether the Court of Appeal is approving as trusts, arrangements that are regarded elsewhere as shams. 