Can a beneficiary exercise "*effective control*" of a Trust via a corporate trustee of which he/she is the shareholder and director?

Settlors want to have "*effective control*" of Trusts but the Courts say that "*effective control*" is not permitted.

A settlor must relinquish ownership of assets that are settled on a Trust.

The case of *Legler v Formannoij & Another* [2021] NZHC 1271[1] shows that there may be a way by which a settlor can legitimately exercise effective control over a Trust and the purpose of this Paper is to test whether the *Legler* decision provides a reliable pathway for a settlor to exercise effective control over a Trust.

***Legler* – the facts**

Mr Ricco Legler was married twice. By his first marriage he had three children.

His second wife was Maria. They were together for 28 years before he died and they had no children.

Ricco established two Trusts which I will call Trusts 1 and 2.

The discretionary beneficiaries of each Trust were Ricco, Maria and the three children.

After some years Ricco made some changes to the Trusts, telling Maria that he wanted Trust No 2 to primarily benefit her and him and Trust No 1 to primarily benefit his three children.

At the time of his death the trustees of Trust No 2 were Maria and a corporate trustee established by an accountant.

One of the children questioned the accountant's competence and the accountant, sensing trouble, resigned. This left Maria as the sole trustee of Trust No 2.

Trust No 2's Deed of Trust required her to appoint a new trustee. She approached a partner in a law firm who declined to act. She spoke with Perpetual Guardian but she thought their fees excessive and she didn't think they would be a "*good fit*" for Trust No 2.

A law firm in Whangarei told Maria that the Deed of Trust for Trust No 2 permitted her to appoint a corporate trustee of which she could be a director. She accepted this advice and after she had done this she resigned as a trustee in her personal capacity.

Maria was advised that there was no requirement for there to be an independent trustee if a corporate trustee was the sole trustee.[2]

---

1 2 June 2021

2 Paragraph 21

Trust No 2's Deed of Trust

The Deed contains some important clauses. They included the following:

(a) "*The interpretation of this Deed in cases of doubt is to favour the broadening of the powers and the restricting of the liabilities of the trustees*."

(b) "*The trustees may alter, vary, add to or revoke all or any of the Trust's, powers or provisions of the Trust by execution of a Deed*…"

(c) "***Any power or discretion vested in the trustees may be exercised in favour of a trustee who is also a beneficiary, by the other trustee or trustees***."

(d) Unless a corporate body was the sole trustee:

(i) "*If any time there is only one trustee, no power or discretion conferred on the trustees by law or by this Deed, other than that of appointing a new trustee, shall be exercised by the surviving trustee until such time as the additional trustee has been duly appointed*";

(ii) "***The trustees must always include at least one person who is not a beneficiary****, nor the spouse, parent or child of a beneficiary or of a trustee, nor a person who is or has been in any sexual relationship with a beneficiary or with a trustee*."

(e) "***Any properly empowered corporate body may act as the sole trustee or as one of two or more corporate Trustees***."

"***It is expressly declared [that] a corporate trustee may exercise all the powers and discretions vested in that trustee by this Deed and by law notwithstanding such exercise may in any way directly or indirectly benefit any beneficiary who has any interest (contingent or otherwise) in that trustee whether as director, officer, shareholder or otherwise howsoever***."

In her role as director of the corporate trustee Maria removed the children as beneficiaries of Trust No 2 and appointed all of its assets to herself.

The three children from Mr Legler's first marriage contended that the appointment of the corporate trustee as sole trustee with Maria as its sole director was a fraud on a power. This argument was rejected by Downs J.

It was also argued that the appointment of a trustee is a fiduciary power and that it was a breach of the fiduciary obligation to appoint a single corporate trustee with a beneficiary as its sole director.

So far as the fraud on a power allegation is concerned, the Judge said that the claim failed "*on the facts*." The facts to which the Judge referred were these:

(a) Maria became the sole trustee "*through circumstance, not exploit*." Her husband had died; the corporate trustee established by an accountant had

resigned and she had attempted to find another trustee but had not found someone she thought suitable.

(b) When a lawyer questioned the legitimacy of having a single corporate trustee Maria had sought legal advice and had been assured that she was permitted to appoint a single corporate trustee of which she was its director. The Judge said "*the sequence suggests Maria wanted to act lawfully; and was acting on legal advice*."[3]

(c) Maria had sought legal advice and was told that she had an "*overarching duty to act in the best interests of the beneficiaries of the Trust, having considered the needs and circumstances of each of the beneficiaries, including Ricco's children and yourself*."

(d) Trust No 2 was intended primarily for Maria and her late husband while Trust No 1 was primarily intended for the three children.

(e) She was "*a careful, fair-minded witness [who] impressed as sincere*."[4] [58]

In summary the Judge said he was "*not persuaded Maria appointed [a corporate trustee] to benefit herself or that this was one of her purposes in appointing that trustee*."[5]

It should be noted that the three children were financially well off. Trust No 1 had a valuable land asset and a fund of at least $3m, and each of the children had received $1.135m from their grandfather.[6]

In reaching this decision, Downs J relied significantly on the Australian High Court's decision in *Montevento Holdings Pty Limited v Scaffidi* [2012] HCA 48.

I will refer in a moment to what the High Court of Australia said in that decision but for the moment, this is what Downs J said:

> *"Montevento is high authority for the proposition [that] a single corporate trustee controlled by a beneficiary is not inherently objectionable in a family Trust setting."*[7]

Whereas it was contended that the appointment of a corporate trustee in *Legler* constituted a "*fraud on the power*" that term was not used in the *Montevento* case. Even so, the concept appears to have been considered in the first instance decision in *Montevento*. Downs J said:

> *"While the phrase 'fraud on the power' was not used [in the first instance decision in the Montevento case] it is clear at least Heenan J was alive to the possibility Montevento was appointed with an improper purpose. As observed, the*

3 Paragraph 51
4 Paragraph 58
5 Paragraph 59
6 Paragraph 56
7 Paragraph 66

> *Judge concluded there was no evidence to support that finding."*[8]

Montevento Holdings Pty Limited v Scaffidi [2012] HCA 48[9]

The High Court's decision in *Montevento* was given in a unanimous judgment of all five Judges.

Eugenio Scaffidi appointed Montevento Holdings Pty Limited as the sole trustee of The Scaffidi Family Trust and Eugenio Scaffidi was its sole director and shareholder.

Another member of the Scaffidi Family contended that the appointment of Montevento "*was invalid because it breached clause 11.03 of the Trust Deed.*" Clause 11.03 provided as follows:

> *"**If, and so long as any individual Appointor is a Beneficiary that individual shall not be eligible to be appointed as a Trustee**."*

Clause 11.01 of the Deed of Trust provided that:

> *"[a] trustee may be a corporation."*

The High Court noted that "*many of the provisions of the Trust Deed distinguish between an 'individual', meaning a natural person and a 'corporation' or 'company*.'"[10]

The trial Judge found that there was no evidence that Eugenio Scaffidi "*had appointed Montevento as a trustee for an improper purpose*."[11] Heenan J said:

> *"I am satisfied that in this case the Deed of Settlement draws a clear distinction between individuals and corporations, recognises that a corporation may be a trustee or co-trustee of this Trust, and contains no actual or implicit prohibition upon a corporation, even if controlled by a beneficiary, from being such a trustee. Because the corporation is distinctly and legally separate from the individual, I do not consider that the prohibition in the Deed of Settlement against an individual beneficiary being a trustee prohibits the appointment of Montevento and, accordingly, I dismiss the application… seeking declarations… on the basis that Montevento was invalidly appointed."*[12]

Heenan J found that there was no evidentiary basis for concluding that Montevento would jeopardise the welfare of the Trust fund or the interests of the beneficiaries.[13] He said:

---

8 Paragraph 66
9 7 November 2012
10 Paragraph 9
11 Paragraph 18
12 Paragraph 19
13 Paragraph 20

> *"As trustee, Montevento is subject to the duties and obligations resting upon any trustee at law and in this case as also set out in the Deed of Settlement. There are ample avenues of redress available to any aggrieved beneficiary to challenge or review the actions of the trustee. More significantly there is no allegation that Montevento has admitted, or is threatening or likely to commit, any breach of trust."*[14]

The High Court approved the dissenting judgment of Buss JA in the Court of Appeal in *Montevento* who noted that the Deed of Trust consistently distinguished between individuals and corporations.[15]

Will Judges accept the distinction between (a) a person and (b) a Company of which the person is the sole shareholder and director?

While the *Legler* decision draws a clear distinction between a person on the one hand and a Company of which the person is both the shareholder and director, it can be expected that some Judges will find the distinction unconvincing.

This happened in *Darby v Haywood* [2020] NZFLR 919. This case involved a married couple. The wife was the sole shareholder and director of a Company which owned a property.

The husband filed a Notice of Claim under s 42(2) of the PRA against the property which the wife resisted on the grounds that the Company was quite separate from her – even though she was its sole shareholder and director. Judge E B Parsons was not convinced by this explanation and she ignored the distinction, relying on the judgement of the Supreme Court in *Clayton v Clayton (Vaughan Road Property Trust)*.[16]

> *"Within the contest of this application, where the respondent is the sole director and shareholder of a Company, of which he alleges is a trustee of a Trust there is a need for 'worldly realism'."*[17]

As I shall mention shortly the term "*worldly realism*" derives from an English decision.

In *Clayton* the Supreme Court said that the PRA is a piece of social legislation and that '*strict concepts of property law may not be appropriate in the relationship property context*.' Judge Parsons said it would be strange for the Notice of Claim to lapse on the ground that the registered owner was not party to the proceedings when the respondent was the only person or entity involved with the Company and she was present in the Court when the matter was argued.[18]

---

14 Paragraph 20
15 Paragraph 22
16 [2016] NZSC 29
17 Paragraph 45
18 Paragraph 45

Judge Parsons referred with approval to a judgment that Judge Pidwell delivered in *Bourne v Baker*[19] where Judge Pidwell had said:

> *"Importantly, the Supreme Court's comments [in Clayton] were also relied upon at [21]*
>
> > *The property definition in s 2 of the PRA must be interpreted in a manner that reflects the statutory context. We see the reference to 'any other right or interest' when interpreted in the context of social legislation, as the PRA is, as broadening traditional concepts of property and potentially inclusive of rights and interests that may not, in other contexts, be regarded as property rights or property interests."*[20]

Judge Parsons said:

> *"Whether the strict concepts of property law remain appropriate in the relationship property context where the Supreme Court speaks of a 'worldly realism' being required within the social legislation of the PRA is the crux of the matter."*[21]
>
> *"I endorse the comments made by [Judge Pidwell] in Bourne v Baker where she commented that it would be unjust for a Notice of Claim to lapse where a party is the only person involved in the Company."*[22]
>
> *"Ms [Haywood] is the sole director and the sole shareholder of [Company X] which owns [Property A]. She is also one of two trustees and a discretionary beneficiary in [Property B] in which she lives with the parties' children."*[23]
>
> *"I find that the parties were in a qualifying relationship under the PRA and that there is an arguable case that [the husband] has an arguable and valid claim to each of those properties under the PRA."*[24]

The *Clayton* decision involved the meaning of the term "*property*" in the PRA, where it is defined broadly:

> "*Property includes –*
> *….*

---

19 [2016] NZFLR 944
20 Paragraph 46
21 Paragraph 49
22 Paragraph 50
23 Paragraph 51
24 Paragraph 52

(e) any other right or interest.**"**

The Supreme Court appeared to be sympathetic to the argument for Mrs Clayton that "*the PRA is social legislation, which justifies a broader approach to concepts of property than may be appropriate in relation to laws dealing with the property of strangers*."[25]

Counsel for Mrs Clayton contended that "*the concept of property, should, in this context, be regarded as having a degree of fluidity and as having the capacity to change to meet social conditions*."[26]

The Supreme Court said:

> *"We see the reference to 'any other right or interest' when interpreted in the context of social legislation, as the PRA is, as broadening traditional concepts of property and as potentially inclusive of rights and interests that may not, in other contexts, be regarded as property rights or proper interests."*[27]

Quoting from *Charman v Charman (No 4)* the Supreme Court said[28] that it should bring "*a judicious mixture of worldly realism and of respect for the legal affairs of trusts, the legal duties of Trustees and, in the case of off-shore trusts, the jurisdictions of off-shore Courts*."[29]

In *Bourne v Baker*[30] a Notice of Claim under s 42 of the PRA was lodged against a property that was owned by a Company of which a Mr B was the sole director and shareholder. He filed a notice for the claim to lapse the claim but this request was refused with the Judge saying:

> *"Within the context of this application, where the respondent is the sole director and shareholder of a Company, of which he alleges is a trustee of a trust, there is a need for 'worldly realism.' In the latest Clayton v Clayton (Vaughan Road Property Trust) decision the Supreme Court has acknowledged that the PRA is a piece of social legislation and that 'strict concepts of property may not be appropriate in the relationship property context.' It would be unjust in my view for the Notice of Claim to lapse on the ground that the registered owner was not part of the proceedings, when the respondent is the only person or entity involved in that Company and he was present in Court when the matter was argued."*[31]

The Judge also referred to the statement in *Clayton* that the definition of "*property*" in the PRA was to be interpreted "*in the context of social legislation… as broadening traditional concepts*

---

25 [2016] NZSC 29 Paragraph 29
26 Ibid
27 Paragraph 38
28 Paragraph 77
29 *Charman v Charman (No4)* [2007] EWCA Civ 503, [2007] 1 FLR 1246
30 [2016] NZFLR 944
31 Paragraph 17

of property and as potentially inclusive of rights and interests that may not, in other contexts, be regarded as property rights or property interests."[32]

This is a not a case where the Company was a corporate trustee but it can be seen to reflect a Court's reluctance to accept a division between an asset of a human and an asset of a Company of which the human was the sole shareholder and director.

***Brkic v White & Others* [2021] NZCA 670**

In this case a creditor claimed that a Ms White had an interest in a Trust which was "*tantamount to ownership*" of land owned by the Trust and that the creditor could obtain a charging order over the land and sell it to recover a judgment debt owed by Ms White. The Court of Appeal held that Ms White's interest in the Trust was not so great. The Trust contained a "*no self-benefit clause*" and it was held that if she was to restructure the Trust so as to be able to take its assets she would be in breach of the no self-benefit clause.

The Court said that the *Clayton* and *Webb*[33] decisions in which it was held that Mr Clayton and Mr Webb respectively had so much control over Trusts that the Trust assets were to be treated as their own did not apply to a creditor's claim since the *Clayton* and *Webb* decisions "*were decided in the context of relationship property proceedings and the approach taken in those cases was not necessarily applicable in a strictly commercial context*…"[34] This was no doubt a reference to the social policy aspect of relationship property litigation which was referred to in the *Clayton* decision.

The creditor argued that Mrs White could appoint a Company as a corporate trustee in the place of herself and her co-trustee and could direct the corporate trustee to distribute the Trust's assets to her but this argument was rejected on the grounds that such an appointment would have constituted a breach of a fiduciary obligation.[35] Dunningham J held that:

> *"Whether or not the power of appointment is fiduciary (though we consider that it is), we agree with the Judge that the power cannot be exercised for a collateral purpose to avoid the restrictions of the no self-benefit clause. It would, as the Judge concluded, be inconsistent with the context which sits behind the Trust's establishment to construe the Trust Deed as permitting Ms White to use her power of appointment to avoid the restriction on self-benefit which constrains the trustees."*[36]

It was therefore held that the reasoning in the *Webb* case did not apply:

> *"We do not consider that reasoning can, without more, be extended to enable to creditor to treat property held on*

32 Paragraph 21
33 *Webb v Webb* [2020] UKPC 22, 3.8.20
34 Paragraph 12
35 Paragraphs 29-35
36 Paragraph 35

> *Trust as, both legally and beneficially, the property of the trustee."*[37]
>
> *"This view is reinforced by the decision in TMSF*[38]*, the case relied upon by the appellants to show a creditor can have an interest in trust property where a debtor has powers of revocation of a trust that are tantamount to ownership. Despite this finding, the Court still had to order that the power of revocation be delegated to the receivers so that they could take possession of the assets of the trust to meet the defendant's creditors. The assets of the trust became available to the creditors only after the trust was revoked. The creditors could not treat the property as beneficially owned by the debtor until that step was taken."*[39]

There are a number of statutes that differ from the *Legler* interpretation

Some New Zealand Acts contains provisions that allow a Court to take into account the "financial resources" of a party or otherwise to treat Trust property as being available to a person who is associated with a Trust.

I refer in particular to the following:

(f) Section 3(c)(i) of the Social Security Act 2018 which provides that the Ministry for Social Development is to take into account that *"where appropriate [people] should use the resources available to them before seeking financial support under this Act*." The discretion given to the Ministry deprives people of the ability to say that assets of a Trust belong elsewhere and that they have no right to them.

(g) Regulation 8(4) of the Legal Services Regulations 2011. These regulations provide that when considering a person's eligibility for legal aid, their relationship to Trusts is to be taken into account.

Regulation 8(5) provides that "*all or part of the assets and income of a trust*" can be treated as "*assets and income of the applicant regardless of the interest of any other person in the trust*."

(h) Subpart 7 of part 8 of the Financial Markets Conduct Act 2013. This provides for orders to ensure that assets are not dissipated during an investigation or during the course of legal proceedings. In *K A No 4 Trustee Limited v The Financial Markets Authority* [2012] NZCA 370 the Court of Appeal considered whether despite the beneficiaries of a discretionary Trust having no "*present proprietary interest*" in the Trust's property it could be said to be arguable that the property was held on their behalf for the purposes of s 60(H)(1)(f) of the Securities Act. The Court of Appeal concluded that the property was arguably held on behalf of the beneficiaries.

---

37 Paragraph 40

38 *Tasarruf Mevduati Sigorta Fomu v Merrill Lynch Bank* [2011] UKPC 17

39 Paragraph 41

Similarly, in *In the matter of Richstar Enterprises Pty Limited v Carey (No 6)* [2006] FCA 814 it was held in Australia that Trust assets were available to a person who was being investigated.

(i) The Criminal Proceeds (Recovery) Act 2009 enables the Court to have access to assets of a Trust.

(j) Section 412 of the Insolvency Act 2006 authorises a Court to look at the "*real nature*" of a transaction.

(k) Section 105(2)(c)(i) of the Child Support Act 1991 empowers a Court to look at "*the financial resources of either parent of a child*."

What does this all mean?

These are my thoughts on the applicability of the *Legler* regime.

(a) The New Zealand Courts have adopted a reasonably traditional method of interpretation for Trusts that are not affected by the PRA. The *Brkic* case illustrates how, in the context of a creditor's attempt to access Trust wealth, the Courts are not likely to "*stretch*" the meaning of words and clauses so as to enable third parties to access it.

(b) What about Trusts that are primarily focussed on protecting relationship property assets?

Will the Family Court uphold a distinction between a person and a corporate trustee of which the person is the sole director and shareholder? The cases of *Darby v Haywood* and *Bourne v Baker* suggest that there will be a reluctance to do so.

(c) What of the use of a corporate trustee where a Trust Deed declares that a trustee is not to self-benefit although the Court in *Legler* allowed the human trustee to self-benefit in her capacity as the sole director of a corporate trustee, I think that regardless of the *Legler* decision some Judges in the case of "*social legislation*" will not agree with this.

(d) The *Legler* case was factually dependent upon the existence of the following clause which allowed a person to be a director of a corporate trustee and a beneficiary:

> *"It is expressly declared [that] a corporate trustee may exercise all the powers and discretions vested in that trustee by this Deed and by law notwithstanding such exercise may in any way directly or indirectly benefit any beneficiary who has any interest (contingent or otherwise) in that trustee whether as director, officer, shareholder or otherwise howsoever."*

For people who wish to follow the *Legler* model, it is necessary to have such a clause.

(e) One of the uncertainties of whether a Court will accept that a person is to be considered as separate from a Company of which the same person is a director and shareholder is whether the appointment of a corporate trustee constituted a fraud on a power. In the *Legler* case the director of a corporate trustee was said to have been innocent and to have had no intention to exploit the Trust for her personal claim – yet she took all of the assets for herself. Some observers may consider the Judge's finding to be charitable.

Determining a person's intentions will always be difficult and there will always be scope for judicial discretion. If discovery is ordered of communications between a lawyer establishing a corporate trustee and the client who is to be its shareholder and director, and the documents record advice that the client will be able to have full control of the Trust and distribute all of its assets to him/herself, there may be a risk that a Court will say that the appointment of the corporate trustee constituted a fraud on a power.

Although having said that, it is not clear to me whether the doctrine of a fraud on a power is even applicable to Trusts in which a human trustee is advised to resign and re-enter the Trust as the director and shareholder of a corporate trustee. The *Montevento* case did not give the doctrine such significance. Even so, if a Trust contains a "*no self-benefit clause*" there must be a risk that a human trustee who resigns and re-enters the Trust as the director and shareholder of a corporate trustee, will be held to have infringed a no self-benefit clause – as was held in the *Brkic* case.

(f) The Supreme Court's attraction to the notion that Trusts should be interpreted with a strong dose of "*worldly realism*" may be seen as consistent to the Government's approach in a number of statutes where it has enacted provisions which allow the Courts to say that assets of the Trust are available to a person – even though the person is no more than a discretionary beneficiary and the Court can "look through" the barriers that stand between the person and the Trust assets. The statutes to which I have referred concern the following regimes:

- Social security payments.
- Investigations under the Financial Markets Conduct Act.
- The proceeds of crime.
- Child support.
- Insolvency.

(g) Even so, I do not foresee that Courts would be likely to allow creditors to access Trust assets on the basis that a debtor could change the terms of a Trust and appoint himself/herself a director and shareholder of a corporate trustee where there is a clear prohibition on self-benefiting. Trusts are too well established in the law for the Courts to treat them all with the cynicism that is inherent in the term "*worldly realism.*"

(h) For the purpose of advising on the wisdom of appointing a corporate trustee of whom a beneficiary is to be the director and shareholder, there appears to be a clear divide between Trusts that are established for creditor protection and Trusts that are challenged in the context of a relationship property dispute. The Supreme Court's "*flexible*" approach to the interpretation of the term "*property*" and the need for "*fluidity*" in the interpretation of relationship property Trusts marks them out for distinct uncertainty.