

How the ‘proper purpose’ rule should be applied to trusts

Trustees may have powers to amend a trust, to resettle it, to appoint and remove trustees, to appoint and remove beneficiaries and so on, but none of these powers can be safely exercised unless it is aligned with the ‘proper purpose’ of the powers

Anthony Grant

This week’s article is concerned with the decision of the Privy Council in *Grand View Private Trust Co Limited & Anor v Wen-Young Wong* [2022] UKPC 47.

In 2001, two brothers settled Trust A for the benefit of their children. On the same day, they created Trust B which was what I will call a quasi-charitable trust which held several billion dollars’ worth of assets.

In 2005, the trustee of Trust A added Trust B as a beneficiary of Trust A. It then removed all the previous beneficiaries of Trust A and distributed all of Trust A’s assets to Trust B. In short, all the original beneficiaries of Trust A were removed as beneficiaries and all of the Trust’s assets were distributed to a new beneficiary.

The decision to do these things was made at the request of the settlors of both trusts. They reasoned that the beneficiaries of Trust A would be inheriting sufficient wealth from other sources and that Trust A was no longer needed for their benefit.

There is no doubt that Trust A was originally intended to benefit the children of the two founders: the trust deed provided that on the expiration of the trust period, the trust fund was to be divided equally between them.

Some of the children challenged these decisions. One of their arguments was that the power to appoint and remove beneficiaries had not been exercised “for the purposes for which they were conferred” and they sought a declaration that the assets transferred from Trust A to Trust B were held on either a resulting trust or a constructive trust for the benefit of the original beneficiaries of Trust A.

The Privy Council held that the power in the trust to appoint and remove beneficiaries was a fiduciary power and the exercise of the power was subject to duties and restrictions imposed by equity [51]. The board considered it had to identify the purpose for which the powers had been granted. This is “the proper purpose rule” – the means by which equity controls the exercise of a fiduciary’s powers in respects not spelled out in a trust deed.

In the past, the proper purpose rule was generally referred to as a “fraud on a power” but the board said the term “fraud on a power” was inappropriate. “There is much to be said for discarding this historical language and referring instead to the proper purpose rule.” [56]

It held that the proper purpose of a power is to be determined at the date when the deed of trust was created. [61]

The board concluded, “it is generally the case that fiduciary

powers conferred on a trustee of a trust with identified beneficiaries must be exercised to further the interests of the beneficiaries” [120] and that the power to remove the beneficiaries of Trust A and replace them had been undertaken for an improper purpose. [122]

The Privy Council’s reasoning is not confined to the power to remove beneficiaries. It extends to all powers that exist in a trust. It will, for example, apply to a power to vary the terms of the trust.

The decision raises important questions about changes that will typically occur with a settlor’s intentions for the objectives of a trust.

At the time a trust is created, a settlor may generally intend that the purpose of a trust is X. But as decades go by, the settlor may intend that the trust is to fulfil purpose Y. A lesson from the *Grand View* case is that if a settlor wishes to preserve the right to change the purpose or objectives of a trust, he/she should use wording which enables a court to interpret the proper purpose of the trust as encompassing both purposes X and Y.

I suspect most New Zealand lawyers are not aware that the “proper purpose” doctrine has been expressly embedded in the Trusts Act 2019.

It can be seen from ss 4(a), 21, 26(b) and 27. Sections 4(a) and 21 provide that trustees must have regard to the “objectives” of a trust. These will align closely with a trust’s “purpose”.

Section 26(b) provides that “a trustee must... further the permitted purpose of the trust...” Section 27 is the most significant of the provisions in the Trusts Act. This provides that “a trustee must exercise the trustee’s powers for a proper purpose”.

Because New Zealand courts have tended to focus on the words “fraud on a power” and not on the words a “proper purpose”, I think it likely that many practitioners will be less familiar with the requirement that trustees must exercise powers only “for a proper purpose”.

The Privy Council’s decision in the *Grand View* case can be seen as an illustration of the requirements of s 27. Although trustees may have powers to amend a trust, to resettle it, to appoint and remove trustees, to appoint and remove beneficiaries and so on, none of these powers can be safely exercised unless it is aligned with “the proper purpose” of the powers. ■

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