+ *Trust law*

Constructive trusts for domestic services

By Anthony Grant, Trusts & Estates Litigator

This week's article is about *Judd v Hawke's Bay Trustee Company Limited* [2014] NZHC 3298 (recently upheld by the Court of Appeal). It concerns the circumstances in which a court will impose a constructive trust over the assets of an express trust.

It is common in second and third marriages/relationships for little relationship property to exist when the relationship ends. This is because assets that existed before the start of the relationship were settled on trusts, and moneys that are earned during the relationship have been spent on living expenses.

Many judges tend to think it unfair that spouses should get nothing after their time together and they have been imposing constructive trusts over the assets of express trusts that have supposedly benefited the "disadvantaged" parties.

The theory of this area of law is that if one spouse has added value to a trust that owns the house in which they live, it is not fair that the beneficiaries alone should get that value. The spouse should be remunerated by the imposition of a constructive trust to the value of the gain that the trust has received from the spouse's endeavours.

As you will see, the *Judd* decision is at the extreme edge of this part of the law – if not right off the edge. I will refer to the parties as "him"/"he" and "her"/"she".

When they got together, he had had two previous marriages and had learned that, if he was to protect his assets from further losses, they should be settled on a trust. By the time he met her, the house in which they would live was owned by a trust. She, too, had had more than one relationship and they both had children from their prior relationships. The marriage only lasted for six and a half years.

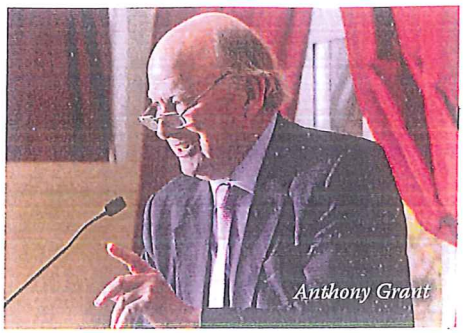
The trust that he established had two trustees: himself and a corporate trustee that was established by an accountant. She knew that the house in which they lived was owned by a trust and she knew she was not a beneficiary of the trust. She would have also been well aware that, having had two prior marriages, he was keen to preserve the house for himself and his children in case his marriage to her should fail.

His hopes were dashed.

When they separated, she sought a constructive trust to the value of 40% of the trust-owned property. She claimed both direct and indirect contributions. Her contributions included "gardening and landscaping", "maintenance of the house (albeit to a minor degree)", and "caring for [him] and his sons" (see para [52]).

The indirect contributions included the freeing up of his time which had enabled him "to pursue his business interests".

The interesting feature about this case is that contributions to an asset are invariably said to have enhanced the value of the asset so that it is unfair for the beneficiaries to gain the extra value without having to pay compensation to the person who added the value.


Anthony Grant

I can think of only three ways to defeat such claims. The first is to live in a tiny apartment with no garden. The second is for the spouse who settled the trust to pay for housekeepers, gardeners and other staff so that the other spouse will not be providing any domestic services. The third and more practical defence is for parties in this situation to insist on entering into pre-nuptial agreements and hope that the courts will not unsettle them.

This was not such a case. None of her actions had added to the value of the property. The property actually fell in value during the course of the relationship.

She relied in part on the fact that she had given him $50,000, which she said was used partially to enhance the value of the house, but he said – and the judge agreed – that he had paid it back.

The fact that her contributions were essentially housekeeping and gardening did not deter the judge from concluding that there should be a constructive trust. Nor did the fact that the house and garden had dropped in value while she did these things. The judge held that she should be awarded $10,000 for each of the years that she spent with him so that an award was made of $65,000.

How could a judge find that "contributions" to a property that was falling in value justified any form of compensation? This was the judge's answer (see para [73] of the High Court decision):

> "... [C]ontributions that directly or indirectly maintain property value will also generate entitlements ... This means that even in a falling market and even in respect of an over-capitalised property, contributions can have proprietary effects."

The *Judd* decision will put many family trusts at risk in circumstances where a pre-relationship house has been settled on a trust and that property has become the family home. In almost all New Zealand marriages, it is common for a spouse to perform some domestic services, and *Judd* appears to say that domestic services justify the imposition of a constructive trust.

The Court of Appeal has upheld the High Court decision, saying that the house was large (it had four bedrooms) and the garden was "substantial" (see *Hawke's Bay Trustee Company Limited v Judd* [2016] NZCA 397). It says the sum of $65,000 is equivalent to "$200 a week for the course of the marriage" and that, by living rent free in the house, the wife saved an additional sum of $200 per week. The benefit to the wife of $400 per week for each week of the marriage was considered to be "reasonable".

On the basis of this decision, most spouses who live in a trust-owned house will be seeking a constructive trust of $400 per week for each week of their relationship.

I can think of only three ways to defeat such claims. The first is to live in a tiny apartment with no garden. The second is for the spouse who settled the trust to pay for housekeepers, gardeners and other staff so that the other spouse will not be providing any domestic services. The third and more practical defence is for parties in this situation to insist on entering into pre-nuptial agreements and hope that the courts will not unsettle them.

Section 21J(4)(d) of the *Property (Relationships) Act 1976* enables the courts to set such an agreement aside if it "has become unfair or unreasonable in the light of any changes in circumstances since it was made". The time has come for Parliament to get rid of this provision and allow people to organise their relationships with certainty. The Law Commission is about to embark on a review of spousal rights and entitlements and one of the changes that I hope it will recommend is that pre-nuptial agreements should be given much greater certainty than currently exists. It is socially objectionable that men and women should be deterred from entering into relationships because of perpetual uncertainty about the state of our ever-changing laws.

In addition to the regular articles Anthony Grant is writing for Law News, *and because there are more developments in the law of trusts and estates than space here allows for, he is also publishing an occasional electronic newsletter entitled "Grant's Trusts & Wills Report", in which he refers to a number of recent developments. Issue 1 has already been sent out, but for readers who have not received it or who would like to receive this newsletter, please email Anthony Grant at anthony@trusts-wills-disputes.nz and ask to be put on the mailing list.*