DISCRETIONARY INTERESTS AND RIGHTS TO REPLACE TRUSTEES: CAN THEY BE PROPERTY?

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ABSTRACT

Since the abolition of estate duty in 1992 new types of discretionary trusts have become popular in New Zealand for the purpose of protecting assets. Asset protection trusts have significant effects in areas of law where outcomes depend on a person's ownership of "property", such as the Property (Relationships) Act 1976, the Insolvency Act 2006 and the Family Protection Act 1955. This is because no individual person beneficially owns the property held in a discretionary trust; while the property is subject to being distributed at the trustee's absolute discretion no individual beneficiary is entitled to the property. This thesis concerns the implications of a type of asset protection trust where one of the discretionary beneficiaries is given the right to replace the trustee. This "controlling" beneficiary is in an economically advantageous position because he or she has the choice to appoint a trustee who is likely, but not obliged, to prefer his or her interests to those of the other beneficiaries. Asset protection trusts will create an issue in these areas of law if they mean a controlling beneficiary can be in an economically advantageous position but not own "property". Most existing remedies to this problem operate by directly removing property from the trust. However, these remedies do not always apply and extending them might create further problems because they coercively interfere with private property arrangements. This thesis argues that there is an alternative remedy under established principles of property law, trust law and statutory interpretation that does not interfere with the trust property but instead recognises that the relationship between the controlling beneficiary and the trustee is itself property. The question for this thesis is whether the controlling beneficiary's rights and interests fit within "property" as that term is used in selected statutes. I argue that the meaning of property in these statutes is broad and includes interests that are legally significant, economically significant and that fit within the scheme of the legislation. I then argue that the controlling beneficiary's discretionary interest and right to replace the trustee are both legally and economically significant. The bulk of the thesis is concerned with issues that arise under these heads, notably: the discretionary interests as "mere expectancies", the economic significance of an "expectancy", the legal significance of interests subject to discretions, the role of fiduciary duties in the right to replace trustees and the principles of valuation. I conclude that the thesis argument succeeds in relation to the Insolvency Act 2006 and Property (Relationships) Act 1976 but may not succeed in relation to other statutes such as the Family Protection Act 1955 due to the scheme of that legislation. The importance of this thesis is that it demonstrates the law is able provide a remedy to the problem caused by asset protection trusts without interfering with the trust's other purposes such as succession planning.

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Dedicated to Liz and Otway.

A Note on Style

I have endeavoured to follow the New Zealand Law Style Guide throughout this thesis, however, I have made one exception to the guide. I have not followed the "above n" cross-referencing notation for subsequent citations nor have I used "ibid". All citations in footnotes have been given in full. This liberty is taken because the length of a thesis makes subsequent citation referencing difficult and, as the thesis does not need to be typed or typeset, there is no practical advantage in doing so.

In terms of gendered language I alternate between the genders where there is a neutral singular pronoun rather than referring to both genders in the alternate.

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GLOSSARY OF DEFINED TERMS

asset protection trust – a trust that has a controlling beneficiary or settlor-beneficiary 3

claim-right – a right that correlates with a duty upon another and that can be enforced by bringing a claim in court 96

controlling beneficiary – a discretionary beneficiary who has the power to remove and replace the trustees 4

default beneficiary – a beneficiary who is entitled to receive all or part of any trust property that remains held upon trust after a discretionary power of distribution has ceased to be exercisable – this beneficiary may be contingently entitled or entitlement may be vested in interest (but not possession) 22

discretionary beneficiary - a beneficiary who may receive distributions of capital or income, or other benefits from the trust at the exercise of the trustee's absolute discretion 22

donee – the holder of a power 88, 95

general power of appointment – a power to appoint property to anyone in the world including oneself – usually, an authority to direct trustees to hold trust property for whomever one chooses 97

independent – a trustee who is not eligible to benefit under any of dispositive clauses in a trust deed – that is, a trustee who is not a beneficiary 25

own – to hold a right, interest or thing that is property 36

possibility – an uncertain hope or expectation of becoming entitled to property in the future 61

power – a right that is a choice rather than a claim 96

proprietary – a right that is 'in' or 'attached to' a 'thing' and that can be exercised to prevent strangers from interfering with the 'thing' or to recover the 'thing' from strangers 40

right – an advantage secured by law 96

settlor-beneficiary – a person who establishes a trust and nominates herself as the object of a special power of appointment held by the trustee 3

special power of appointment – a power to appoint property to a limited class of persons. 22

trust – an obligation to utilise property that one owns for the benefit of others and to the exclusion of one's own interest 17

trust-busting – causes of action that removes property from a trust 13

INTRODUCTION

The subject of this thesis is discretionary asset protection trusts.[1] The primary issue this thesis is concerned with is how asset protection trusts relate to areas of law external to trust law, for example, the law governing relationship property and creditor-debtor relationships. This "external" issue arises out of developments in the constitution of trusts over the last two decades. These developments have also led to an issue arising in trust law itself. This "internal" issue is a tension in the relationship between trustees, who are given exclusive control over trust property, and those beneficiaries who are given some control over the trustees. The purpose of this thesis is to provide a solution to the external issue while adhering to the principles that currently govern the internal issue.

This introduction sets out these two issues in order to provide a clear context for the question investigated in this thesis. The case *Genc v Genc*[2] will provide an example of these issues in practice. The internal issue will be discussed first and leads into the external issue. The example case will show how asset protection trusts affect the application of the Property (Relationships) Act 1976 and, if left without a remedy, would produce unfair outcomes. Two different types of remedies to the external issue are discussed: remedies against the property held in the trust and remedies against the beneficiaries of the trust. This finally leads to the thesis question and argument.

I. The Internal Issue – Tension within Modern Trusts

The internal issue arises out of developments in trust practice over the last two decades. These developments correlate to a large increase in the number of trusts.[3] The data plotted in Figure 1 demonstrates the popularity of trusts and estates that file tax returns has increased in New Zealand, especially compared to other jurisdictions.[4] This data does not include trusts that do not earn income and of which there is no record although there is likely to be many thousands of such trusts.

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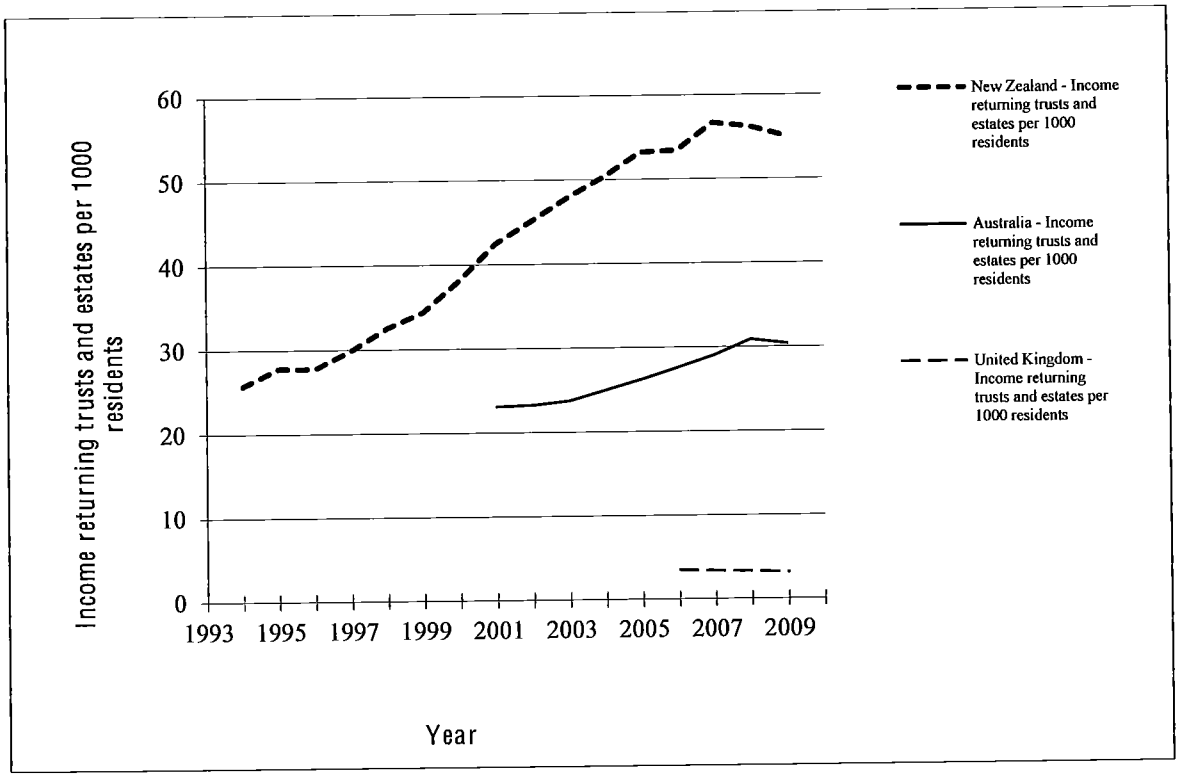
[1] Discretionary trusts are trusts where the trustee is given the absolute power to decide which of two or more discretionary beneficiaries, if any, are to receive a benefit from the trust property. See Chapter One of this thesis for discussion on the nature of a trust and the nature of discretionary trusts.

[2] *Genc v Genc* [2006] NZFLR 1119, 26 FRNZ 67 (HC).

[3] See Law Commission *Some Issues with the Use of Trusts in New Zealand: Review of the Law of Trusts Second Issues Paper* (NZLC IP20, 2010) at [2.1]-[2.7].

[4] There are even fewer trusts per capita in Canada and the United Kingdom (Law Commission *Some Issues with the Use of Trusts in New Zealand: Review of the Law of Trusts Second Issues Paper* (NZLC IP20, 2010) at [2.1]-[2.7]).

Figure 1: Trusts and Estates Returning Income – 1994-2009[5]



The reason for this increase is the subject of enquiry by the Law Commission,[6] but a likely contributing reason is the development of new trust structures that followed the abolition of estate tax in 1992.[7] Estate duty was seen as a restriction on trusts[8] and consequently its removal was seen as enabling a wider range of trust structures.[9] Specifically,

[5] The data for this figure is in Appendix A.

[6] Law Commission *Some Issues with the Use of Trusts in New Zealand: Review of the Law of Trusts Second Issues Paper* (NZLC IP20, 2010).

[7] Estate Duty Abolition Act 1993 which came into force retrospectively on 17 December 1992 (s 1(2)). See also Graeme Kennedy "Business Professionals Seek Asset Protection" The National Business Review (New Zealand, 12 February 1993) at 34; Submission by Andrew Gilchrist to the Law Commission regarding Some Issues with the Use of Trusts in New Zealand: Review of the Law of Trusts Second Issues Paper (NZLC IP20, 2010) (3 May 2011) at 3 [available at <http://www.lawsociety.org.nz/publications_and_submissions/submissions>]); interviews with Ronette Druskovich, Associate at Rainey Collins Lawyers, Wellington and Janet Xuccoa, Chartered Accountant at Gilligan Rowe and Associates, Auckland (Penny Mackay, Insight, Radio New Zealand, 1 May 2011) [available for download at <http://www.radionz.co.nz/national/programmes/sunday/audio/2488222/insight-for-sunday-1-may-2011-family-trusts>]; Kevin Peacock "Top Tips: On Protecting Your Assets in a Trust" New Zealand Herald (New Zealand, 30 November 2008); Romy Udanga "How to Set Up a Family Trust" The Dominion Post (New Zealand, 3 February 2011); Nick Smith "Family Trust Funds Under Siege" New Zealand Herald (New Zealand, 17 June 2011).

[8] See generally DC Potter and HH Monroe *Tax Planning with Precedents* (3rd ed, Sweet & Maxwell, London, 1959) 170-206; WM Patterson, RL Davis and AD Morgan (paper presented to New Zealand Law Society Seminar: Trusts in Transition, 1988).

[9] See Bill Patterson and Maureen Southwick "Family trusts and the impact of the Property (Relationships) Amendment Act 2001" (paper presented to the New Zealand Law Society Trusts Conference, May 2001) 39 at 40; Barry Stafford "The New Zealand Discretionary Trust 40 Years On: Back to First Principles" (paper presented to Auckland District Law Society Seminar: Trusts: Key Selected Issues (Part I), Auckland, March 2004) at 10.

estate duty prevented trusts from being established where the settlor[10] was also a discretionary beneficiary[11] and prevented settlors or other beneficiaries being given special rights that gave power over the trustee.[12] The removal of gift duty in 2011 may increase the use of trusts in the future because it has removed the financial and time costs of gifting programmes.[13]

The removal of estate duty led to trust drafters including new types of provisions, which were previously considered undesirable. It is the inclusion of these provisions that creates the internal issue. The issue is that there is a tension between the rights and expectations of certain discretionary beneficiaries and the duties and powers of the trustee. Tension arises whenever a trust creates a contrast between the formal power of the trustee and the formal power of one or more discretionary beneficiaries. There are many ways this tension can be created but this thesis will exclusively focus on two of the most common developments.[14] In this thesis "asset protection trusts" is used exclusively to mean trusts with either of these developments although in practice a range of different trusts and other legal structures can be used to protect assets.

One development was to include settlors as beneficiaries under discretionary powers. This means a person can settle their property on trust and still be eligible to benefit from it, but not have a fixed beneficial interest in the trust property.[15] Formally, this "settlor-beneficiary" gives the trustee control over the trust property,[16] the absolute power to decide whether or not the settlor-beneficiary will receive any benefit in the future, and the duty to

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[10] The person who establishes the trust relationship by giving property to the trustee to hold on trust or declaring herself to be a trustee of property she owns.

[11] Under the estate duty provisions if the settlor retained any interest in a trust, even a discretionary interest, the settlor's representatives would have to pay estate tax on the value of the trust property. The settlor's reservation of a discretionary interest meant the trust property was deemed to be part of the settlor's estate and tax was payable on the whole (Estate and Gift Duties Act 1968, ss 11-12; *Attorney-General v Heywood* (1887) 19 QBD 326 (QB)). I have found one case in the 19th century before the introduction of estate duty where a settlor did settle a completely discretionary trust where he and his family were the discretionary beneficiaries. The judge considered it to be a novelty: *Holmes v Penney* (1856) 3 K & J 90, 69 ER 1035 (Ch).

[12] See Estate and Gift Duties Act 1968, ss 11-12.

[13] Taxation (Tax Administration and Remedial Matters) Act 2011, s 245.

[14] See Chapter One of this thesis for discussion of what types of trusts this thesis is concerned with and why.

[15] Trusts where a settlor retains a fixed beneficial interest are not new. In fact, they are among the oldest form of trust. However, trusts where the settlor retains a discretionary interest are new. Discretionary trusts were developed in the 19th century after it was confirmed in *Kemp v Kemp* (1801) 5 Ves Jun 849, 31 ER 891 (Rolls) that the courts would not interfere with broadly drafted discretions that gave trustees "absolute" or "uncontrolled" choice. The first use of discretionary trusts for asset protection was spendthrift trusts, which gave trustees the discretion to give income for the maintenance and support of a beneficiary and his family but also allowed them to accumulate the income instead. In the 19th century it was accepted that creditors of the beneficiary could not attach the discretionary interest (see Stuart Anderson *The Oxford History of the Laws of England* (Oxford University Press, Oxford, 2003—) vol 12 at 250-251). However, these trusts could not be settled for the benefit of the settlor as they would usually be void as a fraud on the bankruptcy laws (Stuart Anderson *The Oxford History of the Laws of England* (Oxford University Press, Oxford, 2003—) vol 12 at 251; *Official Assignee v NZI Life Superannuation Nominees Ltd* [1995] 1 NZLR 684 (HC)).

[16] *Financial Markets Authority v Hotchin* [2011] 3 NZLR 469 at [131].

consider benefiting others instead of the settlor.[17] However, the trustee's duties to consider the needs of the other beneficiaries and to make her own decision exist in tension with the fact that she was appointed by the settlor and the property she controls used to belong to the settlor. The expectations and wishes of the settlor-beneficiary, including her wishes regarding how much she should benefit, are likely to significantly influence the trustee's decisions.

The second development was giving a settlor-beneficiary or another discretionary beneficiary a right[18] to replace trustees. The right to replace existing trustees is significantly different from the long established right to appoint new trustees or to fill vacant trusteeships.[19] The right to replace originated with bare trusts in the 19th century[20] and had been retained by settlors in relation to the mirror trusts developed after 1976.[21] However, it was only after the end of estate duty that this right began to be given to discretionary beneficiaries in significant numbers. Usually settlors of asset protection trusts keep the right to replace trustees for themselves, particularly if they retain a discretionary interest; however, sometimes they give these rights to other discretionary beneficiaries, for example, their children.[22] A discretionary beneficiary with a right to replace the trustees will be referred to as a "controlling beneficiary".

There is a contrast between the duties and powers of the trustee and the position of controlling beneficiary. A trustee of a discretionary trust is given an absolute discretion to decide which of the discretionary beneficiaries will receive a benefit from the trust as well as deciding the extent of any benefit and when the beneficiary might receive it. The trustee has duties to all of the discretionary beneficiaries in exercising the discretion and may not act under the directions of the controlling beneficiary.[23] There is tension between these duties and the controlling beneficiary's right to remove the trustee. A trustee who is charged with genuinely exercising an independent decision about which discretionary beneficiaries should benefit but who is subject to being removed by one of those beneficiaries is in a compromised position.

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[17] See Chapter One of this thesis for discussion of trustee's duties.

[18] The term "right" is likely to be controversial. However, it is appropriate and accurate because the broad meaning of "right" is any advantage secured by law (Bryan A Garner (ed) *Black's Law Dictionary* (9th ed, online ed, Thomson Reuters, 2009) "right *n* 3"). Technically the right to replace trustees is made up of a power to remove existing trustees and a power to appoint new or replacement trustees. Powers exercisable at the choice of the holder are an advantage secured by law. Therefore, together these powers give the holder the right to replace the current trustees with new trustees. See Chapter Four of this thesis for further discussion of this point.

[19] These rights were incorporated into the statute book by the Trustee Act 1956, s 43.

[20] See *London and County Banking Company v Goddard* [1897] 1 Ch D 642 (Ch) for the earliest example of a right to remove a trustee which I have found. It occurred in a bare trust under a mortgage arrangement.

[21] See Bill Patterson and Maureen Southwick "Family trusts and the impact of the Property (Relationships) Amendment Act 2001" (paper presented to the New Zealand Law Society Trusts Conference, May 2001) 39 at 40. However, I cannot find examples of mirror trusts where discretionary beneficiaries were granted powers of control in the law reports prior to the abolition of estate duty.

[22] See generally Pravir Tesiram "Drafting Trust Deeds" (paper presented to New Zealand Law Society Conference: Trusts, June 2007) 37 at 41-42.

[23] See Chapter One of this thesis for discussion of the duties and obligations of a trustee.

A controlling beneficiary can be compared to a litigant with the power to choose the judge who will decide her case, particularly a judge exercising a discretion. A litigant with this power could not make the decision for the judge, could not direct the judge, and could not reverse the decision of the judge if she did not like that decision; however, she could choose a judge who would be more likely to decide in her favour. This would give the litigant a form of indirect control over the decision making process.

This tension is illustrated by *Genc v Genc*.[24] Shortly before Mr and Mrs Genc commenced a de facto relationship Mr Genc settled a trust. He did this by transferring his house and business to trustees on the condition that the trustees utilise the property for the benefit of the beneficiaries. Mr Genc included himself as a discretionary beneficiary. The other beneficiaries were Mr Genc's children. Mr Genc appointed himself and his solicitor as trustees. He gave himself and his solicitor, as trustees, an absolute discretion to decide which of the beneficiaries would benefit from the trust property and how they would benefit. The discretion could only be exercised unanimously by both trustees, which meant that Mr Genc needed his solicitor's cooperation before he could benefit from his former property. According to established principle the solicitor was obliged to consider all of the beneficiaries and to make his own decision rather than simply doing what Mr Genc wanted.[25]

The duties that the solicitor was subject to as trustee were in tension with the fact that Mr Genc originally appointed the solicitor as trustee and retained for himself the right to remove trustees. The solicitor had a duty to consider all of the beneficiaries and to not act under Mr Genc's direction, but was subject to being removed by Mr Genc at any point. If the solicitor's genuine exercise of discretion resulted in him not agreeing to act as Mr Genc wished his to act then the solicitor would likely be removed and replaced with someone who was more likely to make a decision that matched Mr Genc's.

This tension had a significant effect on Mr Genc's position. He had given away his property. The only means by which he could get any part of it back was if he and the solicitor decided to grant him an entitlement to it. The possibility that this would occur was subject to his solicitor's independent decision, which means Mr Genc could not force his solicitor to agree to distribute property to him. However, because Mr Genc was also a trustee he could prevent the solicitor distributing the trust property contrary to Mr Genc's wishes. More importantly, if the solicitor appeared unlikely to agree, Mr Genc could remove the solicitor and replace him with someone who was likely to agree. These two facts, Mr Genc's eligibility to be given property and his ability to alter the probability of that happening, put Mr Genc in an economically significant position.

The position of a controlling beneficiary, and to a lesser extent a settlor-beneficiary, creates an issue for trust law. The Law Commission's review of trust law is currently

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[24] *Genc v Genc* [2006] NZFLR 1119, 26 FRNZ 67 (HC).

[25] See Chapter One of this thesis for discussion of the trustee's duties.

examining whether or not trusts that include controlling beneficiaries or settlor-beneficiaries should be allowed by trust law.[26] Apart from the review, trust law appears to be currently settled in favour of accepting these beneficiaries. This thesis starts from the assumption that controlling beneficiaries (and settlors) are compatible with trust law as it currently stands.[27] The issue that is of concern to this thesis is the effect that the existence of asset protection trusts with controlling beneficiaries have on areas of law outside of trust law.

II. The External Issue – Asset Protection Trusts and Other Areas of Law

In many areas of law a person's legal position is determined by whether or not he owns property.[28] For example, one area is the enforcement of debts, both before and after bankruptcy. The High Court Rules and the Insolvency Act 2006 provide mechanisms by which a debtor's property can forcibly be taken from a debtor to satisfy his debts. As a general rule property that a debtor does not own is not subject to these mechanisms and cannot be used to satisfy his debts. There are some remedies that override the general rule but these will be discussed later.

In any such area the person's position could be affected by his relationship with an asset protection trust. The effect of the trust is clearest on a settlor-beneficiary but also occurs for a controlling beneficiary who is not a settlor. The effect is best explained in a series of discrete steps. The external issue is the unfair outcomes that would be produced by the effect of these trusts if there were no remedy.

The first step is when a settlor gives property away to trustees.[29] By doing this the settlor gives away legal ownership of that property to the trustees. The settlor no longer owns that property in law. The settlor might own all or part of the property in equity if the trust is a fixed trust and she retains an equitable interest or she might give the equitable ownership to one or more others.

The second step is when the settlor gives property to a discretionary trust rather than a fixed trust. This is a trust where the trustee is given an absolute power to distribute the trust property between the beneficiaries. Because the trustee must choose who receives any trust property no individual beneficiary is entitled to the property while it is held on trust and subject to the trustee's power.

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[26] Law Commission *Some Issues with the Use of Trusts in New Zealand: Review of the Law of Trusts Second Issues Paper* (NZLC IP20, 2010) at [5.1]-[5.7].

[27] See Chapter One of this thesis.

[28] These areas include, but are not limited to the: Insolvency Act 2006, High Court Rules, Property (Relationships) Act 1976, Family Protection Act 1955, Law Reform (Testamentary Promises) Act 1949, Legal Services Act 2011, Social Security Act 1964, Child Support Act 1991, Criminal Proceeds (Recovery) Act 2009, and Income Tax Act 2007.

[29] In other words, settles a trust.

During the first half of last century there was a doctrine that if there were "default beneficiaries"[30] of the trust, that is, beneficiaries who were entitled to the residue of the trust property after it ceased to be subject to the trustee's discretionary power of distribution, then those default beneficiaries were considered to be the equitable owners, either vested or contingent, of the trust property during the entire trust period.[31] However, this understanding is no longer accepted in the highest courts in Australia and the United Kingdom and should not be accepted in New Zealand.[32] In any event, even if this doctrine were still applicable in New Zealand, to the effect that default beneficiaries had a current interest in the trust property, it could not be reasonably argued that they were entitled to the entire trust property while it was subject to the trustee's discretion.

Therefore, the effect of property being held on discretionary trusts is that for all practical purposes, the property is not owned by anyone as an individual.[33] This means that the trust property is not relevant to, or subject to, any area of law that determines outcomes based on a person owning property. For example, property held on discretionary trusts is not included as property of a debtor under the Insolvency Act 2006. Therefore, when a debtor is bankrupted the trust property does not vest in the Official Assignee but remains in the hands of the trustee to distribute according to her powers and duties under the trust.

The same effect occurs in the Property (Relationships) Act 1976 context. The distinction between property owned by one or both parties to a relationship and property owned by neither party is fundamental to the operation of the Property (Relationships) Act 1976. The starting point is that property that is held on discretionary trusts is not "property of" the party in question. The example of *Genc v Genc* demonstrates the effect this has from Mrs Genc's perspective.

The case arose as a claim brought by Mrs Genc after she and Mr Genc separated. The trust that Mr Genc had set up affected Mrs Genc's rights under the Act. If Mr Genc had never settled his house on the trust, then Mrs Genc would, prima facie, have been entitled to half of the house's value as it would have been classified as "relationship property" owned by Mr Genc and would most likely have been divided equally.[34] She may also have been entitled to a claim against some of the value of Mr Genc's business.[35] However, because both the house

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[30] See Chapter One of this thesis for a description of "default beneficiaries".

[31] *Re Brooks' Settlement Trusts* [1939] Ch 993 (Ch).

[32] *Pearson v Inland Revenue Commissioners* [1981] AC 753 (HL); *Chief Commissioner of Stamp Duties v Buckle* [1998] HCA 4, 192 CLR 226.

[33] It can be said to be owned collectively by all of the beneficiaries and discretionary beneficiaries, but this gives no individual beneficiary any entitlement to the trust property. See Chapter Three of this thesis.

[34] They lived in the house as their family home which, when owned by one or both of the parties, is relationship property. See Property (Relationships) Act 1976, s 8(1)(a); *Genc v Genc* [2006] NZFLR 1119, 26 FRNZ 67 (HC) at [6].

[35] If it had increased in value due to her contributions or the application of relationship property. See Property (Relationships) Act 1976, s 9A; *Rose v Rose* [2009] NZSC 46, [2009] 3 NZLR 1; *Genc v Genc* [2006] NZFLR 1119, 26 FRNZ 67 (HC) at [78], [94].

and business had been settled on the trust they were not "property" that was "owned" by Mr Genc under the Property (Relationships) Act 1976.[36] Therefore, these assets did not come within the provisions of the Act that apply to the division of the property of the parties to the relationship.

The final step is the combination of the effect of a discretionary trust and the effect of a controlling beneficiary. If there were no remedy this combination would produce unfair outcomes. The unfairness lies in the contrast between the property in the discretionary trust being unowned and the economically advantageous position of the controlling beneficiary. The controlling beneficiary is economically better off due to his position in relation to the trust property but his creditors cannot claim the trust property because the controlling beneficiary is not directly entitled to it.

The unfairness of this outcome is demonstrated by Mr Genc even though Mr Genc settled his trust before his relationship with Mrs Genc commenced. If Mr Genc had given his property away to his children or had settled it on discretionary trusts that excluded himself then there could be little argument that it was unfair to Mrs Genc.[37] What made this case unfair was that Mr Genc gave his property away to the trustees of an asset protection trust, of which Mr Genc was the controlling beneficiary. On one hand, this trust meant that Mrs Genc left the relationship without being able to claim against any substantial relationship property. On the other hand, Mr Genc departed the relationship in a significantly advantageous economic position due to being the controlling beneficiary of a trust with valuable property. There can be little doubt that Mr Genc was likely to continue to benefit significantly from his trust after the separation, nor that he had significant influence over that likelihood.

The charge of unfairness is a value judgment and is subject to debate.[38] The existence of this debate means that this thesis is important because it affects the limits and assumptions of

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[36] Property (Relationships) Act 1976, s 2.

[37] Historically, trusts were used as asset protection devices by this means. They were conceptually the same as any gift of property. Settlors would give their property away to trustees but the settlors did not retain any interest in the property themselves. They would settle it for the exclusive benefit of their children or other relatives. This would protect the trust property from any claims brought against the settlor, bar the effect of specific remedies which might claw the property back into the settlor's hands. This historic type of asset protection is conceptually different from the asset protection trusts which are of concern today.

[38] This debate is found in the legal profession, judgments, academia and the media.

Some in the legal profession have expressed concern with the developments in trust law, at least in relation to some areas of law (see Barry Stafford "The New Zealand Discretionary Trust 40 Years On: Back to First Principles" (paper presented to Auckland District Law Society Seminar: Trusts: Key Selected Issues (Part I), Auckland, March 2004) at 10; submission by Andrew Gilchrist to the Law Commission regarding *Some Issues with the Use of Trusts in New Zealand: Review of the Law of Trusts Second Issues Paper* (NZLC IP20, 2010) (3 May 2011) at 17 [available at <http://www.lawsociety.org.nz/publications_and_submissions/submissions>]). Others in the profession suggest that these developments are beneficial for society as a whole (Bill Armitage and others (New Zealand Law Society Seminar: Asset Protection, August-September 1996) at 1; submission by Andrew Gilchrist to the Law Commission regarding *Some Issues with the Use of Trusts in New Zealand: Review of the Law of Trusts Second Issues Paper* (NZLC IP20, 2010) (3 May 2011) at 3 [available at <http://www.lawsociety.org.nz/publications_and_submissions/submissions>]); Interviews with Ronette Druskovich, Associate at Rainey Collins Lawyers, Wellington and Janet Xuccoa, Chartered Accountant at

the debate. However, the value judgment of unfairness is not strictly relevant to my thesis, which is focused purely on whether there is in fact a remedy against such an outcome under the current law. My argument is that under a conservative application of existing principles of statutory interpretation, property law and trust law there is such a remedy.

III. Remedies for the External Issue

The external effect of asset protection trusts has two conceptually distinct types of solution. The first type of solution, the "direct" solution, is to provide remedies that take effect directly on the trust property, usually by reversing the initial transfer of property into trust. For example, the Property Law Act 2007 allows specific transactions to be reversed and

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Gilligan Rowe and Associates, Auckland (Penny Mackay, Insight, Radio New Zealand, 1 May 2011) [available for download at <http://www.radionz.co.nz/national/programmes/sunday/audio/2488222/insight-for-sunday-1-may-2011-family-trusts>]).

In the courts some judges have made comments on these types of trusts in certain areas; this is significant because the judges have impliedly criticised counsel for not arguing against the effect of these types of trusts (*Walker v Walker* [2007] NZCA 30, [2007] NZFLR 772 at [48]; *Harrison v Harrison* (2008) 27 FRNZ 202 (HC) at [14]). However, other judges have suggested that asset protection is a legitimate purpose for trusts (*N v T* [2006] NZFLR 885, 25 FRNZ 840 (FC) at [47]; *Worn v Buxton* HC Auckland M125-SDO1, 17 June 2002 at [35]; *Taranaki Regional Council v Mouland* DC New Plymouth CRI-2008-021-1238, 16 November 2010 at [20]).

Academics have written substantially on these types of trusts both in New Zealand and abroad, some finding problems with asset protection trusts and others dismissing those problems (Nicola Peart "Can Your Trust be Trusted?" (2009) 12 Otago LR 59; Nicola Peart "Intervention to Prevent the Abuse of Trust Structures" [2010] NZ L Rev 567; Sue Tappenden "The Family Trust in New Zealand and the Claims of 'Unwelcome Beneficiaries'" (2009) 2 Journal of Politics and Law 17; Elena Marty-Nelson "Offshore Asset Protection Trusts: Having Your Cake and Eating It Too" (1994) 47 Rutgers L Rev 11; Ritchie W Taylor "Domestic Asset Protection Trusts: The 'Estate Planning Tool of the Decade' or a Charlatan?" (1998) 13 BYU Journal of Public Law 163; Randall Gingiss "Putting a Stop to 'Asset Protection' Trusts" (1999) 51 Baylor L Rev 987; Stewart E Sterk "Asset Protection Trusts: Trust Law's Race to the Bottom?" (1999) 85 Cornell L Rev 1035; Henry J Lischer Jr "Domestic Asset Protection Trusts: Pallbearers to Liability?" (2000) 35 Real Property, Probate and Trust Journal 479; Adam J Hirsch "Fear Not the Asset Protection Trust" (2005) 27 Cardozo L Rev 2685; Darsi N Sirknen "Domestic Asset Protection Trusts: What's the Big Deal?" (2006) 8 Transactions 133).

In the media there has been significant debate and much of the debate portrays these trusts as having an unfair effect, especially in relation to property developers, finance company directors and politicians (Vernon Small "Well-Off Families Rort System" *Dominion Post* (New Zealand, 18 August 2009); Claire Trevett "Key Attacks Rich People who Claim Welfare" *New Zealand Herald* (New Zealand, 19 August 2009); Rob Stock "DIY Trusts Under Siege" *Sunday Star Times* (New Zealand, 1 August 2010); Rob Stock "Wake-up Call for Mum and Dad Trustees" *Sunday Star Times* (New Zealand, 1 August 2010); Nick Smith "Family Trust Funds Under Siege" *New Zealand Herald* (New Zealand, 17 June 2011); Damien Grant "Trusts Industry a Costly Sham" *New Zealand Herald* (New Zealand, 8 May 2011); Bernard Hickey "Havens for Rich Tax Avoiders will Cripple New Zealand" *New Zealand Herald* (New Zealand, 8 May 2011); Damien Grant "King Henry didn't Trust Wily Landowners" *New Zealand Herald* (New Zealand, 31 July 2011); Maria Slade "Finance chief judged bankrupt" *The New Zealand Herald* (New Zealand, 8 August 2008); Phil Taylor "Failed and Bankrupt - But Comfortably Broke" *The New Zealand Herald* (New Zealand, 23 August 2008); Phil Taylor "Blue Chip – The Missing Millions" *The New Zealand Herald* (New Zealand, 27 March 2010); Kelly Gregor "Petricevic's Legal Aid Bid 'A Joke'" *New Zealand Herald* (New Zealand, 19 January 2011) Nick Krause "Legal Fight Over Petricevic Family Trust" *Stuff.co.nz* (New Zealand, 1 June 2010); Nick Krause "Bridgecorp Judge Slates Insolvency Law" *The Dominion Post* (New Zealand, 2 June 2010); Tony Wall "Bankrupt Living it Up" *Sunday Star Times* (New Zealand, 9 September 2007); Vernon Small and Tracy Watkins "Fresh Housing Woes for English" *The Dominion Post* (New Zealand, 9 September 2009)). However, others suggest that even though asset protection trusts may be unfair in particular circumstances overall they provide a benefit to society (Martin Hawes "Greater Good is Served by Using Family Trusts" *New Zealand Herald* (New Zealand, 31 August 2008); Nick Smith "Family Trust Funds Under Siege" *New Zealand Herald* (New Zealand, 17 June 2011) [reporting on an interview with Stuart Cummings]).

property that has been given away to be clawed back for the benefit of creditors. The second type of solution, the "indirect" solution, is to identify that a particular beneficiary's personal relationship with the trustee, as established under the trust, is property. The distinction between the two solutions is that the former takes property out of the trust and the latter leaves the trust as it is established. This thesis argues that the second solution can be applied to discretionary asset protection trusts.

The direct solution is usually preferable from the perspective of those disadvantaged by asset protection trusts because these solutions allow direct access to trust assets. However, these solutions are not available or appropriate in all circumstances.

One prominent remedy that applies the direct solution is the Property Law Act 2007.[39] This Act continues the traditional prohibition against insolvents giving property away before they are bankrupted.[40] It allows any gift or any other transaction that is made with intent to prejudice creditors to be reversed if the person making the transaction was either: unable to pay his debts as they fell due; about to engage in a transaction with unreasonably few assets; or likely to incur debts beyond his ability to pay.[41] The establishment of an asset protection trust will fall outside this remedy if the settlor was able to pay his debts as they fell due and not about to commence financially risky activity.

Similar remedies are found in the Insolvency Act 2006. The trust will fall outside of this Act's remedies if the trust property was gifted to the trustees more than two years prior to bankruptcy and more than five years prior if the gift was made when the debtor had more total liabilities than total assets.[42] It follows that with careful planning settlors can establish asset protection trusts that avoid these remedies.

Similar transaction based remedies apply in the property relationships context. Section 44 of the Property (Relationships) Act 1976 allows the transactions made by one party with intent to defeat the other party's rights under the Act to be reversed.[43] Further, section 44C provides that when relationship property is settled on a trust with the effect of defeating a party's rights under the Act the court may order compensation. However, this is limited because it only allows income to be clawed back from the trust not the capital. In *Genc v Genc*, Mrs Genc made claims under these remedies but did not succeed.[44] It is possible that

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[39] Property Law Act 2007, ss 344-350.

[40] This remedy originates in the Fraudulent Conveyances Act 1571 (UK) 13 Eliz 1, c 5.

[41] Property Law Act 2007, s 346.

[42] Under s 204 of the Insolvency Act 2006 any gifts made within two years of a person's bankruptcy can be cancelled regardless of the person's solvency. Under s 205 any gift made within five years of bankruptcy can be cancelled if the bankrupt was balance sheet (rather than cash flow) insolvent at the time of the gift.

[43] This remedy follows the same formula as s 60 of the Property Law Act 1952 which preceded the current Property Law Act 2007.

[44] Under s 44C of the Property (Relationships) Act 1976 she did not succeed because the trust was established before the relationship and, therefore, the trust property had never been relationship property.

Mrs Genc's claim under s 44 would succeed if the case were heard today as more recent cases have clarified the meaning of intent in these types of provisions;[45] however, this remedy was not seriously considered viable in the High Court.[46] Mrs Genc also attempted to make a claim directly against the trustees to the effect that they held some of the trust property on constructive trust for her. This also failed.[47]

These types of direct remedies can be effective but, as shown above, are not always available. Part of the Law Commission's review has been to ask whether they should be extended. There are two problems with extending these types of remedies. First, they provide a relatively inflexible tool. For example, the Property Law Act 2007 remedy applies to all transactions not only transfers of property onto asset protection trusts. Extending the scope of this remedy would allow a wide range of transactions to be reversed and would significantly reduce certainty of title to property. Second, extending remedies that attach directly to trust property would override the powers and duties granted to the trustees over that property. Parliament has at times given the courts such powers, for example s 182 of the Family Proceedings Act 1980,[48] however, they are not ideal. Extending these types of remedies means that the public is directly interfering with private dispositions of property. The coerciveness that these types of direct remedies could embody if they were extended is seen in the operation of the Criminal Proceeds (Recovery) Act 2009, which allows the Crown to seize any property that was under the de facto control of a convicted criminal even if that means overriding other people's property rights.[49]

These problems with the extension of the direct remedies are consistent with Parliament's decision about extending these remedies at the turn of the century with the amendments to the Matrimonial Property Act 1976 (as it was then called[50]).[51] The Working

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[45] At the time of this case precedent held that a conscious intention to defeat a spouses interests needed to be proved before the remedy was available (*Coles v Coles* (1988) 4 NZFLR 621, 3 FRNZ 101 (CA) at 624). Following the Supreme Court's decision in *Regal Castings Ltd v Lightbody* [2008] NZSC 87, [2009] 2 NZLR 433 the courts have accepted that knowledge of a consequence can imply an intention to bring that consequence about (*Ryan v Unkovich* [2010] 1 NZLR 434 (HC) at [33]). The Supreme Court's decision was on s 60 of the Property Law Act 1952 but that section was is in the same form as s 44 of the Property (Relationships) Act 1976. This is likely to mean s 44 will apply in more cases than formerly. However, the transaction must still be connected with the intention to defeat, therefore, there will need to be evidence of knowledge of the consequences of setting up the trust (See Nicola Peart "Relationship Property and Trusts: Unfulfilled Expectations" (paper presented to New Zealand Law Society Relationship Property Intensive, August 2010) 1 at 15-19; Nicola Peart "Intervention to Prevent the Abuse of Trust Structures" [2010] NZ L Rev 567 at 572-73).

[46] *Genc v Genc* [2006] NZFLR 1119, 26 FRNZ 67 (HC) at [17].

[47] This failed because Mrs Genc's contributions to the trust property were due to her relationship with her husband and she had no reasonable expectation that her contributions would grant her a beneficial interest in the trust property (*Genc v Genc* [2006] NZFLR 1119, 26 FRNZ 67 (HC) at [80]-[93]).

[48] This section gives the court power to vary or alter a trust but only if it was established for the purpose of a marriage and the married couple has divorced. It is a limited remedy.

[49] Criminal Proceeds (Recovery) Act 2009, s 58.

[50] The Property (Relationships) Amendment Act 2001 changed the name of Matrimonial Property Act 1976 to the Property (Relationships) Act 1976.

Group on Matrimonial Property had recommended in 1988 that the Family Court be given power to reverse any transfer of relationship property onto trust.[52] Parliament decided in select committee that this was not appropriate because trusts were created for legitimate purposes and that the courts should not be able to take property directly out of them where the settlor had no intention to defeat the interests of the other party.[53] These comments by Parliament should not be taken as approving the effect of asset protection trusts as there is no evidence that Parliament considered the particular issues with this type of trust and there is other evidence that Parliament does consider them to be a problem;[54] however, it does suggest that Parliament is not eager to extend remedies that operate directly against trust property.

The indirect solution is to recognise the property interests created after the establishment of the trust. This solution does not interfere with the trust property or with the powers and duties of a trustee over that property. Rather it recognises when the beneficiaries of a trust have valuable property as a result of their relationship with the trustee.

Two statutes include a form of the indirect remedy. The Legal Services Act 2011 allows the possibility that a person could receive a benefit under a discretionary trust to be taken into account when establishing her eligibility for legal aid. The legislation allows the Legal Services Agency to take a discretionary beneficiary's economically advantageous position

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[51] Parliament did not extend the remedies in the Insolvency Act 2006 and Property Law Act 2007 when it re-enacted them. Parliament could have done so if it considered that asset protection trusts required this type of remedy. However, there is no evidence that Parliament even considered any issues to do with trusts or asset protection trusts. There was no discussion of potential problems raised by discretionary trusts during the progress of these Bills through Parliament. The Property Law Bill 2007 (89-2), including subpart six of Part six, was based on a report by the Law Commission of considerable vintage (Law Commission Report No 29 *A New Property Law Act* (June 1994, Wellington New Zealand)). Subpart six of Part six received no comment or alteration in Parliament or the Justice and Electoral Select Committee (14 November 2006) 635 NZPD 6460 [1st reading], (11 September 2007) 642 NZPD 11763 [2nd reading], (12 September 2007) 642 NZPD 11826 [in committee], (20 September 2007) 642 NZPD 12115 [3rd reading], Property Law Bill 2007 (89-2) (explanatory note)). Issues surrounding discretionary trusts and creditors were not raised in Parliament or the Law Commission's report (see Law Commission Report No 29 *A New Property Law Act* (June 1994, Wellington New Zealand) at 305-323). Neither were these issues raised in the Parliamentary debates and select committee report on the Insolvency Law Reform Bill 2006 (21 February 2006) 629 NZPD 1318 [1st reading], (5 September 2006) 633 NZPD 5175 [2nd reading], (13 September 2006) 634 NZPD 5441 [2nd reading], Insolvency Law Reform Bill 2006 (14-2) (select committee report)). Therefore, no particular intention can be read into Parliament's lack of action in this case.

[52] Janice Lowe (convener) *Report of the Working Group on Matrimonial Property and Family Protection* (October 1988) at 30.

[53] Government Administration Committee "Matrimonial Property Amendment Bill" [1996-1999] LXVI AJHR 254 at 265.

[54] There are indications that Parliament does consider that there is a problem with asset protection trusts in New Zealand. In 2008 Parliament decided not to progress with the Trustee Amendment Bill (144-2) (9 July 2008) as it did not consider the effect that trust law was having on other areas of law – the external issue as defined above. Before this decision was made the select committee was made aware of issues such as the rights of creditors and the application of the Property (Relationships) Act 1976 to asset protection trusts (Andrew Butler "Supplementary Submission to the Justice and Electoral Committee on the Trustee Amendment Bill 2008" at 1). The Committee's report led to the Law Commission being asked to conduct a comprehensive review of trust law which includes an assessment of the wider problems asset protection trusts (Law Commission *Reivew of Trust Law in New Zealand: Introductory Issues Paper* (NZLC IP19, 2010) at iii; Law Commission *Some Issues with the Use of Trusts in New Zealand: Review of the Law of Trusts Second Issues Paper* (NZLC IP20, 2010) at [1.10]-[1.11]).

into account by including the discretionary interest within "income or disposable capital" and "resources".[55] The Child Support Act 1991 allows a discretionary interest to be taken into account when assessing a person's income to determine liability to pay child support. Discretionary interests can be taken into account as "financial resources".[56] These remedies do not touch the trust at all but instead allow a discretionary beneficiary's economically advantageous position to be assessed.

This type of remedy can be illustrated by considering the outcome if Mrs Genc had been claiming child support from Mr Genc rather than claiming under the Property (Relationships) Act 1976. Mr Genc's relationship with the trust was clearly a financial resource as he was eligible to receive income from the trust and could influence how likely he was to receive income by choosing different trustees. The income that the trust made would have to be taken into account in assessing child support.

An indirect remedy, which only looks to the position of the discretionary beneficiary, cannot attract the same criticisms as the direct remedies. The direct remedies can be criticised as interfering with private property arrangements: they are "trust-busting" remedies. The indirect remedy does not affect the trusts themselves. The duties and powers of the trustees are left intact.

The question for this thesis is whether this type of indirect remedy is available under statutes that do not explicitly authorise the assessment of discretionary interests or specifically include discretionary interests in the meaning of property.

IV. The Thesis Question

This is the question that this thesis seeks to answer. The question is whether or not a discretionary beneficiary or controlling beneficiary has property in selected contexts. The argument made in this thesis is that applying the ordinary principles of statutory interpretation, trust law and property law leads to the conclusion that discretionary and controlling beneficiaries do have property in some contexts, although possibly not in all. The null hypothesis is that discretionary and controlling interests are of such a nature that they cannot be associated with property.

It is important to clarify here that the argument is not that discretionary beneficiaries have equitable interests in the trust property. The hypothesis is that the discretionary beneficiaries' personal rights in relation to the trustee can be recognised as property in and of

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[55] Section 114(1)(h)(v) authorises regulations to be made where property which might be received from a trust to be taken into account in the "calculation of the income, disposable capital, or capital of an applicant for legal aid". The calculation of disposable capital is governed by sch 1 which refers to "assets" and "resources" of an applicant and his or her spouse. This means that an applicant or spouse's discretionary interest is both "income or disposable capital" and a "resource" under the Act (*Petricevic v Legal Services Agency* [2011] 2 NZLR 802 (HC) at [31]-[41]).

[56] The Child Support Act 1991, s 105(2)(c)(i); *B v X* [2011] 2 NZLR 405 (HC) at [101]; *Jaques v Jaques* HC Wellington CIV-2004-485-1226, 31 May 2005 at [5].

themselves. Thus the property held by these beneficiaries is separate from the property held by the trustees, which is left under their control. To a certain extent this argument is related to the concept of a "bundle or rights" that is emerging in family court jurisprudence.[57] To date this concept is not fully formed or coherent so is not relied on by this thesis. However, the "bundle of rights" doctrine also looks to whether the rights and interests a beneficiary has are property in addition to, and separate from, the property held on trust;[58] these rights and interests are the focus of this thesis.

The importance of this hypothesis is that it argues the indirect solution to asset protection trusts is available under the law as it exists today. I argue there is no need for legislation or judicial innovation to pursue this remedy in the courts. Under the current law discretionary and controlling beneficiaries can have property in areas of law where outcomes are determined by that fact.

The focus of this thesis on the above question alone means that a number of related issues are not addressed by this thesis. The internal issue in trust law is not addressed. Currently, trusts with controlling beneficiaries or with settlors as discretionary beneficiaries are accepted in trust law. This thesis works with the current structures to address their implications rather than addressing the structures themselves.

A second issue that is not addressed is whether or not asset protection trusts ought to be sanctioned by the law in order to allow business people to protect their accumulated wealth from their personal liabilities.[59] My opinion is that they should not, but this issue is not directly relevant to this thesis. In this thesis I argue that, if the current law is applied correctly, a remedy is available that limits the effectiveness of discretionary trusts for asset protection purposes. The question whether it would be a good thing for asset protection trusts to be made more effective is a policy issue. The argument that business people need asset protection is not one that ought to persuade a court against applying the law as it currently stands; it is essentially a policy argument, and it would require the court to balance a wide range of competing interests that would be better determined by Parliament. Until Parliament provides

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[57] See *Walker v Walker* [2007] NZCA 30, [2007] NZFLR 772; *Harrison v Harrison* [2009] NZCA 68, [2009] NZFLR 687 at [10]; *R v R* [2010] NZFLR 555 (FC) at [10], [61(d)]; *JR v LR (A Bankrupt)* [2011] NZFLR 797 (FC) at [59(xv)], [59(xviii)], [60].

[58] *JR v LR (A Bankrupt)* [2011] NZFLR 797 (FC) at [59(xviii)].

[59] Some have suggested that trusts which protect assets from personal liabilities are performing the same function as limited liability in company law. The Law Society has suggested that if trusts were made less effective for asset protection purposes it would be tantamount to subjecting the shareholders of a company to the claims of the company's creditors (see Submission by Andrew Gilchrist to the Law Commission regarding *Some Issues with the Use of Trusts in New Zealand: Review of the Law of Trusts Second Issues Paper* (NZLC IP20, 2010) (3 May 2011) at 9-10). This is incorrect. Limited liability in company law protects shareholders from the obligations incurred by the collective enterprise when operating the business. It does not protect the shareholder from being obliged to pay her shares to her creditor if she has personal liabilities to satisfy. A discretionary beneficiary who is obliged to give up his discretionary interest to his creditors due to that interest being included as property (as this thesis argues) is in the same position as a shareholder who is obliged to give up her shares to her creditors. The thesis argument is not tantamount to making shareholders liable for the obligations of a company.

direction on this issue the courts ought to apply the ordinary principles of statutory interpretation, trust law and property law. In short, this thesis does not engage with the question of whether asset protection is a legitimate purpose for a trust;[60] it focuses on whether it is effective.

V. Outline

The thesis takes the following steps in investigating the central question. Together these steps make up the argument that discretionary and controlling beneficiaries have "property" as that term is used in certain contexts. In some contexts I believe this argument succeeds, although in others it may not succeed.

The first chapter is descriptive. It sets out in detail the subject-matter with which this thesis is concerned. The primary subject matter is trusts that contain controlling beneficiaries. This chapter describes the structure and law applying to these trusts. In doing this the chapter also limits the scope of the thesis to the type of trust structure described.

The second chapter commences the argument that discretionary and controlling beneficiaries have property. This chapter is dedicated to what is meant by "property". The first step in working out whether beneficiaries have property is to determine what property means or includes. The starting point in determining the meaning of the concept of property is to look to the statutes that use that term. A key issue here is whether personal rights can be property or whether property is limited to legal or equitable interests 'in' or 'attached to' things. This is part of the broader issue, which is what criteria must be met for something to be characterised as property. This chapter also narrows the scope of the thesis as it limits the thesis to only a few selected statutes. This is done on practical grounds rather than conceptual grounds – only the statutes where the thesis argument is likely to be significant are selected.

The third chapter investigates the discretionary interest. Here I argue that the rights and interests held by a purely discretionary beneficiary can be property under some of the selected statutes. The central issues here are: the fact that the discretionary interest is only a possibility of becoming entitled to trust property in the future; the fact that this possibility is entirely subject to the discretion of the trustee; the fact that a number of cases describe this interest as a "mere expectancy"; a further case that suggests the interest is not economically significant; and the transferability of the interest.

The fourth chapter investigates the additional right to replace the trustee held by the controlling beneficiary. Here I argue that the right to replace trustees can be property in some circumstances. The central issues are: whether the fact this right is a "power" in technical

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[60] Judges in several cases have made obiter comments that asset protection is a legitimate or valid purpose for a trust: *N v T* [2006] NZFLR 885, 25 FRNZ 840 (FC) at [47]; *Worn v Buxton* HC Auckland M125-SDO1, 17 June 2002 at [35]; *Taranaki Regional Council v Mouland* DC New Plymouth CRI-2008-021-1238, 16 November 2010 at [20]. Practitioners have also expressed this view: Bill Armitage and others (New Zealand Law Society Seminar: Asset Protection, August-September 1996) at 1.

legal language prevents it from being property; whether the right is subject to fiduciary duties; and whether a right to replace a fiduciary officer (the trustee) can be property.

The fifth chapter concerns valuation. If the discretionary interest and the right to replace trustees are property, the next question is how they can be valued. The issue here is whether the principles of valuation can apply to an interest that is as uncertain as a discretionary interest.

This chapter describes the position of a controlling beneficiary in detail. This is to provide clarity about the exact type of trust the thesis is concerned with and to set out the assumptions that limit its scope. The description includes the nature of the trust relationship, the positions of the beneficiaries vis-à-vis the trustee and the unique position of the controlling beneficiary.

I. The Nature of Trusts

This thesis is concerned with trusts. A trust is a particular type of legal relationship that exists between trustees and beneficiaries. The basic nature of a trust relationship is an owner of property who is legally obliged to utilise that property, and ultimately dispose of that property,[61] for the benefit of people[62] other than herself.[63] The owner is the trustee and the people for whose benefit the property is to be used are the beneficiaries. The trust obligation may be imposed expressly when property is transferred to the trustee by the settlor or may be imposed by the settlor on herself by a unilateral declaration rendering her a trustee. The trust obligation may also be imposed in transactions where it is implied or presumed that the person receiving the property was not intended to use it for her own benefit.[64]

At present there is a debate about whether to understand the trust as a proprietary relationship or an obligational relationship. The proprietary conception is that a trust exists where the title to property is split into a legal estate and a beneficial estate.[65] This conception was significant in establishing the principle that events that might affect the legal estate did not affect the beneficial estate; the beneficial estate was understood as binding the trust

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[61] An exception to this is a charitable trust which may continue indefinitely. The corpus of the trust may never need to be disposed of (*Perpetual Trust Ltd v Roman Catholic Bishop of Christchurch* [2006] 1 NZLR 282 (HC)).

[62] An exception to this are trusts where the trustee is obliged to utilise the property for a particular purpose rather than for a particular person. In New Zealand trust law a trust can only exist for purposes if they are charitable, or within a very narrow range of exceptions to the rule that there must be a legal person to enforce the trust (John McGhee (ed) *Snell's Equity* (32nd ed, Sweet & Maxwell, London, 2010) at [21-015]). Trusts established for a purpose will be ignored from now on.

[63] *Knight v Knight* (1840) 3 Beav 148 at 172-173, 49 ER 58 (Rolls); *Paul v Constance* [1977] 1 WLR 527 (CA) at 531G-H; *Spellson v George* (1987) 11 NSWLR 300 (SC) at 315; PD Finn *Fiduciary Obligations* (The Law Book Company Limited, Sydney, 1977) at [6], [15], [19]; Daniel Greenberg (ed) *Jowitt's Dictionary of English Law* (3rd ed, Sweet & Maxwell, London, 2010) "trust *it*"; Jessica Palmer "Theories of the Trust and What They Might Mean for Beneficiary Rights to Information" [2010] NZ L Rev 541 at 552-553; John McGhee (ed) *Snell's Equity* (32nd ed, Sweet & Maxwell, London, 2010) at [21-001]; Terence Tan Zhong Wei "The Irreducible Core Content of Modern Trust Law" (2009) 15 Trusts & Trustees 477 at 480-481; Matthew Conaglen *Fiduciary Loyalty: Protecting the Due Performance of Non-Fiduciary Duties* (Hart Publishing, Oxford, 2010) at 260.

[64] *Westdeutsche Landesbank Girozentrale v Islington London Borough Council* [1996] 1 AC 669 (HL) at705-709; CEF Ricketts "The Classification of Trusts" (1999) 18 NZULR 305.

[65] *Ayerst v C & K (Construction) Ltd* [1976] AC 167 (HL) at 180.

property itself and more than an obligation binding the trustee's interest in the trust.[66] That is, the trustee is obliged to utilise the trust property for the benefit of the beneficiaries because the beneficiaries are understood as owners of the property.

In contrast, under the obligational conception of the trust a beneficial estate is not required. Instead the obligation to utilise the trust property on behalf of others and not for oneself is sufficient to establish the trust. Trusts under this conception can include charitable trusts, administrators of deceased estates, liquidators of companies and trustees in bankruptcy; in none of these relationships is there a beneficial estate but in all of them there is a figure who is obliged utilise property it owns for the benefit of others or other purposes and to the exclusion of its own benefit.[67] This conception of the trust puts forward the conscience of the trustee as the primary reason for imposing the trust obligation, rather than the beneficiary's property rights.[68]

The debate about the nature of the trust has been continuing for centuries.[69] In my opinion the obligation conception of trusts is more accurate, at least in relation to discretionary trusts because with a discretionary trust there is no identifiable owner of the trust property while it is subject to the trustee discretion.[70]

The classic three certainties,[71] which are necessary for a trust to exist, can be explained by either conception of the trust. They are certainty of subject-matter, certainty of object and certainty of intention. The subject-matter, or property, to be held on trust needs to be certain because the trust obligation can only attach to an owner of property. The objects, or beneficiaries, of the trust need to be certain because the trust obligation requires the owner to be obliged to someone other than herself, whether that person is the beneficial owner or not. Certainty about intention can either correlate to a requirement that the settlor[72] must intend to

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[66] *Burgess v Wheate* (1759) 1 Black W 123 at 153-166, 96 ER 67 (KB); William Holdsworth *A History of English Law* (2nd ed (reprint), Methuen & Co Ltd and Sweet & Maxwell Ltd, London, 1966) vol 7 at 146.

[67] Terence Tan Zhong Wei "The Irreducible Core Content of Modern Trust Law" (2009) 15 Trusts & Trustees 477 at 479-481; RP Meagher, JD Heydon and MJ Leeming *Meagher, Gummow and Lehane's Equity: Doctrines and Remedies* (4th ed, Butterworths LexisNexis, Chatswood (NSW), 2002) at [4-005]-[4-065].

[68] Terence Tan Zhong Wei "The Irreducible Core Content of Modern Trust Law" (2009) 15 Trusts & Trustees 477 at 479. This conception of the trust is not recent. The first cases which decided that the trustee's creditors, when executing trust property, were bound by the same trusts that bound the trustee, were not decided on the principle that the beneficiary owned the property but that these creditors derived their title from the trustee so were bound in conscience by whatever trusts had bound the conscience of the trustee (*Burgh v Francis* (1670) 1 Eq Ca Abr 320, 21 ER 1074 (Rolls); *Medley v Martin* (1673) Finch 62, 23 ER 33 (Ch)). See further discussion below at n 154.

[69] For an overview of the debate see DWM Waters "The Nature of the Trust Beneficiary's Interest" (1967) 45 Can Bar Rev 119.

[70] See RP Meagher, JD Heydon and MJ Leeming *Meagher, Gummow and Lehane's Equity: Doctrines and Remedies* (4th ed, Butterworths LexisNexis, Chatswood (NSW), 2002) at [4-070]-[4-105].

[71] *Knight v Knight* (1840) 3 Beav 148 at 172-173, 49 ER 58 (Rolls).

[72] The settlor's intention is the only intention relevant in establishing a trust obligation. The trustee's intention is only relevant to the extent that that particular trustee has agreed to be subject to the trust obligation. If the trustee has not agreed then there is still a trust obligation and the courts will act to appoint a replacement so that the

give the beneficial interest in the property to the beneficiaries or intend to legally bind the trustee not to use the property for her own benefit.[73]

It is the trust obligation that creates the relationship between the trustees and beneficiaries. Thus, the core duty for the trustee is to utilise property for the benefit of others and to the exclusion of oneself. It is sometimes suggested that the core duty is solely to "act honestly and in good faith".[74] Honesty and good faith are a necessary part of the core duty but alone they are not sufficient to create a trust relationship. An owner of property could be required to act honestly and in good faith, but without an obligation to utilise the property for the benefit of another he is not a trustee. He must also be obliged to "perform the trusts".[75] The importance of honesty and good faith is in providing a minimum standard to ensure the core duty is enforceable.[76] The minimum standard may include more than just honesty and good faith. A duty to account to the beneficiaries and give information,[77] a duty not to act with gross negligence,[78] and to act with objective honesty[79] have all been suggested as

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obligation can attach to someone. Even Langbein agreed that in regard to the duty to dispose of property to others only the settlor's intention was relevant (John H Langbein "The Contractarian Basis of the Law of Trusts" (1995) 105 Yale J 625 at 652). This does not contradict the finding in *Official Assignee v Wilson* [2007] NZCA 122, [2008] 3 NZLR 45 that under the doctrine of sham both the trustee's and settlor's intentions are relevant. As Palmer has said the debate about the need for mutual intention in the doctrine of sham is not necessarily relevant to the intention to create trust obligations (Jessica Palmer "A Modern Law of Trusts: Theories of the Trust and What They Might Mean for Beneficiary Rights to Information" [2010] NZ L Rev 541 at 544). See also Nicola Glover and Paul Todd "The Myth of Common Intention" (1996) 16 LS 325. See further discussion below n 503

[73] See *Malim v Keighley* (1794) 2 Ves Jun 333, 30 ER 659 (Rolls); *Re Adams and the Kensington Vestry* (1884) 27 Ch D 394 (CA); *Re Hamilton* [1895] 2 Ch 370 (CA); *Paul v Constance* [1977] 1 WLR 527 (CA) at 531G-H.

The intention to dispose of the beneficial interest is what distinguishes the transfer of property on trust from a transfer subject to an equitable charge. In both cases the property becomes subject to an obligation. With the trust the intention is that the property is to be used for the benefit of the beneficiaries. With an equitable charge the intention is that the recipient is to be able to use it for his own benefit. This distinction was made in *Re Bond Worth Ltd* [1980] 1 Ch 228 (Ch) where a supplier attempted to impose a trust obligation in relation to goods supplied to a manufacturer. However, the purpose of supplying the goods was so that the manufacturer could utilise them for its own benefit by turning them into manufactured goods. Therefore, the manufacturer could not be under a duty to utilise the supplied property for the benefit of the supplier or anyone else. The relationship was not a trust but an equitable charge.

[74] Law Commission *The Duties, Office and Powers of a Trustee: Review of the Law of Trusts Fourth Issues Paper* (NZLC IP26, 2011) at [1.17].

[75] *Armitage v Nurse* [1998] Ch 241 (CA) at 253H-254A.

[76] Otherwise the core trust duty will become unenforceable. *Armitage v Nurse* [1998] Ch 241 (CA) at 253H; David Hayton "The Irreducible Core Content of Trusteeship" in AJ Oakley (ed) *Trends in Contemporary Trust Law* (Clarendon Press, Oxford, 1996) 47 at 58-60.

[77] *Spellson v George* (1987) 11 NSWLR 300 (SC) at 315F-316C. Contrast David Hayton "The Irreducible Core Content of Trusteeship" in AJ Oakley (ed) *Trends in Contemporary Trust Law* (Clarendon Press, Oxford, 1996) 47 at 49-50.

[78] *Spread Trustee Company Limited v Sarah Ann Hutcheson* [2011] UKPC 13 [per Lady Hale and Lord Kerr in dissent].

[79] Anthony Grant "Clauses that Exonerate Trustees from Fault may be Worthless" *NZ Lawyer Magazine* (New Zealand, 10 February 2012).

necessary to enforce the trust obligation. This issue is currently under review by the Law Commission.[80]

In addition to the minimum standard of honesty, good faith and accountability, there are further duties or standards including skill, care, prudence and diligence. These duties are imposed on the trustee to protect and enhance the performance of the core duty.[81] They have been understood as deriving from the voluntary agreement between the trustee and settlor.[82] The consequence is that these additional duties founded on consent are not essential to the trust relationship, and can be excluded by negotiation between the trustee and the settlor, although the default position is inclusion.[83]

The core right of a beneficiary correlates to the core duty of the trustee: the right to enforce the due administration of the trusts correlates to the duty to perform the trust obligation.[84] This core right is enhanced by rights to enforce the minimum and additional standards with which the trustee must comply, provided the settlor has not limited the additional standards. The right to due administration also gives rise to particular rights arising out of the terms of the trust. For example, an income beneficiary's right to payment of income arises from the right to enforce a term in the trust concerning income.

A final right held by beneficiaries is the collective right to terminate the trust.[85] This feature of the trusts is usually understood as founded on the proprietary conception of the trust where the beneficiaries collectively own the trust property.[86] However, if the trustee has a right to some of the trust property, for example a right to reimbursement of expenses, the beneficiaries' collective right is subordinate to it, which suggests the proprietary conception of the trust is not absolute.[87]

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[80] Law Commission *The Duties, Office and Powers of a Trustee: Review of the Law of Trusts Fourth Issues Paper* (NZLC IP26, 2011) at [1.16]-[1.21].

[81] See Jessica Palmer "Theories of the Trust and What They Might Mean for Beneficiary Rights to Information" [2010] NZ L Rev 541 at 552-554; Matthew Conaglen *Fiduciary Loyalty: Protecting the Due Performance of Non-Fiduciary Duties* (Hart Publishing, Oxford, 2010) [Conaglen argues that the purely fiduciary duty of loyalty is a prophylactic duty that protects the performance of the trustee's basic obligation to perform the trust]; Law Commission *The Duties, Office and Powers of a Trustee: Review of the Law of Trusts Fourth Issues Paper* (NZLC IP26, 2011) at [1.9]-[1.13].

[82] Jessica Palmer "Theories of the Trust and What They Might Mean for Beneficiary Rights to Information" [2010] NZ L Rev 541; Law Commission *The Duties, Office and Powers of a Trustee: Review of the Law of Trusts Fourth Issues Paper* (NZLC IP26, 2011) at [1.9]-[1.13].

[83] Law Commission *The Duties, Office and Powers of a Trustee: Review of the Law of Trusts Fourth Issues Paper* (NZLC IP26, 2011) at [3.9].

[84] *Target Holdings v Redferns* [1995] UKHL 10, [1996] 1 AC 421 (HL) at 434A-B; Matthew Conaglen *Fiduciary Loyalty: Protecting the Due Performance of Non-Fiduciary Duties* (Hart Publishing, Oxford, 2010) at 32-34.

[85] *Saunders v Vautier* (1841) 4 Beav 115, 49 ER 282 (Rolls); affirmed *Saunders v Vautier* (1841) Cr & Ph 240, 41 ER 482 (Ch).

[86] *Younghusband v Gisborne* (1844) 1 Coll 400, 63 ER 473 (Ch); *Re Smith* [1928] Ch 915 (Ch).

[87] *CPT Custodian Pty Ltd v Commissioner of State Revenue* [2005] HCA 53, 224 CLR 98.

As the right to reimbursement indicates, the trust obligation does not require a complete prohibition on the trustee benefiting herself from the property, provided the benefit is authorised by the settlor.[88] This allows a person to be both a trustee and beneficiary. It also allows a trustee-beneficiary to make decisions in his own interest when exercising some discretions.[89]

However, it is currently controversial how far a trustee may be authorised to benefit himself and still be subject to a trust obligation. It is possible that a person who is given property, apparently to be held on trust, but who is authorised to benefit himself to the entire exclusion of anyone else's interests is not under a trust obligation.[90] For example, a person who is put in the position of sole trustee but who is authorised to distribute the entire trust fund to himself at his sole discretion. Because this person is authorised to exercise his power, given to him as a 'trustee' under the deed, in favour of himself he cannot be under an absolute duty to dispose of the property to others. At most he has a duty to *consider* benefiting others in preference to himself.

Ford and Lee in Australia and Fogarty J in *B v X* suggest that a duty to consider benefiting others before oneself, but without a duty to utilise the property on behalf of others and not oneself, is not sufficient to create a trust obligation.[91] However, the Court of Appeal has given leave to appeal Fogarty J's decision and other commentators suggest a trustee with a discretionary power in his own favour does not destroy the trust obligation.[92] Trusts with a sole trustee who is also a discretionary beneficiary have come before the courts in other cases but as far as I am aware no comment has been given regarding the validity of these structures as trusts and the issue was not argued.[93] This issue is important but cannot be resolved within the scope of this thesis. This thesis is focusing on the position of the beneficiary not the position of the trustee. This thesis is limited to commenting on trusts where the assumption of validity holds true.

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[88] See Matthew Conaglen *Fiduciary Loyalty: Protecting the Due Performance of Non-Fiduciary Duties* (Hart Publishing, Oxford, 2010) at 204-205: "The principal may bring an end to the fiduciary relationship completely, thereby releasing the former fiduciary from the strictures of the fiduciary conflict principle, or the principal may alter the fiduciary's non-fiduciary duties in respect of a particular transaction so that, for that specific transaction, there is no longer any conflict between those non-fiduciary duties and the fiduciary's personal interest."

[89] For example, in *Edge v Pensions Ombudsman* [1998] Ch 512 (Ch) at 539-541 the Court held that it was acceptable for particular beneficiaries of an employees' pension fund who were elected to the board of trustees to exercise a power in a way which preferred existing employees (the group of beneficiaries to which the trustees belonged) to former employees. This is authority that in some circumstances a trustee can also be a beneficiary and be able to exercise discretionary powers in his own favour. However, this case does not go so far as holding that a trustee can exercise a discretionary power in his own favour to the complete exclusion of all other beneficiaries. This point is yet to be firmly decided.

[90] HAJ Ford and William A Lee *Principles of the Law of Trusts* (2nd ed, Law Book Company Limited, Sydney, 1990) at [503]; *B v X* [2011] 2 NZLR 405 (HC) at [83], [86], [96] and [98].

[91] *Darby v Bolton* [2011] NZCA 474, [2011] NZFLR 1065.

[92] See Geraint Thomas *Thomas on Powers* (Sweet & Maxwell, London, 1998) at [9-33].

[93] For example, the case *Chief Commissioner of Stamp Duties v Buckle* [1998] HCA 4, 192 CLR 226 involved a trust where the father was both sole trustee and a discretionary beneficiary. However, it was in neither party's interests to argue that there was no trust and the issue did not arise to be decided.

This basic understanding of the trust allows the position of the controlling beneficiary to be placed in context. This beneficiary is one among many types; they are united in their core right of due administration against the trustees; and they are distinguished by their particular rights and powers under the terms of the trust. The next step is to describe the discretionary beneficiary.

II. Discretionary Interests

The controlling beneficiary is a type of discretionary beneficiary. It is often said that "discretionary" in trust law is a descriptive not a normative term.[94] However, it is used with reliable consistency to describe a trust where the trustee is given a discretion regarding the beneficial disposition of the trust property, rather than an administrative discretion. Discretionary beneficiaries are identified by a term in the trust that gives the trustee a power to use trust income and/or capital to benefit any one or more of a class of beneficiaries as the trustee decides.[95] The technical term for this discretion is a "power of appointment". A trustee usually holds a "special" power of appointment, which means that only certain people or classes of people are authorised to be distributed property. The discretion is usually qualified by words like "absolute" or "uncontrolled", indicating that the merits of the trustee's decision is not intended to be subject to review.[96]

There is a distinction between a discretionary power that must be exercised by the trustee at the end of the trust's life (an "exhaustive" power[97]) and a power that may be exercised but if it is not then another class of beneficiaries will become entitled to receive the undistributed property or the settlor will become entitled under a resulting trust (a "non-exhaustive" power[98]).[99] The distinction is not material for this thesis.[100] The usual practice with trust drafting in New Zealand is to have a non-exhaustive power exercisable by the trustee for a designated perpetuity period and then to have a residuary gift of any property that

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[94] *Chief Commissioner of Stamp Duties v Buckle* [1998] HCA 4, 192 CLR 226 at [8].

[95] An example of such a clause is found in *McNulty v McNulty* HC Dunedin CIV-2010-412-810, 30 September 2011 at [7]:

> INCOME AND CAPITAL PAYMENTS The Trustees may at their discretion until the Vesting Day pay or apply the whole or any part of the capital and/or income for or towards the personal support, maintenance, comfort, education or advancement in life or other benefit of any of the Beneficiaries then living or in existence during the trust period in any manner, at any times, in any proportions and subject to any terms and conditions which the Trustees in their absolute discretion may decide. Any income not paid to or applied for any Beneficiary during, or within six months after, any income year shall be accumulated and added to the trust fund.

[96] Geraint Thomas and Alastair Hudson *The Law of Trusts* (2nd ed, Oxford University Press, Oxford, 2010) at [20.07]-[20.13]; Geraint Thomas *Thomas on Powers* (Sweet & Maxwell, London, 1998) at [6-211].

[97] This is also commonly known as a "trust power" (*Re Gulbenkian's Settlements* [1970] AC 508 (HL) at 525) or a power in the nature of a trust (see *Gomez v Gomez-Monche Vives* [2008] EWCA Civ 1065, [2009] Ch 245 at [100]).

[98] Also commonly known as a "mere" power.

[99] *Re Gulbenkian's Settlements* [1970] AC 508 (HL) at 525B-C; *Re Baden's Deed Trusts* [1971] AC 424 (HL) at 444G-H [per Lord Guest in dissent].

[100] See *Schmidt v Rosewood Trust Ltd* [2003] UKPC 26, [2003] 2 AC 70 at [66].

has not been appointed to a different class of beneficiaries; these are the final or "default" beneficiaries.

Discretionary powers are a means of carrying out the trustee's core duty to utilise trust property for the benefit of the beneficiaries. The settlor intends the trustee to dispose of the trust property to the beneficiaries but leaves the decision about which beneficiaries and in which proportions to the trustee to allow flexibility in the future. Out of respect for the settlor's decision the courts have declined to interfere with what it perceives to be an "unwise or unjustified exercise of the discretion in the circumstances."[101] However, the courts will review the process by which the trustee exercises discretions. This means that a decision of dubious merit can only be corrected if there was a fault in the process by which the trustee came to that decision; however, the range of grounds on which the process can be challenged means that the merits will often be able to be reviewed.

Two New Zealand High Court cases have further blurred the distinction by reviewing trustee decisions on the basis that they were objectively unreasonable[102] but a later case has reversed this trend.[103] Currently, unreasonableness, even "Wednesbury" unreasonableness in the administrative law sense, is an unsure ground to review a trustee's decision.[104]

The trustee's duty to exercise discretions following proper process translates into a number of procedural duties. The trustee must periodically consider exercising the power[105] and she cannot ignore requests that she exercise it.[106] The trustee's exercise of discretion must be real and genuine.[107] This means the exercise must be for a proper purpose[108] and in good faith,[109] and it must not: be under someone else's direction,[110] be capricious,[111] ignore relevant considerations or take into account irrelevant considerations.[112] Relevant considerations

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[101] *Karger v Paul* [1984] VR 161 (SC) at 164; *Edge v Pensions Ombudsman* [1998] Ch 512 (Ch) at 535E-G.

[102] *Blair v Vallely* HC Whanganui CP8/98, 23 April 1999 at 28; *Craddock v Crowhen* (1995) 1 NZSC 40,331 (HC) at 40,337.

[103] *Gailey v Gordon* [2003] 2 NZLR 192 (HC) at [88]-[89].

[104] See also *Karger v Paul* [1984] VR 161 (SC) at 164, 166; *Edge v Pensions Ombudsman* [1998] Ch 512 (Ch) at 536C-D.

[105] *Re Gestetner Settlement* [1953] Ch 672 (Ch) at 688; *Re Gulbenkian's Settlements* [1970] AC 508 (HL) at 518A-E; *Re Baden's Deed Trusts* [1971] AC 424 (HL) at 449C-D; *Re Hay's Settlement Trusts* [1982] 1 WLR 202 (Ch) at 209B, 210D-E; *Karger v Paul* [1984] VR 161 (SC) at 164.

[106] *Re Manisty's Settlement* [1974] Ch 17 (Ch) at 26F, 27H-27A.

[107] *Karger v Paul* [1984] VR 161 (SC) at 164-165. This does not prevent the trustee from forming a view prior to exercising the power.

[108] *Karger v Paul* [1984] VR 161 (SC) at 164, 166; *Edge v Pensions Ombudsman* [1998] Ch 512 (Ch) at 535F.

[109] *Karger v Paul* [1984] VR 161 (SC) at 164.

[110] *Re Steed's Will Trusts* [1960] Ch 407 (CA) at 418.

[111] *Re Manisty's Settlement* [1974] Ch 17 (Ch) at 26C-D; *Re Hay's Settlement Trusts* [1982] 1 WLR 202 (Ch) at 209D.

[112] *Re Manisty's Settlement* [1974] Ch 17 (Ch) at 26E-F; *Edge v Pensions Ombudsman* [2000] Ch 602 (CA) at 625G-627E.

include the range of beneficiaries,[113] the settlor's intention[114] and individual claims on the bounty of the settlor.[115] However, the requirement to only consider relevant considerations is diluted by the fact that trustees are not obliged to give reasons for their decisions.[116]

Thus the discretionary interest has two central features. The first is the core right to enforce the due administration of the trust, like any other beneficiary.[117] This right gives rise to further rights to have the trustee consider exercising the discretionary power in his favour, to have the trustee consider any requests and to hold the trustee accountable.[118]

The second core feature is that the discretionary beneficiary may "take and enjoy whatever part of the income [or capital] the trustees choose to give to him."[119] In my opinion, this means that the discretionary beneficiary has an entitlement to any property that the trustee appoints, allocates or appropriates to him. This is not a present entitlement; it is only a possibility of receiving an entitlement in the future. The realisation of that possibility is dependent on the trustee's decision.

III. The Controlling Beneficiary

The controlling beneficiary, as defined in this thesis, differs from an ordinary discretionary beneficiary in that she has the right to remove the trustee and replace him with another. This right is a "power" under Hohfeld's categories of legal interest but is within the broad meaning of "right".[120]

This right is granted in the trust deed and can be found vested in one person, jointly vested in two people or even split into two rights each relating to a different trustee. The latter form is common where a couple sets up a trust and wish to each appoint their own trustee to ensure balance between their interests.[121] The commonest controlling beneficiary is the settlor who retains both a discretionary interest and the right to replace. However, the settlor may put another person in the position of controlling beneficiary such as a child.

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[113] *Re Hay's Settlement Trusts* [1982] 1 WLR 202 (Ch) at 210A-B.

[114] *Re Manisty's Settlement* [1974] Ch 17 (Ch) at 26E-F.

[115] *Re Manisty's Settlement* [1974] Ch 17 (Ch) at 26G; *Re Hay's Settlement Trusts* [1982] 1 WLR 202 (Ch) at 210D-E.

[116] *Karger v Paul* [1984] VR 161 (SC) at 164.

[117] *Schmidt v Rosewood Trust Ltd* [2003] UKPC 26, [2003] 2 AC 70 at [60]; *Spellson v George* (1987) 11 NSWLR 300 (SC) at 316D-G.

[118] *Spellson v George* (1987) 11 NSWLR 300 (SC) at 316D-G.

[119] *Re Gartside's Will Trust* [1968] AC 553 (HL) at 606E.

[120] See Chapter Four of this thesis.

[121] Bill Armitage and others (paper presented to New Zealand Law Society Seminar: Asset Protection, August-September 1996) at 12; Pravir Tesiram "Drafting Trust Deeds" (paper presented to New Zealand Law Society Conference: Trusts, June 2007) 37 at 40.

In my opinion, discretionary beneficiaries with control create different and more serious issues than settlors who retain control but are prohibited from benefiting.[122] These settlors also create an internal tension in trust law between the control of the settlor and the duties of the beneficiary. However, controlling beneficiaries are more problematic because they can use their powers for their own benefit. Then there is a grey area where settlors might retain control without nominating themselves discretionary beneficiaries but do not prohibit themselves from benefiting, which leaves open the possibility of using other means to legitimately use their control to benefit themselves.

There are other means by which a beneficiary may have control over the institution of trustee. These include retaining a trusteeship, retaining shares in a corporate trustee, being the director of a corporate trustee, retaining powers to alter the class of discretionary beneficiaries and retaining powers to vary the trust. This thesis cannot adequately examine all of these means of control. As the right to replace trustees held by a discretionary beneficiary is the most distinctive feature of the asset protection trusts developed in the last two decades the scope of this thesis will be limited to this means of control.[123]

IV. Assumptions

A number of initial assumptions are set out here concerning the type of trust relationship that is of concern to this thesis and the limit of its scope.

First, it is assumed that there is a valid trust with an independent[124] trustee who is obliged to utilise the trust property on behalf of the beneficiaries and to the exclusion of her own interest. This assumption avoids two issues. It avoids detailed examination about deeds that purport to create trusts but that authorise the trustees to take the entire trust property for themselves, which possibly negates the core trust obligation.[125] It also avoids any concerns about sham trusts.[126] This means, for the purpose of this thesis, the trust deed can be taken as it is written.[127]

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[122] In practice control is usually retained by a settlor, which is why the issues with rights to replace trustess and other rights in relation to the trust are often referred to as issues with settlor control. See Law Commission *Some Issues with the Use of Trusts in New Zealand: Review of the Law of Trusts Second Issues Paper* (NZLC IP20, 2010) at 60-63; Donovan Waters "Trusts: Settlor Reserved Powers" (2006) 25 ETPJ 234; Donovan Waters "Settlor control – What Kind of Problem is it?" (2009) 15 Trusts & Trustees 12.

[123] See Barry Stafford "The New Zealand Discretionary Trust 40 Years On: Back to First Principles" (paper presented to Auckland District Law Society Seminar: Trusts: Key Selected Issues (Part I), Auckland, March 2004) at 10; Bill Patterson "Sham Trusts, Modern Trust Structures and Current Gifting Problems" (paper presented to New Zealand Law Society Trusts Conference, August 1999) 247 at 252.

[124] "Independent" here means a trustee who is not authorised to distribute the entire trust property to himself.

[125] See *B v X* [2011] 2 NZLR 405 (HC) at [83], [86], [96] and [98].

[126] See *Official Assignee v Wilson* [2007] NZCA 122, [2008] 3 NZLR 45.

[127] An example of a relatively typical New Zealand trust deed can be found in Bill Patterson's "Trust Structuring" (paper presented to the ADLS Cradle to Grave Conference, Auckland, 21 March 2011).

Second, it is assumed that the clause granting the controlling beneficiary a discretionary interest grants the trustee an absolute discretion and cannot be interpreted to reduce the trustee's power. It is possible that a discretionary power in a trust deed could be interpreted, in light of its purpose and context,[128] to grant only a limited discretion.[129] However, this possibility is entirely dependent on the terms and circumstances of the individual trust. This assumption confirms that the controlling beneficiary only has a possibility of becoming entitled to property in the future.

Third, it is assumed that the controlling beneficiary has a right to replace the trustees but is not a trustee and has no other means of control. No assumption is made about whether the controlling beneficiary settled the trust or not. This detail will be mentioned where it makes a difference.

Fourth, any social influence or factual control the controlling beneficiary might have is assumed to be irrelevant. It is assumed that only the controlling beneficiary's legally cognizable rights and interests are relevant to whether she has property.[130]

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[128] Inter vivos trust deeds are interpreted like any other legal document. The trust deed has the meaning which it would convey to a reasonable person having all relevant background knowledge (*Sunny Metal and Engineering Pte Ltd v Ng Khim Ming Eric* [2007] SGCA 36, 113 ConLR 112 at [27]; *Manukau City Council v Lawson* [2001] 1 NZLR 599 (HC) at [24]; *Gailey v Gordon* [2003] 2 NZLR 192 (HC) at [51]-[53]). Trust deeds are communications by settlors and the purpose of communications is to convey meaning. Therefore, the meaning which a trust deed would convey to the reasonable person is the meaning which the reasonable person would take the settlor to have intended. The initial assumption of the reasonable person is that the settlor apparently intends to communicate the ordinary linguistic meaning of the words he has used. This assumption can be displaced if the context and purpose of the trust deed makes it apparent that the settlor's intention departed from the linguistic meaning. The same process applies where ambiguity or uncertainty in the linguistic meaning means the reasonable person must look to the context and purpose to ascertain what meaning the settlor apparently intended to convey (Adam Kramer "Common Sense Principles of Contract Interpretation (and how we've been using them all along)" (2003) 23 Oxford Journal of Legal Studies 173; *Re Gulbenkian's Settlements* [1970] AC 508 (HL) at 522B-D. See also *Vector Gas Ltd v Bay of Plenty Energy Ltd* [2010] NZSC 5, [2010] 2 NZLR 444 at [27] per Tipping J, contrast McGrath J at [76]). However, because the recipient of a communication never knows the actual subjective intentions of the communicator those actual intentions cannot inform the meaning that was *apparently* intended to be conveyed and are not usually taken into account (see *Investors Compensation Scheme Ltd v West Bromwich Building Society* [1997] UKHL 28, [1998] 1 WLR 896 at 912-913). An exception is likely to be made for statements of subjective intention that are made expressly available to all intended recipients of the communication; for example, a settlor's letter of wishes will no doubt be taken into account in the interpretation of a trust deed.

Testamentary trusts are interpreted according to s 32 of the Wills Act 2007. This section allows the court to take into account external evidence when the terms of the trust are meaningless, or are ambiguous or uncertain in light of the surrounding circumstances. The subjective intentions of the testator can be taken into account in resolving a meaningless, ambiguous or uncertain term but are not included as part of the surrounding circumstances that might make the term appear ambiguous or uncertain. This is essentially the same method of interpretation that applies to other legal documents. See also Julian Rivers and Roger Kerridge "The Construction of Wills" (2000) 116 LQR 287.

[129] Geraint Thomas and Alastair Hudson *The Law of Trusts* (2nd ed, Oxford University Press, Oxford, 2010) at [20.07]-[20.13]; Geraint Thomas *Thomas on Powers* (Sweet & Maxwell, London, 1998) at [6-211].

[130] See *Vestey's (Lord) Executors v Inland Revenue Commissioners* [1949] 1 All ER 1108 at 1119H (HL); *Official Assignee v Wilson* [2007] NZCA 122, [2008] 3 NZLR 45 at [70]; Jessica Palmer "Dealing with the Emerging Popularity of Sham Trusts" [2007] NZ L Rev 81 at 89-90.

Fifth, it is assumed there is only one controlling beneficiary with a single right to replace. The possibility of two or more discretionary beneficiaries with a joint power raises specific issues related to whether a joint power can be property.[131] These issues cannot be considered in this thesis.

Sixth, it is assumed that the existence of the right to replace the trustee will not alter or affect the duties that the court has imposed on trustees exercising their discretions. Control of the trust property remains with the trustee.[132] It might be argued that the existence of the right constitutionally alters the office of trustee in a manner that requires the imposition of different duties, or creates a direct relationship between the controlling beneficiary and trustee.[133] However, any such argument is speculative and is ignored for present purposes.

The cumulative effect of these assumptions is that the thesis is limited to a particular type of trust that is common in New Zealand trust drafting. The distinctive feature of the trust is that it grants one discretionary beneficiary a right to replace the trustees. The thesis makes an argument that applies to all discretionary beneficiaries but its focus is on this particular type of trust. The issue is whether this controlling beneficiary has property due to his position in the trust relationship.

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[131] The issue is that a number of cases have held that general powers of appointment which would be property if they were held by one person have been excluded from being property because they are held jointly by more than one. However, these cases do not consider possibility of severing the joint power. Severing a joint interest is used for other joint interests to be turned into individual interests which can be property. See *Charlton v Attorney-General* (1879) 4 App Cas 427 (HL) at 446; *Re Earl of Coventry's Indentures* [1974] Ch 77 (Ch); *Re Churston Settled Estates* [1954] 1 Ch 334 (Ch); Roger J Smith *Plural Ownership* (Oxford University Press, Oxford, 2005) at 209-211.

[132] *Financial Markets Authority v Hotchin* [2011] 3 NZLR 469 at [131].

[133] This type of argument was used by Flannigan in his debate with Cullity about trading trusts (see Robert D Flannigan "Beneficiary Liability in Business Trusts" (1984) 6 Est & Tr Q 278; Maurice C Cullity "Liability of Beneficiaries: A Rejoinder" (1985) 7 Estates & Trusts Quarterly 35; RDM Flannigan "The Control Test of Principal Status Applied to Business Trusts" (1986) 8 Est & Tr Q 37; Maurice C Cullity "Liability of Beneficiaries: A Further Rejoinder to Mr Flannigan" (1986) 8 Est & Tr Q 130).

CHAPTER TWO: THE CONCEPT OF PROPERTY IN SELECTED STATUTES

For asset protection trusts to live up to their name, controlling and discretionary beneficiaries must be able to claim they have no property – this is the null hypothesis. This thesis's argument is that the controlling beneficiary does in fact have property. The resolution of these conflicting claims depends on whether the controlling beneficiary's rights and interests fit within operative terms found in statutes. The purpose of this chapter is to examine the meaning of terms, such as "property" and "estate," that are found in statutes, which will lead to an investigation of the general or ordinary concept of property.

There are too many statutes that determine outcomes based on the ownership of property for this thesis to investigate them all. Certain statutes are selected for investigation on the practical ground that the thesis argument is likely to be most significant for them.

This chapter poses three broad questions about the idea of property as found in the law. The first and overriding question is what features a right or interest must have to be included within the meaning of property in a particular context. The intention of this question is to establish a general understanding of which rights and interests are property and which are not. This understanding will then be used in the following chapters to analyse in more detail whether the controlling beneficiary's interests can be property.

The second and third questions are sub-issues within the first question. The second question is whether property is limited to entitlements to things. If property is limited to rights that give an entitlement 'in' or 'attached' to a 'thing' then the controlling beneficiary can argue she does not have property because she has no entitlement or right 'in' or 'attached' to the trust property. If property is not so limited then it may be argued that the controlling beneficiary has property despite having no rights that directly relate to the trust property.

The third question is whether property can include a possibility of receiving something in the future. If property cannot include future possibilities then the controlling beneficiary's expectation of receiving economic benefits from the trust is unlikely to be property.

These questions about the idea of property will be investigated in a series of steps. The first step is to look at the terms and definitions used by Parliament.

The second step is to see whether the terms used by Parliament have any ordinary meaning or meanings that Parliament could be assumed to have intended. These two steps seek the linguistic or literal limitations on what abstract concepts words like "property" can symbolise. A central issue here is whether property is a unified concept in law or has plural meanings that vary according to context.

The final step is to look at the context and purpose of the relevant statutes and come to a conclusion on what Parliament is likely to have intended these terms to mean. It is argued that in the context of these statutes there are three threshold criteria that must be met before an interest can be property. It will be argued that interests must be legally significant, economically significant and capable of being dealt with within the statutory schemes.

I. Selecting Statutes

Only certain statutes can be investigated within the scope of this thesis. The Insolvency Act 2006, High Court Rules, Property (Relationships) Act 1976, Family Protection Act 1955 and Law Reform (Testamentary) Promises Act 1949 have been chosen. All of these statutes determine outcomes, at least in part, by reference to the existence of property.

Other statutes also use property in the same way but are not investigated because the remedies included in those statutes are broader; therefore, the remedy in this thesis is less relevant. For example, the Child Support Act 1991 and Legal Services Act 2011 both include provisions that allow the existence of discretionary interests to be taken into account. In child support a person's "financial resources" can be taken into account[134] and in legal aid the possibility of a person receiving a benefit from a discretionary trust can be taken into account.[135] These are both indirect remedies that allow the discretionary interest to be taken into account and supplant the immediate need for the argument made in this thesis.

Statutes that govern economic exchanges between Government and citizens often include references to property ownership. This includes areas of asset or income testing such as Working for Families tax credits, student allowances, unemployment benefits and Residential Care Subsidies. In these areas the direct remedies that reverse the establishment of asset protection trusts are able to provide an effective remedy. This is possible because these statutes do not actually interfere with property but simply assess its extent and value to determine eligibility for Government assistance. Therefore, the establishment of a trust can be deemed to have not occurred for the purposes of the assessment, but the trust itself is not affected.[136] This explains why the remedies in these statutes reach further than those in the Property Law Act 2007 or Property (Relationships) Act 1976. These remedies mean that asset protection trusts have less effect on these statutes and the thesis argument is less important.

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[134] Child Support Act 1991 s 105(2)(c)(i).

[135] Legal Services Act 2011 ss 4, 114(1)(h)(v) and sch 1.

[136] See the Social Security Act 1964, ss 74 and 147A for provisions that allow all property that a person has "deprived" herself of to be taken into account in asset and income testing for Government benefits and Residential Care Subsidies. See the Income Tax Act 2007, s MB 7 for provisions which deem all income earned by a trust and retained by a trustee to be income of the settlor for the purposes of Working for Families tax credits and student allowances.

II. Statutory Definitions of Property and Other Terms

Statutory interpretation begins with the terms that Parliament has used.[137] Despite the importance of Parliament's purpose and context in interpretation, the literal meaning of words is still crucial because statutes are communications from Parliament to the public. A person receiving a communication will, absent indications to the contrary, make basic assumptions about the communicator. The primary assumption is that communicators use words according to the common conventions on the meaning and use of those words.[138] Words in language symbolise concepts. Some symbolise specific concepts, for example "halyard"; others unspecific concepts, like "thing". Most words are able to convey a range of meanings, depending on their context. However, there is a limit to how far the meaning of words can be stretched. As Browne-Wilkinson VC (as he then was) said:[139]

> ... however desirable it may be to construe the Act in a way calculated to carry out the parliamentary purpose, it is not legitimate to distort the meaning of the words Parliament has chosen to use in order to achieve that result. Only if the words used by Parliament are fairly capable of bearing more than one meaning is it legitimate to adopt the meaning which gives effect to, rather than frustrates the statutory purpose.

As mentioned above different terms are used in the selected statutes and the terms have different definitions. Information on these terms is set out in Table 1 and has been sorted into categories that will be explained below.

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[137] See Interpretation Act 1999, s 5(1); John F Burrows *Statute Law in New Zealand* (3rd ed, LexisNexis, Wellington, 2003) at 201.

[138] See Adam Kramer "Common Sense Principles of Contract Interpretation (and how we've been using them all along)" (2003) 23 Oxford Journal of Legal Studies 173.

[139] *Bristol Airport PLC v Powdrill* [1990] Ch 744 (CA) at 759A-C. This case was only three years before Browne-Wilkinson VC's judgment supporting the purposive approach in the House of Lords in *Pepper v Hart* [1993] AC 593 (HL).

Table 1: Statutory Definitions of Property and Other Terms

1. Statute	2. Operative Term	3. Statutory Definition?	4. Inclusive / Exhaustive Definition	5. Interests Specifically Included in the Operative Term	6. Interests Specifically Excluded from the Operative Term
Insolvency Act 2006	"Property"[140]	Section 3	Inclusive: "Property means property of every kind"	"tangible or intangible" property "real or personal" property "corporeal or incorporeal" property "rights, interests, and claims of every kind in relation to property"	Property held on trust[141]
High Court Rules	"Property"[142]	Rule 1.3	Inclusive: "Property includes"	"real and personal property" "any estate or interest in any property real or personal" "any debt" "any thing in action" "any other right or interest"	

[140] Insolvency Act 2006, s 101.

[141] Insolvency Act 2006, s 104.

[142] High Court Rules, rr 17.40-17.82.

Property (Relationships) Act 1976	"Property"[143]	Section 2	Inclusive: "Property includes"	"real and personal property" "any estate or interest in any property real or personal" "any debt" "any thing in action" "any other right or interest"	Property held in any way other than as "the beneficial owner of the property under any enactment or rule of common law or equity"[144]
Family Protection Act 1955	"Estate"[145]	Not in the Act itself, but in section 2 of the Administration Act 1969	Ambiguous: "Estate means real and personal property of every kind"	"things in action"	
Law Reform (Testamentary Promises) Act 1949	"Estate"[146]	Not in the Act itself, but in section 2 of the Administration Act 1969	Ambiguous: "Estate means real and personal property of every kind"	"things in action"	

[143] Property (Relationships) Act 1976, ss 8-18.

[144] This is the definition of "owner" under section 2 of the Act (despite that word not appearing in the Act).

[145] Family Protection Act 1955, s 4.

[146] Law Reform (Testamentary Promises) Act 1949, s 3.

The second column contains the operative terms. These are the terms that are directly relevant to this thesis's argument, which is that the controlling beneficiary has "property" and "estate" and is, therefore, subject to the rules those terms are within and hence the consequences of those rules being applied. These consequences are as follows:

1. Under s 101 of the Insolvency Act 2006, on an insolvent's bankruptcy all of her "property" is transferred to the Official Assignee and is then administered by the Official Assignee for the benefit of the bankrupt's creditors.

2. Under the High Court Rules the High Court can order a debtor's "property" to be charged, sold or transferred to a judgment creditor in satisfaction of a creditor's debt.[147]

3. Upon the separation of the parties to a domestic relationship, or on the death of one party, the "property" of either or both parties is subject to the Property (Relationships) Act 1976. Anything that is their "property" is classified as relationship or separate property under sections 8-10 and then the relationship property is divided between them under sections 11-18.

4. Sections 4 of the Family Protection Act 1955 and 3 of the Law Reform (Testamentary Promises) Act 1949 allow claims to be made against, and satisfied out of, a deceased's person's "estate".

If a controlling beneficiary has no "property" or "estate" then she will not be subject to any of these consequences. Her relationship with the asset protection trust will continue as if these statutes never existed, or, if she is dead, her relationship will cease.

The operative term "estate" cannot be meaningfully distinguished from "property". The definition of "estate" directly refers to "real and personal property".[148] Therefore, all the selected statutes rely on the idea of property.

The fourth column categorises the definitions as inclusive or exhaustive. An inclusive definition is one that adds to the potential meaning of a term ("X includes Y") as opposed to an exhaustive definition that contains all intended meanings ("X means Y"). This could suggest that the Insolvency Act 2006 definition is exhaustive as it uses "means", however, because it goes on to say "property of every kind" it is as inclusive of the potential meanings of property as it is possible to be. The definition of "estate" in the Administration Act 1969 is somewhat ambiguous. Because it is restricted to "real and personal property of every kind" rather than "property of every kind" it is open to an argument that the potential meaning of "real and personal property" is narrower than the potential meaning of "property". However,

[147] High Court Rules, rr 17.40-17.82.

[148] Administration Act 1969, s 2.

it is difficult to conceive of any thing that is "property" that could not also be classified as "real" or "personal".

The significance of the definitions being inclusive is that the potential meanings of "property" are not limited by the definitions. That is, "property" in these statutes may include interests that are outside of the interests that are specifically included. For example, the phrase "any other right or interest" is left out of the definition in the Insolvency Act 2006, but this does not mean that other rights or interests cannot be "property" under that definition. Because "property" is inclusive the Insolvency Act 2006 might include other rights or interests if they are included in the central term "property".

The fifth column contains extended definitions that are added to "property". Depending on how they are understood they have two potential effects. One understanding is that they extend the ordinary meanings of the operative term "property". The other is that they simply confirm the inclusion of interests already contained in ordinary meaning of the operative term. That is, sometimes extended definitions are circular or redundant.[149] The first understanding is implied by Browne-Wilkinson VC when he says in regard to the definition of property in the Insolvency Act 1986 (UK):[150] "It is hard to think of a wider definition of property."[151] This implies that the definition extends the ordinary meaning of property. The second understanding was stated by Lord Atkin in *Nokes v Doncaster Amalgamated Collieries Ltd* with regard to a definition of "property" in the Companies Act 1929 (UK) (that included "property, rights and powers of every description" [152]):[153]

> But in truth the general words in this section describing "property" seem to me to add nothing to the word "property" standing by itself which would be taken by any lawyer to include property, rights and powers of any description.

The question whether the extended definitions in our statutes extend the ordinary meaning of "property" cannot be answered until we have established what property ordinarily means. Lord Atkin's comment suggests the ordinary meaning is broad.

The extended meanings found in the Insolvency Act 2006 and Property (Relationships) Act 1976 definitions do shed light on the question of whether a beneficiary can only have property if it has an entitlement 'in' or 'attached' to the trust property. The definitions include interests in property as one of the types of interests that are included in the broader concept of

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[149] *Re Celtic Extraction Ltd* [2001] Ch 475 (CA) at [26].

[150] Insolvency Act 1986 (UK), s 436: "'Property' include money, goods, things in action, land and every description of property wherever situated and also obligations and every description of interest, whether present or future or vested or contingent, arising out of, or incidental to, property."

[151] *Bristol Airport PLC v Powdrill* [1990] Ch 744 (CA) at 759D-E.

[152] Companies Act 1929 (UK), s 154.

[153] *Nokes v Doncaster Amalgamated Collieries Ltd* [1940] AC 1014 (HL) at 1033.

property. This suggests that property may include rights that are not in things, but also rights against persons or the possibility of receiving rights in the future.

The sixth column of Table 1 excludes certain rights that might otherwise be included in the meaning of property. The Insolvency Act 2006 and Property (Relationships) Act 1976 make it clear that property held on trust is not included as "property" under those Acts. It could be argued that the additional definition provided in the Property (Relationships) Act 1976 limits property interests in relation to trusts to only traditionally recognised beneficial interests in the trust property. However, this would contradict the implication from the definition of "property" that property is wider than equitable rights in things. In my opinion, the definition of "owner" merely excludes any property that is not held beneficially but is held for the benefit of someone else.

The exclusion of property bound by fiduciary duties from the meaning of property is not novel but simply incorporates common law doctrine. A trustee or other fiduciary is bound by fiduciary duties is not the true owner of property. This doctrine has existed since the time of Lord Nottingham.[154] It even applies to the definition of property under the Criminal Proceeds (Recovery) Act 2009, which has the most invasive effects on property ownership of any current statute.[155] The specific exclusion of these interests in statute is merely enacting the common law and the same rule will apply to the other statutes that do not include the specific exclusion.

In conclusion, the statutory provisions provide little assistance in understanding the meaning of property. Their inclusiveness means nothing can be ruled out; if a particular interest is within the ordinary meaning of property it cannot be excluded by the statutory terms but only by reference to context and purpose. In fact the statutory definitions are not truly definitions at all; each definition "is not in truth a definition of the word 'property'. It only sets out what is included."[156] There is potential for the extended definitions to broaden

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[154] This rule is founded in equity. Before the unification of equity and law a trustee's interest could be executed at law by a creditor but there was a rule that the creditor was bound by the same trusts as the trustee. Lord Nottingham is credited (see *Burgess v Wheate* (1759) 1 W Bl 123 at 161, 96 ER 67) with formulating this principle alongside the complementary principle that the beneficiary's equitable interest could be executed in equity by the beneficiary's creditors. The first principle: that the trustee was not treated as the true owner of property is found in *Burgh v Francis* (1670) 1 Eq Ca Abr 320, 21 ER 1074 (Rolls); *Medley v Martin* (1673) Finch 62, 23 ER 33 (Ch); *Finch v Earl of Winchelsea* (1715) 1 P Wms 277, 24 ER 387 (Ch); *Zinck v Walker* (1777) 2 Black W 1154, 98 ER 681 (KB); *Foley v Burnell* (1783) 1 Bro C C 274 at 278, 28 ER 1125 (Ch); *Farr v Newman* (1792) 4 TR 621, 100 ER 1209 (KB); *Taylor v Plumer* (1815) 3 M & S 562, 105 ER 721 (KB); *Re Beattie* (1887) 5 NZLR 342 (SC); *Motor Vehicle Dealers Institute Inc v UDC Finance (1991) Ltd* [1994] 1 NZLR 659 (CA) at 663-664; and *Isolare Investments Ltd v Fetherston* HC Auckland CIV 2002-404-1791, 15 September 2006 at [8]. The second principle: that the beneficiary was treated as an owner whose interest could be executed in equity is found in the Statute of Frauds (1677) 29 Cha II c 3, s 10; *Pit v Hunt* (1681) 2 Chan Cas 73, 22 ER 852 (Ch); *Smithier v Lewis* (1686) 1 Vern 398, 23 ER 542 (Ch); *Balch v Wastall* (1718) 1 P Wms 445, 24 ER 465 (Rolls); *Scott v Scholey* (1807) 8 East 467, 103 ER 423 (KB); *Gore v Bowser* (1855) 3 Sim & Giff 1, 65 ER 537 (Ch); and *Kirkby v Dillon* (1824) CP Cooper 504, 47 ER 623 (Ch).

[155] *R v Williams [Instrument Forfeiture Order]* HC Rotorua CRI-2009-063-5871, 22 July 2011.

[156] *Ord v Upton* [2000] Ch 352 (CA) at 360.

the statutory definition of property beyond the ordinary meaning, but the extent to which this occurs will not be known until the ordinary meanings is considered.

III. The Many Ordinary Meanings of Property

The next step is to look to the ordinary meaning of property. It can be presumed that Parliament intended to use terms like "property" to symbolise concepts with which they are ordinarily associated.

Dictionary meanings of property include "a thing or things belonging to someone",[157] "ownership",[158] "the right to possess, use, and dispose of anything",[159] "something of value, either tangible, such as land, or intangible, such as patents, copyrights, etc"[160] and "any external thing over which the rights of possession, use, and enjoyment are exercised".[161] This diversity suggests that in ordinary language the concept of property involves more than one meaning.

I argue that there is no one ordinary meaning of property but a range of meanings. This pluralistic understanding of property will first be proved and then the range of meanings will be explored.

A. Academic Concepts of Property

The concept of property has received considerable treatment in academia. A number of different concepts of property appear in the literature. One of the most significant in relation to this thesis' argument is from scholars who have developed theories where all instances of property are explained as a manifestation of proprietary rights *in rem* or rights to exclude others from a thing. If these theories are a convincing depiction of the idea of property then the selected statutes ought to be interpreted in accordance with these theories and my argument will fail. However, first Salmond's understanding of property will be examined.

i. Salmond's Meanings of Property

The idea that property has plural meanings is found in Salmond's jurisprudence.[162] He sets out four different meanings of property in a scale. He commences with the broadest:[163]

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[157] Catherine Soanes and Angus Stevenson (eds) *The Concise Oxford English Dictionary* (12th ed, online ed, Oxford University Press, Oxford, 2008) "property *n*".

[158] Catherine Soanes and Angus Stevenson (eds) *The Concise Oxford English Dictionary* (12th ed, online ed, Oxford University Press, Oxford, 2008) "property *n*".

[159] *Collins English Dictionary: Complete & Unabridged 10th Edition* (online ed, HarperCollins Publishers, 2009) "property *n*".

[160] *Collins English Dictionary: Complete & Unabridged 10th Edition* (online ed, HarperCollins Publishers, 2009) "property *n*".

[161] Bryan A Garner (ed) *Black's Law Dictionary* (9th ed, online ed, Thomson Reuters, 2009) "property *n*".

[162] See also DWM Waters "The Nature of the Trust Beneficiary's Interest" (1967) 45 *The Canadian Bar Review* 119; Ronald Sackville "Property, Rights and Social Security" (1978) 2 UNSWLJ 246 at 250; Margaret Davies *Property: Meanings, Histories, Theories* (Routledge-Cavendish, Oxford, 2007).

> In its widest sense, property includes all a person's legal rights, of whatever description. A man's property is all that is *his in law*. This usage, however, is obsolete at the present day, though it is common enough in the older books.

This matches one of the Oxford Dictionary's definitions, which is "a thing or things belonging to someone".[164] It can be accepted that the broadest meaning that can be conveyed by the term "property" is something that could be said to belong to a person. This meaning could certainly include a controlling beneficiary's interest.[165]

Salmond next puts forward a narrower meaning of property:[166]

> In a second and narrower sense, property includes not all a person's rights, but only his proprietary as opposed to his personal rights. The former constitute his estate or property, while the latter constitute his status or personal condition. In this sense a man's land, chattels, shares, and the debts due to him are his property; but not his life or liberty or reputation.

However, Salmond does not use "proprietary" in the way most others use it[167] but in economic terms:[168]

> ... proprietary rights are *valuable*, and personal rights are not. The former are those which are worth money; the latter are those that are worth none. The former are the elements of a man's *wealth*; the latter are merely elements in his *well-being*. The former possess, not merely juridical, but also economic significance; while the latter possess juridical significance only.

This second meaning of property matches the Collins Dictionary's definition of property as "something of value".[169] It also fits with a meaning that only includes those rights that belong to one person and are not shared with others. For example, civil rights such as the right to bodily integrity and the right to vote are shared by every adult person, but rights such as contractual rights are only held by the contracting parties. This second narrower meaning of private property only includes those rights that create a distinction between the members of

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[163] John W Salmond *Jurisprudence* (7th ed, Sweet & Maxwell, London, 1924) at 443 [emphasis in original].

[164] Catherine Soanes and Angus Stevenson (eds) *The Concise Oxford English Dictionary* (12th ed, online ed, Oxford University Press, Oxford, 2008) "property *n*".

[165] See also Laura S Underkuffler "On Property: An Essay" (1990) 100 Yale LJ 127.

[166] John W Salmond *Jurisprudence* (7th ed, Sweet & Maxwell, London, 1924) at 444.

[167] Most modern authors use "proprietary" to mean proprietary rights *in rem* (see P Birks *Unjust Enrichment* (2nd ed, Oxford University Press, Oxford, 2005) at 29; Lionel Smith in "Transfers" in Peter Birks and Arianna Pretto (eds) *Breach of Trust* (Hart Publishing, Oxford, 2002) 111 at 112-119).

[168] John W Salmond *Jurisprudence* (7th ed, Sweet & Maxwell, London, 1924) at 264 [emphasis in original]

[169] *Collins English Dictionary: Complete & Unabridged 10th Edition* (online ed, HarperCollins Publishers, 2009) "property *n*".

a society. It is only rights that are not shared generally by everyone that can be of economic value to those that have them.[170]

Salmond's third meaning for the term property includes only proprietary rights *in rem*.[171] A proprietary right *in rem* or 'in a thing' is a right that is 'in' or 'attached' to a thing and acts as a negative right to exclude a wide range of others from that thing. This is akin to the famous quotation from Blackstone:[172]

> There is nothing which so generally strikes the imagination, and engages the affections of mankind, as the right of property; or that sole and despotic dominion which one man claims and exercises over the external things of the world, in total exclusion of the right of any other individual in the universe.

The exclusionary right *in rem* derives from a special relationship with the things to which it attaches.[173] For example, the owner of land in New Zealand has a right *in rem* to exclude others from entering onto her land. In contrast, a right *in personam* does not attach to a thing but operates against particular people. It derives from a special relationship with a person not with a thing. For example, contractual rights are *in personam* because they are created by explicit agreement between particular people and rights to sue in tort are *in personam* because they derive from a wrong done by a particular person.

This meaning of property matches one of Black's Dictionary's definitions of property, "any external thing over which the rights of possession, use, and enjoyment are exercised".[174] Limiting property to "external things" implies that property does not include rights that are personal. Possession, use and enjoyment necessarily imply that the person having these rights also has the right to exclude others from interfering with them. The right to exclude others from interfering is another way of describing the proprietary right *in rem*.

It is important to note that this understanding of property, that property is limited to exclusionary proprietary rights *in rem*, says nothing about what 'things' can be the subject matter of these rights. For example, a security right or an equitable right is a proprietary right that attaches to a right held by someone else[175] says nothing about what rights they can attach to. It follows that the 'things' that can be subject to security rights or equitable rights must be defined by some other meaning of property than proprietary rights *in rem*. For example, the holder of a security has a right *in rem* to take whatever the subject matter of the security is in

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[170] Lionel Smith *The Law of Tracing* (Clarendon Press, Oxford, 1997) at 52-54; WN Hohfeld "Fundamental Legal Conceptions as Applied in Judicial Reasoning" (1917) 26 Yale LJ 710 at 718 n 20.

[171] John W Salmond *Jurisprudence* (7th ed, Sweet & Maxwell, London, 1924) at 444.

[172] William Blackstone *Commentaries on the Laws of England: Book the Second* (Clarendon Press, Oxford, 1766) at 134.

[173] John W Salmond *Jurisprudence* (7th ed, Sweet & Maxwell, London, 1924) at 258-264.

[174] Bryan A Garner (ed) *Black's Law Dictionary* (9th ed, online ed, Thomson Reuters, 2009) "property *n*".

[175] See Ben McFarlane and Robert Stevens "The Nature of Equitable Property" (2010) 4 Journal of Equity 1; Ben McFarlane *The Structure of Property Law* (Hart Publishing, Oxford, 2008).

certain circumstances. The subject matter of the security might itself be a right *in rem* or it might be a right *in personam* such as a debt or a contractual right. A common colloquial understanding of property is the thing to which a proprietary right can attach.

The narrowest meaning of "property" put forward by Salmond is proprietary rights *in rem* in material objects.[176] The idea of property as things such as land and umbrellas is likely the origin of the idea of property.[177] This meaning is also found in the Collins Dictionary, which includes the meanings "possessions collectively or the fact of owning possessions of value" and "a piece of land or real estate".[178]

Salmond's four meanings of property form a firm base from which to explore the concept of property found in judicial and academic writing. In this thesis "proprietary" rights will not be used as Salmond used it but will be restricted to proprietary rights *in rem.*[179]

ii. Rights to Exclude Strangers

One set of theories are based around the idea that the distinctive mark of property is a right to exclude unidentified strangers from interfering with a thing – that is, a proprietary right *in rem.* The idea of exclusion is not necessarily physical exclusion but exclusion of interacting with the thing in some way. For example, in New Zealand, land owners have a right to physically exclude others from their land, which is clearly a proprietary right *in rem.* However, in Scotland landowners may not exclude others from walking on their land[180] but they do have the right to exclude others from using their land for making a profit. On the other hand, not all rights to exclude others are proprietary rights of exclusion. For example, I may contractually promise you that I will not walk over your neighbour's land in view of your window; this does not give you a proprietary right in your neighbour's land but only a personal right against me.[181]

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[176] John W Salmond *Jurisprudence* (7th ed, Sweet & Maxwell, London, 1924) at 444-445.

[177] See JW Harris *Property and Justice* (Oxford University Press, Oxford, 1996).

[178] *Collins English Dictionary: Complete & Unabridged 10th Edition* (online ed, HarperCollins Publishers, 2009) "property *n*".

[179] This use of "proprietary" is frequent in the literature (see P Birks *Unjust Enrichment* (2nd ed, Oxford University Press, Oxford, 2005) at 29; Lionel Smith in "Transfers" in Peter Birks and Arianna Pretto (eds) *Breach of Trust* (Hart Publishing, Oxford, 2002) 111 at 112-119).

[180] In Scotland the Land Reform (Scotland) Act 2003 has granted the Scots a right to enter onto almost any land for recreational, educational and transport purposes, provided they do so responsibly (John A Lovett "Progressive Property in Action: The Land Reform (Scotland) Act 2003" (2011) 89 Neb L Rev 739 at 741). Armstrong argues that the right to exclude is a relatively new development. For example, he gives examples of societies where sheep farming was an important industry and landowners had no right to exclude herders from crossing or accessing (and damaging) their land (George M Armstrong "The Reification of Celebrity: Persona as Property" (1991) 51 La L Rev 443 at 445-448).

[181] William Blackstone *Commentaries on the Laws of England: Book the Second* (Clarendon Press, Oxford, 1766) at 134; Felix S Cohen "Dialogue on Private Property" (1954) 9 Rutgers L Rev 357; Kevin Gray "Property in Thin Air" (1991) 50 CLJ 252; JW Harris *Property and Justice* (Oxford University Press, Oxford, 1996); JE Penner *The Idea of Property in Law* (Clarendon Press, Oxford, 1997); TW Merrill "Property and the Right to Exclude" (1998) 77 Neb L Rev 730.

This idea of property is about deciding disputes about resources and usually marks the outline of "Property Law" as an academic subject.[182] As Eleftheradis describes this understanding of property:[183]

> The rules of property are established in order to solve the problem of the distribution of resources in a state of scarcity. Private property achieves such a solution by assigning resources to persons separately.

Attempts have been made to extend this understanding of property into a unified explanation of property in all contexts.

The exclusion theory of property efficiently distinguishes proprietary rights *in rem* from personal rights. However, it does not explain why personal rights such as debts and contractual rights are included in the concept of property. Personal rights do not help solve disputes between people's claims to something external to them. For the exclusion theories to provide a unified theory of property they have to include these rights.[184]

Penner, who has put forward the ablest exposition of the exclusion theory, agrees that this is an issue:[185]

> ... a debt cannot be destroyed, or damaged, or taken, or otherwise interfered with in any way which an impersonal duty *in rem* seems well placed to prohibit. The reason is obvious. A debt is an abstract personal right. It has no obvious presence or existence in the world, not even a negative presence like a monopoly in the market place, with which any person might interfere.

The issue with personal rights is that due to their inherently personal nature, from the perspective of the person who holds the right, it is not something that unidentified strangers can interfere with.

Penner's solution is to argue that personal rights that are generally included as property are not actually personal rights but are in fact proprietary. In relation to the right of debt, he suggests that a creditor has a proprietary right to exclude others from interfering with the

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[182] See P Birks *Unjust Enrichment* (2nd ed, Oxford University Press, Oxford, 2005) at 29.

[183] Pavlos Eleftheradis "The Analysis of Property Rights" (1996) Oxford Journal of Legal Studies 31 at 34.

[184] Several scholars who use exclusion theories accept that according to these theories personal rights are excluded as property and simply hold that personal rights are only property in a popular or non-legal sense. See Samantha J Hepburn *Principles of Property Law* (Cavendish Publishing Pty Ltd, Sydney, 1998) [Hepburn gives an account of property law that does not include debts or choses in action that are not related to tangible objects]; R Chambers *An Introduction to Property Law in Australia* (LBC Information Services, Sydney, 2001) at 11; Arianna Pretto-Sakmann *Boundaries of Personal Property: Shares and Sub-Shares* (Hart Publishing, Oxford, 2005) at 107-108, 170-171, 212; Ben McFarlane *The Structure of Property Law* (Hart Publishing, Oxford, 2008) at 21-22, 32-33, 136; Sarah Worthington *Equity* (Oxford University Press, Oxford, 2003) at 77-79 [but see 47-48 where Worthington implies that debts and share holdings are proprietary rights but does not explain why they are not personal]; P Birks *Unjust Enrichment* (2nd ed, Oxford University Press, Oxford, 2005) at 29.

[185] JE Penner *The Idea of Property in Law* (Clarendon Press, Oxford, 1997) at 128-129.

debtor's property that is available to pay the debt.[186] However, Penner admits that, "the holder of the chose in action or equitable interest is not, in general, able to sue the interferer in his own right; the debtor or company or trustee must do so."[187] This admission undermines Penner's argument. He confirms that the holder of a right against a person does not have a right to exclude an open-ended class of others from a thing.[188] A person who must rely on another to enforce her rights does not, in fact, have any rights.

Another solution is to argue the reason a debt is property is not because of the personal right to payment but because the owner of a debt has proprietary rights in the abstract debt relationship. It suggests that a personal right is only property if it is protected by ancillary proprietary rights. Candidates for these proprietary rights have included criminal sanctions against stealing the debt and the tort against interference with contractual relations.[189] For example, the fact that stealing a debt is a crime prevents people from interfering with it.[190] However, because a debt is a personal right, the debt itself can only be stolen from a creditor by the thief dishonestly inducing the creditor to cooperate.[191] The creditor must be involved before the debt can be transferred to the thief, therefore, the criminal law does not act as an exclusionary proprietary interest but rather prohibits fraud against the person holding the interest.

However, this scenario of a debt being taken fraudulently does give rise to one possibility of a proprietary right in relation to personal rights. This is the possibility of a creditor being able to trace and recover a fraudulently taken debt from an innocent receiver of

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[186] JE Penner *The Idea of Property in Law* (Clarendon Press, Oxford, 1997) at 129-132.

[187] JE Penner *The Idea of Property in Law* (Clarendon Press, Oxford, 1997) at 142.

[188] See also John Tarrant "Characteristics of Property Rights" (2008) 16 APLJ 51.

[189] JW Harris *Property and Justice* (Oxford University Press, Oxford, 1996) at 25; TW Merrill "Property and the Right to Exclude" (1998) 77 Neb L Rev 730 at 751. Others have suggested have suggested the tort against interference with contract although this was suggested by FH Lawson and Bernard Rudden *The Law of Property* (2nd ed, Clarendon Press, Oxford, 1982) at 32 who generally follow the economic theory rather than the exclusionary theory. See also Roger J Smith *Property Law* (4th ed, Pearson Education Ltd, Harlow (Essex), 2003) at 12 who generally follows an exclusionary theory but suggests that the tort against interference does not make contractual rights into proprietary rights *in rem*.

[190] On its face it is possible to steal a debt (such as a bank account) under the Crimes Act 1961. Section 2 of the Act includes "any debt, and any thing in action" in its definition of property and theft requires the offender to take property with "intent to deprive the owner permanently of that property" (s 219).

[191] A thief can only steal a bank account with the cooperation of the bank account holder. If a thief uses impersonation, bank cards or internet fraud to induce the bank to pay them money from the creditor's account it does not alter the bank's obligation to the creditor. The thief has defrauded the bank but has not taken the debt because the debt remains payable by the bank to the creditor. The only way a thief could steal the account itself would be by fraudulently inducing the creditor to assign it to them. However, this theft is not so much interfering with the debt; rather it is dishonestly inducing someone to transfer it. Therefore, the law against theft does not prevent interference with personal rights.

Tort, for example, the tort against interference with contract, is unlikely to have a wider scope than the prohibition of theft. For example, the tort cannot prevent interference with a contractual debt (let alone a judgment debt) because an outside party's interference cannot alter the creditor's right to be paid. Outside parties can only interfere with performance of the contractual rights they cannot take or interfere with those rights themselves.

the debt.[192] For example, if Vernon defrauds Harry of a debt and then sells it to Gabrielle, Harry has no personal right against Gabrielle to recover the debt. If Harry has a right against Gabrielle it must be a proprietary right that attaches to the debt and travels with it.[193] Unfortunately, the law of tracing is at present unclear on whether the holder of a legal personal right such as a debt is able to establish such a claim.[194]

It has also been suggested that the holder of a personal right has a proprietary right because they can stop someone else from exercising their right.[195] For example, a creditor can stop someone else calling up their debt and a shareholder can stop someone else from voting on their shares.[196] However, this does not prove there is a proprietary right in a personal right. It only proves that the nature of personal rights is personal.

This relates to Gray's conclusion that excludability is the defining feature of property. A quality of excludability is broader than a proprietary right to exclude others from a thing. It includes personal rights because they naturally exclude others.[197] However, excludability extends the meaning of property to something like Salmond's first meaning of property. Any right that belongs to someone has the quality of excludability.

At present there is no strong presentation of the exclusionary concept of property that can explain all instances of property by the presence of exclusionary proprietary rights *in rem*. There are possibilities, but they all have difficulties.

In my opinion, it is likely that proprietary rights *in rem* are a consequence of an interest being included as property rather than a reason to include it as property. For example, if the owner of a debt is granted a right to recover it from a stranger it is likely because the debt is understood to be property for its economic value and is, therefore, worth protecting with

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[192] A right to recover the debt or damages from the person who committed the fraud in the first place proves nothing in the way of a proprietary interest because they are personally liable for their offending.

[193] See generally Lionel Smith in "Transfers" in Peter Birks and Arianna Pretto (eds) *Breach of Trust* (Hart Publishing, Oxford, 2002) 111 at 112-119; Roger J Smith *Property Law* (4th ed, Pearson Education Ltd, Harlow (Essex), 2003) at 11.

[194] See Lionel Smith *The Law of Tracing* (Clarendon Press, Oxford, 1997) at 326-347. Smith assesses a number of possible grounds for the holder of a legal chose in action to assert a proprietary right if their chose is transferred as a result of fraud. They include a possible common law proprietary right where the stolen debt and any proceeds are automatically legally vested in the defrauded prior owner; even though this would mean that a bank paying money to the thief without notice of the fraud would be liable to the legal owner (*FC Jones & Sons (Trustee in Bankruptcy) v Jones* [1996] 3 WLR 703 (CA)). Smith then looks at the action for money had and received which appears to grant a limited proprietary right to the proceeds of debts (*Lipkin Gorman v Karpnale Ltd* [1991] 2 AC 548 (HL)). Smith finally looks at proprietary claims in equity and whether they can arise to protect the owner of a legal interest. He concludes that they should be able to but that this is not certain (at 347).

[195] Roger J Smith *Property Law* (4th ed, Pearson Education Ltd, Harlow (Essex), 2003) at 5; Sarah Worthington *Equity* (Oxford University Press, Oxford, 2003) at 48.

[196] Shareholders' rights are personal not proprietary rights *in rem*, except in relation to any share certificates (Arianna Pretto-Sakmann *Boundaries of Personal Property: Shares and Sub-Shares* (Hart Publishing, Oxford, 2005) at 73-81.

[197] Kevin Gray "Property in Thin Air" (1991) 50 CLJ 252 at 302.

proprietary rights. The presence of exclusionary proprietary rights is a symptom of property not a cause.

iii. Other Academic Concepts of Property

Other concepts of property are found in the literature but they have not been developed as much as the plural and exclusion theories.

One concept of property that has already made an appearance is the idea that property means rights of economic significance.[198] Apart from Salmond, other formulations of the idea of economic significance include rights that are "cashable"[199] and a right where "the law (or social morality) will in any circumstances at all allow or compel the substitution of money or other value in kind for the thing in question".[200]

Closely aligned to the concept of economic value is the idea of things that can be bought and sold.[201] As Lawson and Rudden said when discussing the reasons why personal rights to be paid a sum of money are included as property:[202]

> ... since they have value, people are willing to buy them; and any valuable asset which is the object of commerce is properly treated as a thing, just as much if it is an abstraction such as a share in a company as if it is a physical object such as a ship or a motor-car.

Associated with this concept of property is the idea of transferability more generally. The acceptance and enforcement by the courts (particularly Chancery) of the assignment of personal rights has been seen as an important step in personal rights being accepted as property in this context.[203] Transferability is one means by which a right can be valuable.

Another concept of property derives from Honoré's famous essay on ownership that identified the core features of ownership of a tangible thing (he used an umbrella as his

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[198] John W Salmond *Jurisprudence* (7th ed, Sweet & Maxwell, London, 1924) at 264; JW Harris *Property and Justice* (Oxford University Press, Oxford, 1996) at 51; Arianna Pretto-Sakmann *Boundaries of Personal Property: Shares and Sub-Shares* (Hart Publishing, Oxford, 2005) at 167-170.

[199] JW Harris *Property and Justice* (Oxford University Press, Oxford, 1996) at 51.

[200] Arianna Pretto-Sakmann *Boundaries of Personal Property: Shares and Sub-Shares* (Hart Publishing, Oxford, 2005) at 168.

[201] FH Lawson and Bernard Rudden *The Law of Property* (2nd ed, Clarendon Press, Oxford, 1982) at 16; Gregory S Alexander *Commodity and Propriety: Competing Visions of Property in American Legal Thought 1776-1970* (University of Chicago Press, Chicago, 1997) at 1. Also see the following where assignability and rights to exclude others are given as the two traditional markers of property: Stephen R Munzer *A Theory of Property* (Cambridge University Press, Cambridge, 1990) at 25; Roger J Smith *Property Law* (4th ed, Pearson Education Ltd, Harlow (Essex), 2003) at 3; Murray Raff "Environmental Obligations and the Western Liberal Property Concept" (1998) 22 MULR 657 at 659-660; Kevin Gray "Property in Thin Air" (1991) 50 CLJ 252 at 292.

[202] FH Lawson and Bernard Rudden *The Law of Property* (2nd ed, Clarendon Press, Oxford, 1982) at 16.

[203] Sarah Worthington *Equity* (Oxford University Press, Oxford, 2003) at 47, 60; Craig Rotherham *Proprietary Remedies in Context* (Hart Publishing, Oxford, 2002) at 8-9.

paradigm example).[204] Honoré identified the following elements that made up full ownership of an umbrella:[205]

> Ownership comprises the right to possess, the right to use, the right to manage, the right to the income of the thing, the right to the capital, the right to security, the rights or incidents of transmissibility and absence of term, the prohibition of harmful use, liability to execution, and the incident of residuarity:

This idea can be extended into a more general concept of property, rather than simply a description of a particular type of interest, by a process of analogy.[206] Interests that share some features of Honoré's core meaning of ownership are included in the penumbra of the concept.[207]

This idea of property offers no logical or internal means to decide if a new interest is property or not. However, it could be an accurate description of how courts decide whether to include a new type of interest as property. It suggests that the ordinary meaning of property is the sum of everything that has already been decided by judges to be property although with a degree of flexibility to add new interests that are sufficiently similar to other previously accepted interests.

As a final point Tarrant has put forward a concept of property based on the idea of "thinghood". That is, property can include anything that is capable of being separated from a person and reified into a thing that may be owned.[208] He first applies this reasoning to include personal rights for the payment of money and then extends it to all other personal legal rights.[209] This concept is very broad and is close to Salmond's widest meaning of property. It may even be broader; the process of reification is simply turning an abstraction into a concrete 'thing';[210] it is not necessarily limited to legal rights. For example, a social relationship like a friendship could be reified into a 'thing'. This concept of property would appear to extend somewhat further than most others.

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[204] See also Roscoe Pound "The Law of Property and Recent Juristic Thought" (1939) 25 ABAJ 993 at 997 for an earlier statement of the elements that make up property. Pound identified six elements: a right to possess, a right to exclude others, a power to transfer, a privilege to use, a right to the fruits and profits, and a right to destroy.

[205] AM Honoré "Ownership" in AG Guest (ed) *Oxford Essays in Jurisprudence* (Oxford University Press, Oxford, 1961) 107 at 113.

[206] See also Stephen R Munzer *A Theory of Property* (Cambridge University Press, Cambridge, 1990) at 22-27.

[207] This concept shares the idea of core and penumbra with HLA Hart "Positivism and the Separation of Law and Morals" (1958) 71 Harv L Rev 593 at 606-615.

[208] John Tarrant "Characteristics of Property Rights" (2008) 16 APLJ 51 at 52-55.

[209] John Tarrant "Characteristics of Property Rights" (2008) 16 APLJ 51 at 55-60.

[210] Catherine Soanes and Angus Stevenson (eds) *The Concise Oxford English Dictionary* (12th ed, online ed, Oxford University Press, Oxford, 2008) "reify *V*".

B. Judicial Concepts of Property

A significant weight of judicial authority supports the pluralistic understanding of property. It is epitomised by Viscount Radcliffe in *Commissioner of Stamp Duties (Queensland) v Livingston*:[211]

> ... the terminology of our legal system has not produced a sufficient variety of words to represent the various meanings which can be conveyed by the words "interest" and "property". Thus propositions are advanced or rebutted by the employment of terms that have not in themselves a common basis of definition.

Pluralism mostly appears during statutory interpretation of terms like property but this does not mean that pluralism is only a product of statutory interpretation rather than part of the ordinary meaning of property. If the courts used statutory interpretation to suggest that property has more than one meaning when ordinarily it only has one then they would be distorting the ordinary meaning of the word.[212]

In New Zealand the Court of Appeal has held that the concept of property is affected by both the statute in which the term is used and the wider context.[213] In Australia, the Queensland Court of Appeal has said "there is no single test for determining what constitutes property"[214] and the Federal Court of Appeal has said "the concept of property may have different connotations for different legal purposes".[215] This view was supported by the High Court of Australia, including Heydon J in dissent, in *Kennon v Spry*.[216] The Supreme Court of Canada has adopted the principle,[217] as has the House of Lords:[218]

> In truth the word "property" is not a term of art but takes its meaning from its context and from its collocation in the document or Act of Parliament in which it is found and from the mischief with which that Act or document is intended to deal.

In contrast to the strong authority for plural meanings of property there are a few cases that have taken a narrower view. However, these can be explained by their context.[219] These statements include the narrow view expressed by Isaacs J in his concurring judgment in

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[211] *Commissioner of Stamp Duties (Queensland) v Livingston* [1965] AC 694 at 712F, 112 CLR 12 (PC).

[212] See *Bristol Airport PLC v Powdrill* [1990] Ch 744 (CA) at 759A-C.

[213] *Z v Z (No 2)* [1997] 2 NZLR 258 (CA) at 279, 282.

[214] *St Vincent De Paul Society (Qld) v Ozcare Ltd* [2009] QCA 335 at [36].

[215] *Wily v St George Partnership Banking Ltd* [1999] FCA 33, 30 ACSR 204 at [6].

[216] *Kennon v Spry* [2008] HCA 56, 238 CLR 366 at [52], [89] and [162].

[217] *Saulnier v Royal Bank of Canada* 2008 SCC 58, [2008] 3 SCR 166 at [16]-[17].

[218] *Nokes v Doncaster Amalgamated Collieries Ltd* [1940] AC 1014 (HL) at 1051 per Lord Porter. See also *Queensbury Industrial Society Ltd v Pickles* (1865) 1 LR Ex 1 at 4-5; *O'Brien (Inspector of Taxes) v Benson's Hosiery (Holdings) Ltd* [1979] 3 WLR 572 (HL); *Kirby (Inspector of Taxes) v Thorn EMI plc* [1988] 1 WLR 445 (CA) at 452F-H; *Re Celtic Extraction Ltd* [2001] Ch 475 (CA) at [26]; *Raymond Saul & Co (a firm) v Holden* [2008] EWHC 2731 (Ch).

[219] See also *Hirschorn v Evans* [1938] 2 KB 801 (CA) at 815.

Commissioner of Stamp Duties (NSW) v Yeend[220] and the widely cited statement of Lord Wilberforce in *National Provincial Bank Ltd v Ainsworth.*[221]

Isaacs J in *Yeend* decided that "property", in a statute with a definition identical to that in the Property (Relationships) Act 1976, must be confined to only include rights "in the nature of property as ordinarily understood".[222] What Isaacs J understood as the nature of property can be inferred from his contrast of "property right" with "personal right" and his reference to authorities that were concerned with proprietary rights. The result Isaacs J reached was that a contractual right was not "property" because it was merely a personal right not a proprietary right in any thing.[223]

Lord Wilberforce's famous statement on property is:[224]

> Before a right or an interest can be admitted into the category of property, or of a right affecting property, it must be definable, identifiable by third parties, capable in its nature of assumption by third parties, and have some degree of permanence or stability.

Like Isaacs J this statement conflates the meaning of property with the meaning of a proprietary right.

The context of this case was a dispute about a house – that is, it was a dispute about who had property rights 'in' that house. The house was legally owned by Mr Ainsworth and the National Provincial Bank Ltd held a charge over the house securing a debt guaranteed by the husband. Mrs Ainsworth was deserted by Mr Ainsworth and had obtained a maintenance order taking into account the fact that she and her children were occupying the house rent free. When the bank made attempts to exercise its rights under the charge Mrs Ainsworth claimed she was entitled to continue living there. The case turned on whether Mrs Ainsworth's right to live in the house was a proprietary right *in rem* that attached to the house or only a personal right against her husband.

Once the context is explained Lord Wilberforce's statement makes sense. The requirements he states are the requirements that must be met before a right that refers to a thing will be recognised by the courts as a right that 'attaches' to that thing and may be asserted against other people generally. Lord Wilberforce is not concerned with the ordinary meaning of "property" but with proprietary rights *in rem.* His statement is a reasonable

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[220] *Commissioner of Stamp Duties (NSW) v Yeend* [1929] HCA 39, 43 CLR 235 at 243-247.

[221] *National Provincial Bank Ltd v Ainsworth* [1965] AC 1175 (HL).

[222] *Commissioner of Stamp Duties (NSW) v Yeend* [1929] HCA 39, 43 CLR 235 at 245.

[223] *Commissioner of Stamp Duties (NSW) v Yeend* [1929] HCA 39, 43 CLR 235 at 245-246.

[224] *National Provincial Bank Ltd v Ainsworth* [1965] AC 1175 (HL) at 1247G-1248A.

description of what is required before a personal right, which refers to a thing, transforms into a proprietary right attaching to that thing and may be exercisable against strangers.[225]

In light of strong authority that property does have plural meanings Lord Wilberforce and Isaacs J's statements on the meaning of property should be treated with caution. They are not good authority to support an argument that property can only mean proprietary rights *in rem*.

C. Conclusion

In conclusion, the ordinary concept of property is plural; there is no single coherent meaning that can be intended by using this term. This conclusion is supported by authoritative judicial comment and the inability of theorists to provide a convincing unified theory of property.

The question of what personal rights are included in property is not answered because it appears that property has a range of ordinary meanings. Depending on the context the ordinary meaning could include rights of economic value, rights that are transferable, proprietary rights in things, all possible rights, or even abstractions that are not legal or equitable rights.

However, the literature shows that the idea of property as exclusionary proprietary rights *in rem* is not universal. This idea explains property as that concept is used in the idea of "Property Law" but does not explain "property".

IV. Parliament's Intended Meanings of Property

The final step in this investigation of the meaning of property is to return to the relevant statutes. We have established that the terms and definitions in these statutes are inclusive so the only literal restriction on the meaning Parliament has conveyed is that it must be a meaning that the term "property" is fairly capable of bearing. We have also established that property has more than one ordinary meaning so Parliament may have intended one or more of a number of meanings. The next step is to ascertain what meaning or meanings Parliament did intend its use of "property" to convey in light of the purposes that the statutes achieve.

From the definitions Parliament has provided it is unlikely to be restricted to equitable or legal proprietary rights *in rem*. It is likely that rights *in rem* are included in the meaning of property but it is also likely that all of the rights and interests that can be the subject-matter of proprietary rights *in rem* are also included. This subject-matter can include personal rights, physical objects, other proprietary rights *in rem* and even abstractions such as the negative monopoly in the marketplace that is intellectual property.

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[225] See Lionel Smith in "Transfers" in Peter Birks and Arianna Pretto (eds) *Breach of Trust* (Hart Publishing, Oxford, 2002) 111 at 112-119 where he suggests equity's extends proprietary rights *in rem* by transforming personal rights *ad rem* (personal rights which refer to a thing, e.g. a personal right to purchase a horse) into proprietary rights *in rem* (e.g. a proprietary right in the horse under the institutional constructive trust that arises under a sale contract).

It will be argued that Parliament's meaning of property in these statutes is likely to include three requirements that must be met before an interest crosses the threshold of property. These requirements are that the interest is legally significant, economically significant and capable of being dealt with under the particular statutory scheme.

A. Legal Significance

Legal significance is implicit in most of the meanings of property discussed so far. All of Salmond's meanings of property referred to legal rights and interests. The judicial comments on property referred to rights, powers and interests. The academic comments also talked about the idea of property in terms of legally significant interests. Even Tarrant, who suggested that the idea of property could include every 'thing' that could be reified, only extended this concept to legally significant things including all rights even though his analysis could be extended to non-legal things.[226]

It appears universally accepted that property is limited to interests that are understood as having current legal significance. In my opinion, this limit on the meaning of property obscures important judicial choices. Whether something is understood as having legal significance is always a difficult judicial choice. The choice ought to be explicit so it can provide guidance on similar future choices.

The line between something that is considered to be legally significant for a particular purpose is illustrated by *Z v Z (No 2)*.[227] Here the Court of Appeal drew a line between legal interests that could be property and personal characteristics such as "intelligence, memory, physical strength or sporting prowess"[228] that could not. The Court held that the husband's enhanced future income earning capacity and qualifications were not property. Future earning capacity, or human capital, was accepted by the Court as an economic concept but was distinguished from property.[229]

In my opinion this distinction can only be made on the basis that earning capacity is not recognised as legally significant. The Court suggested the basic distinction was between "rights in respect of the person, and rights in things."[230] This could be taken as the Court reverting to the exclusionary theories that property is restricted to proprietary rights *in rem*; however, it is clear the Court agreed personal rights were included as property.[231] What the

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[226] John Tarrant "Characteristics of Property Rights" (2008) 16 APLJ 51.

[227] *Z v Z (No 2)* [1997] 2 NZLR 258 (CA).

[228] *Z v Z (No 2)* [1997] 2 NZLR 258 (CA) at 279.

[229] *Z v Z (No 2)* [1997] 2 NZLR 258 (CA) at 283.

[230] *Z v Z (No 2)* [1997] 2 NZLR 258 (CA) at 279.

[231] *Z v Z (No 2)* [1997] 2 NZLR 258 (CA) at 282.

Court appeared to mean by rights in respect of persons was actually "personal characteristics" that lacked any legal significance.[232]

Another area where the line between legal significance and property appears is executory contingent interests in the 18th century. At the start of the 18th century contingent interests were regarded as bare possibilities of receiving rights in the future. They were not accorded any current legal significance and, therefore, could not be assigned, devised by will or descend to heirs.[233] The limit of their legal significance was that they could be released.[234]

Over the course of the 18th century there was a progression towards accepting these interests as legally significant. They were held to be assignable to trustees in bankruptcy solely because they could be released.[235] They were accepted as capable of descending to personal representatives.[236] Their assignment was enforced in equity,[237] but only for consideration, which put them at the same level of significance as the possibility of succeeding to property under the will of a still living relative.[238] The requirement for consideration before equitable assignment would be enforced was then reduced so that all that was needed was love and affection for the assignee.[239] They were then compared to legal contingent remainders and treated as interests in the settled property, which at this time was predominantly land.[240] This culminated in the courts explicitly deciding that contingent interests were interests in the land itself. This was necessary for them to be able to be devised by will under the Statute of Wills 1540,[241] which only authorised the devise of present interests in land.[242] Finally it was accepted at law that contingent interests could be assigned.[243]

The progress of contingent interests from a bare possibility that could not be treated like property to a fully accepted interest in land tracks a change in the courts' acceptance of what is legally significant enough to be property. The nature of the contingent interests themselves did not change.

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[232] *Z v Z (No 2)* [1997] 2 NZLR 258 (CA) at 279.

[233] *Bishop v Fountaine* (1701) 3 Levinz 427 (Ch) [available at www.archive.org].

[234] *Thomas v Freeman* (1706) 2 Vern 563, 23 ER 967 (Ch).

[235] *Higden v Williamson* (1731) 3 P Wms 132, 24 ER 1000 (Ch)

[236] *King v Withers* (1735) Cases T Talbot 117 at 123, 25 ER 693 (Ch).

[237] *Grey v Kentish* (1749) 1 Atk 280, 26 ER 179 (Ch).

[238] *Hobson v Trevor* (1723) 2 P Wms 191, 24 ER 695 (Ch).

[239] *Wright v Wright* (1750) 1 Ves Sen 410, 27 ER 1111 (Ch).

[240] *Goodtitle v Wood* (1740) Willes 211, 125 ER 1136 (CP); *Moor v Hawkins* (1765) 2 Eden 342, 28 ER 929 (Ch).

[241] Statute of Wills 1540 (Eng) 32 Hen 8, c 1.

[242] *Jones v Roe* (1789) 3 TR 88, 100 ER 470 (KB).

[243] *Spragg v Binkes* (1800) 5 Ves Jun 583 at 588, 31 ER 751 (Rolls).

One possible reason for the change in the courts attitude is found in *Goodtitle v Wood* where Willes LCJ pointed out that contingent interests were used in situations where a settlor intended a legal contingent remainder but that interest could not work because of limitations in legal rules.[244] Therefore, the equivalent equitable interests ought to be treated the same as legal contingent remainders. This suggests that social pressures by property owners wishing to use the more flexible equitable interests in their property settlements was the driving factor behind the recognition of these interests as legally significant.

In my opinion, the interests that are legally significant enough to be property are not indicated by Parliament. This aspect of property appears to be largely left up to the courts to decide.

I can find no coherent theory to explain why courts accept that some interests have sufficient legal significance to be property but others do not. In my opinion, this aspect of the concept of property operates by a process of comparing potential legal interests with established legal interests. Thus the extent of interests that are accepted as legally significant changes.

Legal significance is a central issue for the controlling beneficiary's discretionary interest. The discretionary interest is a possibility of receiving property in the future. Some other similar possibilities are treated as legally significant in the present while others are dismissed as merely hopes of receiving something legally significant in the future. This is a central issue in Chapter Three.

B. Economic Significance

Another factor in the meaning of property is that property means interests that are economically significant as well as legally significant. Economic significance means that at least some instances of the relevant type of interest have real economic value. Economic significance is required of property under the selected statutes because these statutes pursue economic purposes.

Economic significance means that the type of interest is capable of being economically valuable but it does not require each instance of that interest to be valuable for it to cross the threshold into property. Sometimes even tangible property has no economic value but is still considered to be property. For example, a lease is a recognised property interest for most purposes but if the rent is higher than the value it can be an economic burden. It is recognised as economically significant because often leases do have economic value. Interests that are recognised as property under the Insolvency Act 2006 can be disclaimed by the Official Assignee if they are onerous.[245]

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[244] *Goodtitle v Wood* (1740) Willes 211 at 213, 125 ER 1136 (CP).

[245] Insolvency Act 2006, s 117.

Another example is contingent or vested but defeasible interests under trusts. They are economically significant because they might result in the receipt of property in the future. However, many instances of such an interest will have no present economic value because the contingencies they are subject to mean that their possible economic benefit is unlikely to be realised. For example, in *Chief Commissioner of Stamp Duties v Buckle* a vested interest in trust property was accepted to be property but was held to have a nil value because it was subject to significant discretionary powers in the trustee.[246]

The purpose of enforcement provisions in the High Court Rules is to provide a means to enforce civil liabilities of an economic nature. They are limited to economic liabilities because the Rules can only be used to enforce a judgment debt, which must be quantified in money terms.[247] Therefore, the creditors should only be able to take things that economically compensate them under the judgment debt.

The Insolvency Act 2006 operates in the same context as the High Court Rules and shares the purpose of providing a means of enforcement for creditors.[248] It has an additional purpose of ensuring creditors have equal access to the debtor's property. Because insolvency is about enforcing economic liabilities the only interests that can compensate that liability are economic interests. In this respect insolvency procedures have changed since the time of the Roman Republic where severed body parts could suffice as satisfaction of debts.[249]

The Property (Relationships) Act 1976 acts as a set of rules to resolve disputes about resources when couples separate or one dies and, therefore, it operate in the same context as proprietary rights *in rem*. However, the Act replaces the ordinary rules of proprietary rights in the 'things' that may be disputed by the separating couple with the statutory rules about how those things are divided.[250] Under the common law of property one separating partner could claim an equitable proprietary right *in rem* in the other partner's personal rights against a bank; the Act overrides this right and replaces it with a statutory mechanism by which the personal right against the bank is included as "property" that is classified and divided between the parties.

The Act's purpose in replacing the ordinary property law is to promote fairness and equality in relationship separations. One of its purposes is to fairly divide the economic advantages and disadvantages accumulated by the separating parties during their

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[246] *Chief Commissioner of Stamp Duties v Buckle* [1998] HCA 4, 192 CLR 226 at [41]

[247] High Court Rules, r 17.1.

[248] Paul Heath and Michael Whale *Heath and Whale on Insolvency* (online looseleaf ed, LexisNexis, New Zealand) at [1.2].

[249] SP Scott *The Civil Law* (The Central Trust Company, Cincinnati, 1932) vol 1 at 64 [being a translation of the Twelve Tables, Table III, Law X].

[250] Property (Relationships) Act 1976, s 4.

partnership.[251] Part of the economic advantage referred to is made up by the parties' "property".[252]

Judicial interpretation has confirmed that property in this context means rights of economic significance. In *Z v Z (No 2)*[253] the Court held: "It is enough that those rights or the interest can be given a money value."[254] Further support is provided by the same Court in *Walker v Walker*,[255] which held that the various interests held by a controlling beneficiary of an asset protection trust, including powers to appoint and remove trustees, could be a valuable bundle of property because the husband would have been willing to pay to keep them.[256] They were clearly an economic advantage.

The connection between economic value and property is only slightly weaker in relation to interests that pass to a deceased's estate. The Family Protection Act 1955 does not explicitly limit provision that may be ordered for plaintiffs to monetary payments but this is implied by the context of the statute as there are several references to "payment".[257] Monetary remuneration for promises is explicitly required in the Law Reform (Testamentary Promises) Act 1949.[258] Although it is possible that non-economic interests might by passed by will, they are not the type of interests that could be claimed against as part of the deceased's estate under these Acts. In *Jones v Skinner*[259] Langdale MR said when interpreting a will, "'property' is the most comprehensive of all terms which can be used, inasmuch as it is indicative and descriptive of every possible interest which the party can have."

Economic significance will not always be part of the meaning of property, as the above discussion of the ordinary meaning of property demonstrates, however, for all of these statutes it is a threshold requirement.

C. Interests Capable of Being Dealt With Under the Statutory Scheme

The third threshold in the meaning of property that appears from the interpretation of these statutes does not derive from Parliament's purpose in legislating but in the scheme that Parliament has chosen to forward its purpose. The statutory scheme adopted by Parliament is relevant to Parliament's intention in respect to the terms it has used.[260] If the interests of the

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[251] Property (Relationships) Act 1976, s 1N.

[252] Dealing with the accumulated economic advantages and disadvantages to the parties is also achieved by a separate assessment of the parties' potential to earn income after the relationship, and by a division of the parties' debts attributable to the relationship.

[253] *Z v Z (No 2)* [1997] 2 NZLR 258 (CA).

[254] *Z v Z (No 2)* [1997] 2 NZLR 258 (CA) at 282.

[255] *Walker v Walker* [2007] NZCA 30, [2007] NZFLR 772.

[256] *Walker v Walker* [2007] NZCA 30, [2007] NZFLR 772 at [60].

[257] Family Protection Act 1955, ss 5, 6, 7.

[258] Law Reform (Testamentary Promises) Act 1949, s 3.

[259] *Jones v Skinner* (1835) 5 LJ Ch 87 (Rolls) at 90.

[260] John F Burrows *Statute Law in New Zealand* (3rd ed, LexisNexis, Wellington, 2003) at 155.

controlling beneficiary are to be property under these statutes they must be capable of being adjudicated under the statutory schemes. The major issue here is transferability.

i. Statutory Schemes in the Insolvency Context

The statutory scheme of the High Court Rules is a series of orders that can be made in relation to a debtor's property. The Rules allow property to be sold, charged and transferred. These are all actions that the debtor could do and, in my opinion, the purpose of the Rules is to force the debtor to take that action. It is unlikely that Parliament would have intended these orders to be used to make a debtor do something that the debtor herself could not have done.[261] Therefore, under the Rules an interest must be assignable or chargeable before it can be property.

Comparison can be made with *Nokes v Doncaster Amalgamated Collieries Ltd*, which concerned a statutory power to transfer property from one company to another in an amalgamation. Property in this context was defined broadly but interpreted to mean only assignable rights on the ground that Parliament could not have intended to give companies power to transfer rights in an amalgamation that they could not have transferred at any other time.[262]

It could be argued that to be chargeable an interest must also be assignable. However, there is a potential argument that an unassignable interest can be charged. In *Don King Productions Inc v Warren*[263] unassignable contractual rights in the name of a partner in a partnership were held to be property that belonged to the partnership. The Court held that it could enforce the other partners' interests in the property by recognising that the partner held the unassignable rights on trust.[264] The inclusion of unassignable rights as property that may be held on trust is a new development and has been criticised.[265] However, this decision could conceivably be extended to allow a debtor's unassignable rights to be charged under the High Court Rules, although it is not certain it would succeed.[266]

The Insolvency Act 2006 operates in the same context as the High Court Rules but there are important differences in their statutory schemes. Two important differences are bankruptcy's finality and the office of Official Assignee.

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[261] This is implied by *Hollinshead v Hazleton* [1916] 1 AC 428 (HL) at 436 where Lord Atkinson speaks about interests which are not subject to execution or unassignable in the same sentence. However, this is not an implication on which much weight can be placed as it was not the focus of Lord Atkinson's statement.

[262] *Nokes v Doncaster Amalgamated Collieries Ltd* [1940] AC 1014 (HL) at 1024, 1033.

[263] *Don King Productions Inc v Warren* [2000] Ch 291 (CA).

[264] *Don King Productions Inc v Warren* [2000] Ch 291 (CA) at [26]-[30].

[265] PG Turner "Charges of Unassignable Rights" (2004) 20 JCL 97.

[266] *Don King Productions Inc v Warren* [2000] Ch 291 (CA) was implicitly approved by the New Zealand Court of Appeal in *Levin v Ikiua* [2010] NZCA 509, [2011] 1 NZLR 678 at [35]-[38], [43] and [46].

The Insolvency Act 2006 is a final accounting by the debtor after which the bankrupt moves on free from his liabilities. This has implications for the meaning of property. The bankrupt's termination of liabilities is a policy compromise between the interests of creditors and the interests of debtors. The debtor gives up his property to compensate the creditors for having their economic rights terminated. The creditors will not be reasonably compensated for giving up their rights unless the debtor gives up all of his rights that could possibly be turned to compensation. Parliament is unlikely to intend that debtors be discharged while retaining economically significant rights that could have been used to compensate the creditors. At least, if Parliament did intend this it would be explicit, as it is when allowing the debtor to keep a certain amount of trade tools.[267] Allowing debtors to keep economically significant interests would critically undermine the compromise between creditors' and debtors' interests. This suggests Parliament must have intended property to mean all of a debtor's economically significant interests regardless of whether they were transferable or not.

This fits with the second difference, which is that the property is vested in the Official Assignee who acts independently and has broad powers to deal with it in the interests of creditors.[268] This mean the property does not need to be transferred to creditors but can be retained by the Official Assignee who can extract economic value from it. If it is assignable then it can be sold, but if it is not then other valuable features of the interest can be used to realise a gain. In principle, an unassignable interest will vest in the Official Assignee because the Assignee "stands in the shoes" of the debtor.[269]

In an early case in England, *Smith v Coffin*,[270] where the basic structure of the insolvency regime was the same as in New Zealand,[271] a right that was not ordinarily assignable was held to pass on bankruptcy. The right in question was a right to recover real property, which at the time could not be assigned or sold or transferred by deed.[272] Eyre LCJ decided that although the right could not be sold it still passed on bankruptcy because, "the most express and plain spirit of the bankrupt laws, which is, that every beneficial interest which the bankrupt has shall be disposed of for the benefit of his creditors."[273] Buller J concurred stating that the object of the bankruptcy laws was "that every thing belonging to the bankrupt that can be turned to profit, shall pass by the assignment for the benefit of the

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[267] Insolvency Act 2006, s 158.

[268] Insolvency Act 2006, s 217, sch 1.

[269] *Official Assignee v Wilson* [2007] NZCA 122, [2008] 3 NZLR 45 at [19], [105].

[270] *Smith v Coffin* (1795) 2 H Bl 444, 126 ER 641 (CP).

[271] The bankruptcy laws at the time were found in the An Acte Touchyng Orders for Banckruptes 1571 (Eng) 13 Eliz, c 7; Bankruptcy Act 1623 (Eng) 21 Jac 1, c 19; An Act to prevent the Committing of Frauds by Bankrupts 1732 (UK) 5 Geo 2, c 30.

[272] *Smith v Coffin* (1795) 2 H Bl 444 at 457, 126 ER 641 (CP).

[273] *Smith v Coffin* (1795) 2 H Bl 444 at 461, 126 ER 641 (CP).

creditors."[274] The House of Lords has stated that property that is neither assignable nor executable passes on bankruptcy.[275]

Some unassignable rights that do result in economic gain have been held not to transfer to the Official Assignee. However, the reason for this is not because they are unassignable. This exception is limited to personal rights where "damages are to be estimated by immediate reference to pain felt by the bankrupt in respect to his body, mind, or character, and without immediate reference to his rights of property."[276] The reason for this exception is expressed in the United States case *Sibley v Nason* which observed, "it is not and never has been the policy of the law to coin into money for the profit of his or her creditors, the bodily pain, mental anguish, or outraged feelings of a bankrupt."[277]

In conclusion, the meaning of property under the Insolvency Act 2006 is likely to include all economically valuable interests regardless of whether they are assignable or not, but with some exceptions based on competing public policy grounds. However, under the High Court Rules property only includes assignable or chargeable interests.

ii. The Statutory Scheme of the Property (Relationships) Act 1976

In relation to the issue of assignability the Property (Relationships) Act 1976 differs from the Insolvency Act 2006 because there is no Official Assignee to extract economic value from the property before passing it on to the separating (or deceased) parties. This could suggest that property under this Act has to be "capable in its nature of assumption by third parties"[278] because property must generally be transferred to one or the other of the separating parties. However, the Court of Appeal has decided that transferability is not required. In *Z v Z (No 2)* a non-transferable partnership interest belonging to the husband was included in the inventory of relationship property.

This is possible because the Act deals with property in two stages.[279] The first step is to establish an inventory of the total property owned by the separating (or deceased) parties and classify it as relationship or separate property.[280] The second step is to divide the relationship property between the parties.[281] An unassignable interest, like the partnership interest in *Z v Z (No 2)*, can be categorised and valued as relationship property in the first stage. It does not have to be assignable because not all relationship property needs to be transferred at the

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[274] *Smith v Coffin* (1795) 2 H Bl 444 at 462, 126 ER 641 (CP).

[275] *Hollinshead v Hazleton* [1916] 1 AC 428 (HL) at 436.

[276] *Beckham v Drake* (1849) 2 HLC 579 at 604, 9 ER 1213 (HL). See also *Wilson v United Counties Bank Ltd* [1920] AC 102 (HL) at 130; *Leach v Official Assignee* [1975] 1 NZLR 83 (SC) at 87.

[277] *Sibley v Nason* 81 NE 887 (Mass 1907) at 889. This case stated that it took the same position as English law.

[278] *National Provincial Bank Ltd v Ainsworth* [1965] AC 1175 (HL) at 1248A.

[279] See *Yeoman v Public Trust* [2011] NZFLR 753 (HC) at [33]-[37].

[280] Property (Relationships) Act 1976, ss 8-10.

[281] Property (Relationships) Act 1976, ss 11-18.

second stage. Provided there is sufficient other relationship property, the other party can be given the assignable property and the unassignable property can be left with its current owner.[282]

Adopting a broad meaning under the New Zealand Act is consistent with Australian family law. The Family Law Act 1975 (Cth) also attempts to fairly distribute the accumulated economic advantages and disadvantages between separating couples, although it achieves this by a different mechanism than the New Zealand Act. The Australian Family Court is given a broad discretion to make orders dealing with the "property of the parties".[283] Property is defined inclusively:[284]

> *property* means ... in relation to the parties to a marriage or either of them ... property to which those parties are, or that party is, as the case may be, entitled, whether in possession or reversion

Despite the use of "means" it is difficult to be more inclusive. Essentially the definition says that "property" means "property" to which a party is entitled. The reference to entitlement only excludes property to which others are entitled. The Family Court has held that the phrase "in possession or reversion" only refers to types of entitlement not to types of property.[285]

The Australian Court is given greater flexibility than the New Zealand Court through being permitted to also consider the parties' "financial resources" as well as "property". However, it is not permitted to make orders that alter or otherwise deal with those financial resources.[286] Despite this extra flexibility, which reduces the necessity for a broad meaning of property, the majority in the leading Australian case of *Kennon v Spry*[287] has confirmed, with reference to Parliament's purpose as evidenced by the ancestry of the legislation, that "property" is to be given a wide meaning.[288] The High Court decided that a right to due administration held by a discretionary beneficiary wife and a husband's power as a trustee to appoint property to his wife were both items of property within the meaning of the Australian Act.[289]

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[282] The understanding of property which has been adopted by the Court of Appeal may create a difficulty if there is ever a case where there is only one piece of relationship property and that one piece is non-transferable and cannot be transferred without interfering with third party rights.

[283] Family Law Act 1975 (Cth), s 79.

[284] Family Law Act 1975 (Cth), s 4.

[285] *In the Marriage of Duff* (1977) 29 FLR 46 (FamCA) at 55-56.

[286] When making orders dealing with property under s 79 the Court may consider those matters listed in s 75 but is not authorised to make orders regarding the things it may only consider (s 79(4)(e)). A party's financial resources are included under s 75(2)(b) of the Family Law Act 1975 (Cth).

[287] *Kennon v Spry* [2008] HCA 56, 238 CLR 366

[288] *Kennon v Spry* [2008] HCA 56, 238 CLR 366 at [54], [91].

[289] *Kennon v Spry* [2008] HCA 56, 238 CLR 366 at [126].

In conclusion, Parliament's intended meaning of the term "property" in the Property (Relationships) Act 1976 has been found to be a wide meaning that is focused on the economic advantages that have been acquired by the parties to the relationship. The ordinary meaning of property as economically significant interests is appropriate. It can even include valuable rights that are not transferable due to the fact that the assessment of property is conducted in two stages.

iii. Statutory Schemes in the Context of Deceased Estates

The scheme of the Family Protection Act 1955 and the Law Reform (Testamentary Promises) Act 1949 simply requires that the property passes to the deceased's estate. As we have seen, "estate" is not defined in the statutes that allow claims to be made, but is in the Administration Act 1969. When Parliament uses the word "estate" it would be logical to include all interests that can be passed by will. Otherwise, the contents of estates would differ depending on whether there was a will or an intestacy. In my opinion, an estate should include all of the deceased's economically valuable interests that a will-maker is capable of passing to her personal representative for the benefit of her descendants.

The next issue is whether a will-maker is capable of passing all of her valuable economic interests by her will. It is argued that a will-maker ought to at least be able to pass all of the valuable interests that would pass to an Official Assignee. It would be contrary to the idea of testamentary freedom if the deceased's valuable rights disappeared or were abandoned on her death simply because they were deemed not to be property. Early cases on the transmission of uncertain contingent interests placed weight on the fact that any interest that could be released ought to be transmissible.[290]

The role of the estate administrator can be compared to the role of the Official Assignee. The duty of the administrator is to use the estate property to pay the deceased's debts and distribute the property according to the will or intestacy, which is similar to administration after bankruptcy. However, the length of time for administration may be shorter than in insolvency. The general informal rule is that administrators have a year to distribute the assets but may postpone distribution for a good reason.[291] This means that administrators may have less freedom to wait for assets to be realised. If the controlling beneficiary's interests are property that passes to the estate then it is likely that the administrator will have a duty to realise them or to pass them on to the estate beneficiaries. In contrast the Official Assignee can wait a very long time in order to realise assets.[292]

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[290] *King v Withers* (1735) Cases T Talbot 117, 25 ER 693 (Ch); *Jones v Roe* (1789) 3 TR 88, 100 ER 470 (KB).

[291] Roger Kerridge *Parry & Kerridge: The Law of Succession* (12th ed, Sweet & Maxwell, London, 2009) at [20-18].

[292] For example, the administration of Equiticorp Holdings has been continuing in New Zealand for more than two decades since it was put into statutory management (Denise McNabb "Equiticorp: The Longest Goodbye" *New Zealand Herald* (Auckland, 15 November 2010)).

However, in many cases there are particular reasons for interests to terminate upon death. The terms of some interests, such as life interests, are specifically that they end upon the death of the holder. It is property that may pass under insolvency but as it ceases to exist on the death of the owner it does not pass to the deceased's estate. Another such interest is a joint interest. The joint interest does not terminate but it passes to the surviving joint owner or owners under the principle of survivorship. Thus nothing passes to the administrators of the estate.

There is a distinction between an interest that ends on death because the person who created the interest wanted the property to pass to someone else on death and interests that would simply be lost or abandoned if they ceased on death. For example, the settlor of a life interest in land intends the land to pass to someone else on the life tenant's death. In contrast, a personal right that ceased on death would simply disappear benefiting the person it was against, which is unlikely to have been explicitly intended. Public policy has tended towards preserving personal rights of action that are not otherwise assignable or transferable by making them transmissible to the personal representatives for the benefit of the deceased's heirs. This is true even of rights that do not pass to the Official Assignee because they relate to the deceased's distress, but defamation actions are an exception.[293]

One particular interest that does terminate on death is a general power of appointment. In the 19th century general powers of appointment were not included in a deceased's estate because the power was understood as neither property nor a proprietary interest in the property subject to the power.[294] Therefore, it did not pass to the deceased's estate but it simply disappeared and the interest that had been subject to the power vested absolutely.

However, because general powers of appointment are such economically significant interests the traditional rule was undermined by a rule of construction. The courts developed a doctrine of interpreting wills disposing of property as an implied execution of the power if it could be inferred that the deceased's will included the property subject to the power. For example, if the power was over a property called Blackacre and the will gifted Blackacre to a particular beneficiary then it would be inferred that the deceased had intended to execute the power over Blackacre. This fiction was incorporated into legislation and has been carried forward into the Wills Act 2007.[295] This means that property subject to a general power of appointment will usually be deemed to pass under a will.

This rule is unsatisfactory because it means that the general power of appointment, which is now understood to be property in the creditor context,[296] will pass under a will but

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[293] Law Reform Act 1936, s 3.

[294] *Bradly v Westcott* (1807) 13 Ves Jun 446, 33 ER 361 (Rolls); contrast *Standen v Standen* (1795) 2 Ves Jun 589, 30 ER 791 (Ch).

[295] Wills Act 2007, s 26.

[296] See Chapter Five of this thesis.

not under an intestacy.[297] Under an intestacy there can be no pretence that the power has been executed.

V. Conclusion

The purpose of this chapter was to understand the meaning of property in the statutes that have been chosen as having the most relevance to controlling beneficiaries.

The overall question was what things, rights or interests are considered property and which are not. This was not answered by the statutory definitions as they were inclusive. The ordinary meanings of property that could be derived from the literature were helpful but produced a broad range of meanings. The purpose and context of the statutes prove most useful in identifying the meaning of property in those particular statutes.

It is argued that three threshold requirements apply before an interest can be property in these contexts. The first is that the interest is recognised by the courts as legally significant. The second is that it must be a type of interest that is capable, in at least some instances, of being economically valuable. The third is that the interest is justiciable under the specific statutory scheme. The first threshold appears to apply to the meaning of property generally. The second threshold applies to all of the selected statutes because their purpose is to provide economic compensation. The third threshold varies in its application between the statutes because they all use different statutory schemes.

These threshold criteria can be applied to the controlling beneficiary's interests in the next two chapters to determine whether his interests can be property in the context of the selected statutes. In addition, this chapter concluded that property is not limited to proprietary rights *in rem* but may include personal rights and other interests. The issue of whether a possibility (that is, an uncertain possibility of receiving property in the future) are considered property in the present was broached briefly in relation to the threshold of legal significance, but is dealt with in more detail in the next chapter.

[297] *Re Churston Settled Estates* [1954] Ch 334 (Ch) at 344.

CHAPTER THREE: DISCRETIONARY INTERESTS AS PROPERTY

This chapter is concerned with whether a discretionary interest meets the threshold requirements to be property under the selected statutes. This chapter is critical in answering whether controlling beneficiaries have property but the analysis also extends to other discretionary beneficiaries such as settlor-beneficiaries.

The question that this chapter asks is whether a discretionary interest can itself be property under the selected statutes.[298] The issue is not whether it is a property interest in the assets held on trust. A discretionary interest is an interest held by the beneficiary and is outside of the trust. It is an interest that is derived from the trust relationship but is not a proprietary right in the trust property.[299]

Further regarding proprietary rights, it is likely that a discretionary beneficiary does have standing to trace misapplied trust property on behalf of the trust.[300] However, this does not necessarily translate into an interest in the trust property.[301] In my opinion it would not be desirable for a discretionary beneficiary to have a proprietary interest in the trust property. If such a beneficiary had an interest sufficient to support a caveat it would interfere with the duties and powers given to the trustees.[302] As such it would make discretionary trusts impractical and cumbersome.[303] This thesis does not argue the discretionary interest is a proprietary interest in the trust property.

A discretionary interest is a type of "possibility". A "possibility" or "expectancy" is a possibility of becoming entitled to property in the future where that future entitlement is uncertain. Many other types of "possibilities" are found in the law and are contrasted with rights that are presently enjoyed or enforceable, or will certainly be received in the future. The overall issue in this chapter is whether a discretionary interest can be property for the

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[298] The Insolvency Act 2006, High Court Rules, Property (Relationships) Act 1976, Family Protection Act 1955 and Law Reform (Testamentary Promises) Act 1949.

[299] *JR v LR (A Bankrupt)* [2011] NZFLR 797 (FC) at [59(xviii)].

[300] Richard C Nolan "Equitable Property" (2006) 122 LQR 232 at 257; *Yeoman v Public Trust* [2011] NZFLR 753 (HC) at [71].

[301] The discretionary beneficiary's tracing right might not be a proprietary right *in rem* in the trust property. Instead it could simply be that the beneficiary has standing to bring claims to protect estate property on behalf of the trustees. This would be similar to the beneficiary of an unadministered estate who has no proprietary right in the estate property but has standing to assert the administrators' rights in the estate property (*Commissioner of Stamp Duties (Queensland) v Livingston* [1965] AC 694 (PC) at 707G-708A, 712E-F).

[302] Cases where a discretionary beneficiary has tried to uphold a caveat are generally, but not completely, supportive of this opinion. Some cases have held that a discretionary beneficiary does not have a sufficient interest to uphold a caveat to protect trust property (see *Naran v Sim* HC Auckland CIV-2010-404-1015, 7 May 2010 at [13]-[14]; *Crosby v Levin Mall Ltd* HC Palmerston North CIV-2011-454-301, 2 June 2011 at [41]). On the other hand, at least one case has suggested that a discretionary interest is sufficient to support a caveat (*Norrie v Registrar-General of Land* (2005) 6 NZCPR 94 (HC) at [40]).

[303] See *Commissioner of Stamp Duties (Queensland) v Livingston* [1965] AC 694 (PC) at 707G-708A, 712E-F.

purposes of the selected statutes while the realisation of the possible entitlement remains uncertain. As established by the previous chapter there are three requirements that must be met before the discretionary interest can meet the threshold of something that is property under the selected statutes.

First, it must be legally significant. That is, the possibility of becoming entitled to property in the future must be recognised as a legally significant interest in the present. It cannot be merely a possibility of receiving a legally significant entitlement in the future, which has no present status. This involves a number of difficult issues and there are arguments each way.

The first issue with legal significance is a tradition of dividing interests in trusts into dual categories: proprietary rights in the trust property and mere expectancies. The latter are regarded as having no legal significance. I challenge this tradition and the cases that follow it. The second issue is the fact the discretionary beneficiary's possible entitlement to trust property depends on the decision of a third party – he will only become entitled if the trustee decides to give him property. This is a reason why discretionary interests have not been regarded as legally significant in at least some contexts. However, in two other contexts possibilities of becoming entitled to property are legally significant despite being subject to discretions. The final issue raised is the relationship between rights that protect an interest while it is inchoate and the recognition of legal significance.

Second the discretionary interest must be economically significant. The case *Re Gartside's Will Trust*[304] (*Gartside*) suggests that a discretionary interest may not be economically significant. It is argued that this case can be distinguished. The second issue is whether any economic advantage received by the discretionary beneficiary is causally linked to the interest he has prior to the trustee's decision. Part of this issue is about whether a discretionary interest is solely the right of due administration or whether the possibility of becoming entitled to trust property is part of the interest. Finally, various cases are raised that have recognised the economic significance of this interest.

The third threshold issue is whether the discretionary interest is amenable to the specific statutory schemes. That is, whether the interest can be charged or assigned under the High Court Rules; pass to the Official Assignee under the Insolvency Act 2006; pass to the discretionary beneficiary's estate on death; or be categorised and valued under the Property (Relationships) Act 1976.

I. The Legal Significance of a Discretionary Interest

The greatest challenge for a discretionary interest being included as property in any of the selected statutes is the issue of whether it has legal significance. This is because discretionary interests are close to the very fine line between interests that have present legal

[304] *Re Gartside's Will Trust* [1968] AC 553 (HL).

significance and those interests that may become legally significant in the future but are not presently accorded any significance.

A discretionary interest is one of many types of interests that can be known as "possibilities". A possibility is where a person may become entitled to property or rights in the future but the realisation of that possibility is uncertain. Possibilities create a dilemma because things that might happen in the future are often an important consideration in the present. For some purposes what is only a possibility or expectation can sensibly be treated as legally significant in the present.

A discretionary interest is a possibility of becoming entitled to property in the future. The possibility will be realised if the trustee decides to appropriate or appoint property to the discretionary beneficiary. The question is whether this possibility is legally significant enough to be treated as property in the present. The same issue arises with all other types of possibility.

An early example of this dilemma appears in relation to the crops that might be grown on land in the future or sheep that might be born in the future. The rights of an owner in relation to land are present rights. However, the rights of an owner to the crops that he may grow on his land are not present rights as the crops do not yet exist. When the crops come into existence the owner will become entitled to present rights in them but if the plants die or for any reason fail to produce a crop no rights will come into existence. Until a present right in crops is actually received the owner only has the possibility of those rights. Thus there is a question whether the possibility of these rights coming into existence at the end of the growing season is legally significant before or during the growing season.

In the 17th century this created a conflict between contract law, which only allowed the sale or mortgage of property, and farmers, who wanted to be able to mortgage and sell their future crops to raise money in the present. This conflict was resolved by treating the uncertain possibility of future rights as having legal significance in the present so it was able to be included as property. In *Grantham v Hawley*[305] it was held that the owner of land or sheep had an interest in his "potential possession" of the fruits of that property. This interest was recognised as having sufficient legal significance that it could be validly sold.[306]

Granting the possibility of future crops legal significance is no longer necessary to fulfil farmers' needs and this doctrine no longer applies. This is because contract law now accepts that the subject matter of contracts is not required to have current legal significance. Sales and mortgages of future crops now take effect as agreements to sell or mortgage those things in

[305] *Grantham v Hawley* (1616) Hobart 132, 80 ER 281 (KB). See also Samuel Williamson "Transfers of After-Acquired Personal Property" (1906) 19 Harv L Rev 557 at 558-559.

[306] It is noted that this solution excluded other forms of potential future property. Any sheep or crops which a farmer might buy in the future rather than grow out of his existing property were excluded from the solution because they were "neither actually nor potentially" his property (*Grantham v Hawley* (1616) Hobart 132 at 132, 80 ER 281 (KB)).

the future when they come into existence.[307] However, the example illustrates the general issue, which is whether a future possibility can be a present interest.

A great range of possibilities are found in law. This thesis cannot survey them all but here is a short list of some:

1. The entitlement which a residuary beneficiary might receive at the end of an estate's administration. While the estate remains unadministered it is uncertain because the beneficiary will not receive anything if property abates in the payment of the estate's debts.[308]

2. Any interest under a trust where the trustee has a prior claim under her right to reimbursement. Until the trustee's claim is satisfied the possibility the beneficiaries will receive property and how much they will receive is uncertain.[309]

3. The possibility of receiving a vested interest under a contingent beneficial interest prior to the condition precedent being satisfied.[310]

4. Vested beneficial interests that may be defeated by a condition that takes effect prior to the beneficiary receiving a right to enjoy the property.[311]

5. A contractual right that is subject to a condition.[312]

6. A future receipt of income.[313]

7. The possibility of becoming entitled to property under the will or intestacy of a relative who is currently still alive.[314] This is known as a ***spes successionis*** or the hope of succeeding to property.[315]

8. An acquisition of property by a future lease or purchase.[316]

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[307] Sale of Goods Act 1908, s 7(3).

[308] See further section I.A.i. below.

[309] *Chief Commissioner of Stamp Duties v Buckle* [1998] HCA 4, 192 CLR 226 at [48].

[310] See *Bishop v Fountaine* (1701) 3 Levinz 427 (Ch) [available at www.archive.org]; *Jones v Roe* (1789) 3 TR 88, 100 ER 470 (KB).

[311] See *Pearson v Inland Revenue Commissioners* [1981] AC 753 (HL).

[312] See *Bevin v Smith* [1994] 3 NZLR 648 (CA).

[313] *Williams v Commissioner of Inland Revenue* [1965] NZLR 395 (CA) at 399; *Johnstone v Commissioner of Inland Revenue* [1966] NZLR 833 (SC) at 838; *Kelly v Commissioner of Inland Revenue* [1970] NZLR 161 (SC) at 163; *Hadlee v Commissioner of Inland Revenue* [1991] 3 NZLR 517 (CA) at 527-529; *Waller v New Zealand Bloodstock Ltd* [2005] 2 NZLR 549 (HC) at [117]-[118]; *Z v Z (No 2)* [1997] 2 NZLR 258 (CA) at 273-283.

[314] *Re Lind* [1915] 2 Ch 345 (CA).

[315] See generally Bryan A Garner (ed) *Black's Law Dictionary* (9th ed, online ed, Thomson Reuters, 2009) "spes successionis *n*"; Albert H Oosterhoff "Great Expectations: Spes Successionis" (1998) 17 ETPJ 181.

All of these possibilities are uncertain. Before any of these possibilities are realised they are merely a chance that the expected future entitlement will materialise. However, some of these possibilities are understood to have current legal significance, whereas others are not.

The fact that the discretionary beneficiary may never become entitled to any property from the trust is not sufficient to exclude it from being property. All possibilities have a chance that no rights will become exercisable. The question of whether a discretionary interest has sufficient legal significance to be property is conceptually the same as the question of whether any of these other possibilities is property. This thesis argues that discretionary interests are legally significant enough to be property and can be distinguished from those possibilities that are understood not to be legally significant.

A. Legal Significance and Proprietary Rights In Rem

The first issue with discretionary interests being recognised as legally significant is a line of New Zealand cases that have categorised them as "bare possibilities" or "mere expectancies". These cases adopt a dual categorisation in which any interest that is not a proprietary interest in the trust property – that is a "possibility coupled with an interest" – must be a mere expectancy and has no legal significance. For example:[317]

> Possibilities are generally arranged into two classes: the one consisting of possibilities which are coupled with an interest, such as contingent remainders, executory devises, springing or shifting uses; the other bare or naked possibilities, such as the hope of inheritance entertained by the heir on the courtesy of his ancestor, or the chance of succession of an individual where the gift is to several with remainder to the survivor. The former class may, perhaps, with more propriety be denominated contingent interests, and the latter mere expectancies; for a possibility coupled with an interest is more than a possibility, it is a present interest, and may be devised.

This categorisation suggests that the discretionary beneficiary's possibility must be connected to a proprietary right *in rem* in the trust property if it is to be more than a mere expectancy.

The leading case in New Zealand on discretionary interests, *Hunt v Muollo*,[318] has applied this dual categorisation. The Court of Appeal was concerned with an application by creditors who wished to examine a debtor, Mr Hunt, on his ability to pay a judgment debt. The creditors sought release of the financial details of trusts of which Mr Hunt was a discretionary beneficiary and companies held on those trusts. The High Court Rules provide a mechanism for discovery in aid of execution of property by creditors. Under the Rules the Court could order the production of documents that aided in the examination of the debtor as to his "income and expenditure, his assets and liabilities, and generally as to his means for

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[316] *New Zealand Bloodstock Ltd v Waller* [2006] 3 NZLR 629 (CA) at [64].

[317] Charles Watkins *The Principles of Conveyancing* (8th ed (revised), Henry Hopley White (ed), Saunders and Benning, London, 1838) at 219-220. See also Charles Watkins *The Principles of Conveyancing* (9th ed, Henry Hopley White (ed), William Benning & Co, London, 1845) at 228.

[318] *Hunt v Muollo* [2003] 2 NZLR 322 (CA).

satisfying the judgment".[319] The Court could only order discovery of documents that were relevant to the debtor's assets or means so if the debtor had no "asset" in relation to the trust then there could be no discovery of the trust's financial details.[320] The Court acknowledged that an "unduly technical approach" to the statutory terms was to be avoided.[321]

The issue the Court presented itself to decide was "whether the interest of a purely discretionary beneficiary in a trust is a species of property capable of coming within the concepts of 'assets' or 'means' for the purposes of"[322] the rule. This is the same issue that is the subject of this chapter.

The Court decided that the discretionary interest was not an "asset"; it held it was a mere expectancy and not an equitable interest in the trust assets:[323]

> It is generally regarded as settled law that a discretionary beneficiary's interest in a normal discretionary trust is no more than a mere expectancy. It is simply an expectation or hope (in Latin a spes) that the trustee's discretion may be exercised in the beneficiary's favour: see Dal Pont and Chalmers, Equity and Trusts in Australia and New Zealand (2nd ed, 2000) at p 505. The position, as stated, is supported by high authority: see *Gartside v Inland Revenue Commissioners* [1968] AC 553 at p 607 per Lord Reid and at p 615 per Lord Wilberforce. An ordinary discretionary beneficiary has no interest, legal or equitable, in the assets of the trust: see *Queensland Trustees Ltd v Commissioner of Stamp Duties* (1952) 88 CLR 54 at pp 62 - 65, *Commissioner of Stamp Duties (Queensland) v Livingston* [1965] AC 694 (PC) and *Pearson v Inland Revenue Commissioners* [1981] AC 753 at p 775 per Viscount Dilhorne and at p 786 per Lord Keith of Kinkel. It is only on the making of a distribution to the discretionary beneficiary that the beneficiary obtains any interest in property, and then only to the extent of the distribution.

This statement by the Court of Appeal can be summarised into two propositions: 1) a discretionary interest is a mere expectancy; and 2) it is not an equitable interest in the assets held by the trustee on trust. The case implies that the discretionary interest must be either one or the other.

Counsel in the case suggested that the interest could be property for the purposes of the High Court Rules even if it was a mere expectancy; however, this was dismissed by the Court. The Court said that whether something is property must be decided on a principled basis and that trust and property law concepts cannot be cast aside.

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[319] High Court Rules, r 621 [this was as the High Court Rules existed in 2003 when the case was heard; the rule is now found in r 17.12].

[320] *Hunt v Muollo* [2003] 2 NZLR 322 (CA) at [14].

[321] *Hunt v Muollo* [2003] 2 NZLR 322 (CA) at [12].

[322] *Hunt v Muollo* [2003] 2 NZLR 322 (CA) at [8].

[323] *Hunt v Muollo* [2003] 2 NZLR 322 (CA) at [11].

In my opinion, the reasoning in this case cannot be supported by trust and property law concepts. First, a possibility can be property without being an equitable proprietary interest in trust property. Second, contrary to the Court of Appeal, it is not settled law that a discretionary interest is a mere expectancy.

i. An Interest can be Property Without Being a Proprietary Right 'in' Anything

In Chapter Two I concluded that the ordinary meaning of property is not restricted to proprietary rights *in rem*. This conclusion is equally as applicable to possibilities as it is to other interests. The suggestion in *Hunt v Muollo* that a discretionary interest is not itself an "asset" because it is not an equitable interest in the trust "assets" is incorrect.

A proof of this argument is provided by the beneficiary of an unadministered estate. The interest of a beneficiary of an unadministered estate is a possibility because the beneficiary hopes to receive property when the administration is complete but this hope may never be realised. The beneficiary's interest may abate through the payment of the deceased's debts. Until the deceased's debts are cleared there is no certainty about what property will be available.

According to *Commissioner of Stamp Duties (Queensland) v Livingston*[324] the beneficiary of an unadministered estate has no interest in or attached to the property held in the estate that the beneficiary might receive. The case was about whether Mrs Coulson, a residuary beneficiary under a will, had a beneficial interest in real or personal property located in Queensland. If she did then that property was subject to succession duty. The Privy Council held that Mrs Coulson did not have such an interest because a residuary interest did not grant a beneficial interest in the estate property. The reason there was no such interest was because a trust could not arise until the subject matter it attached to was certain; until the debts were paid there was no certainty what property would be held in trust for the estate beneficiaries.[325] Therefore, Mrs Coulson had no proprietary interest *in rem* in any one or more of the estate assets located in Queensland.

If a possibility could only be property if it was coupled with a proprietary right *in rem* then, according this case, the residuary beneficiary could have no property. However, Viscount Radcliffe was explicit that Mrs Coulson had a "chose in action, capable of being invoked for any purpose connected with the proper administration of his [sic] estate".[326] Mrs Coulson had a personal right against the trustees to enforce the administration of the estate.

During the administration of the estate Mrs Coulson's personal right allowed her to protect her interest while the possibility that she would become entitled to any property remained uncertain. After the estate was administered, if Mrs Coulson's interest in the residue

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[324] *Commissioner of Stamp Duties (Queensland) v Livingston* [1965] AC 694 (PC).

[325] *Commissioner of Stamp Duties (Queensland) v Livingston* [1965] AC 694 (PC) at 707F-708C.

[326] *Commissioner of Stamp Duties (Queensland) v Livingston* [1965] AC 694 (PC) at 717D.

had not abated then she would become entitled to property as the executors would at that point become obliged to hold the residue on trust on her behalf. However, until it was known whether her interest would abate or not Mrs Coulson had nothing but a possibility of becoming entitled to property in the future protected by a right to enforce due administration of the estate in the present. She had no future right 'in' or 'attached to' the estate property; she only had the possibility of receiving such a right in the future.

However, despite this interest only being made up of a personal right and future possibility it qualifies as property under the Insolvency Act 2006 and the other statutes.[327] Mrs Coulson's possibility of receiving an entitlement to property in the future was legally significant from the point her husband died. From that point she had a personal right to enforce the due administration of the trust. Any property she eventually received from the estate would be derived from and causally connected to her personal right and interest during the estate administration.[328] The value of the right while it was still a possibility would the estimated value of the property that might be received subject to the contingency it might not be received.

Therefore, the legal significance of a possibility does not depend on the existence of equitable rights *in rem*. The Court of Appeal's proposition in *Hunt v Muollo* that the discretionary beneficiary had no equitable right in the trust property could not, by itself, lead to the conclusion that a discretionary interest was a mere expectancy and, therefore, not an "asset".

ii. A Discretionary Interest is More than a Mere Expectancy

The other proposition made in *Hunt v Muollo* is that it is settled law that the discretionary beneficiary has nothing but a "hope" or a mere expectancy of receiving property. In my opinion this is incorrect.

None of the cases cited by the Court of Appeal held that a discretionary interest was a mere expectancy,[329] although earlier cases do agree with the Court. One of the most well-known is *Re Brooks' Settlement Trusts*.[330] Here Farwell J held that a son who was an object of a non-fiduciary power of appointment held by his mother, "had nothing more than a mere

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[327] *Re Leigh's Will Trusts* [1970] Ch 277 (Ch) at 282; *Re Cameron* (1987) 9 NZTC 6,187 (HC); *Official Receiver in Bankruptcy v Schultz* [1990] HCA 45, 170 CLR 306 at 314.

[328] *Raymond Saul & Co (a firm) v Holden* [2008] EWHC 2731 (Ch).

[329] Dal Pont and Chalmers' text does assert a discretionary interest is a mere expectancy (GE Dal Pont and DRC Chalmers *Equity and Trusts in Australia and New Zealand* (LBC Information Services, Sydney, 1996) at 359). However, the only authority it provides is to cite *Re Gartside's Will Trust* [1968] AC 553 (HL). As is explained below *Gartside* does not propose that the discretionary interest is a mere expectancy, indeed it says the exact opposite. The error is repeated in GE Dal Pont *Equity and Trusts in Australia* (5th ed, Thomson Reuters, Sydney, 2011) at [20.125] and in an article by Butler (Lisa Butler "The Legitimate Bounds of a Trustee's Discretion" (1999) 11 Bond LR 14 at n 23).

[330] *Re Brooks' Settlement Trusts* [1939] Ch 993 (Ch). See also *Boyle v Bishop of Peterborough* (1791) 1 Ves Jun 299, 30 ER 353 (Ch); *Smith v Lord Camelford* (1795) 2 Ves Jun 698, 30 ER 848 (Ch); *Lee v Olding* (1856) 25 LJ Ch 580; *Sweetapple v Horlock* (1879) 11 Ch D 745 (Ch).

expectancy, the hope that at some date his mother might think fit to exercise the power of appointment in his favour".[331] However, the authority of this case is no longer valid since the watershed case of *Gartside* – at least not in relation to fiduciary powers of appointment held by trustees.

The House of Lords in *Gartside* held that a discretionary interest was not the type of interest that met the criteria to be an "interest" under the taxation statute in question (this will be discussed below). However, the House did hold that the discretionary beneficiary had a legally significant interest.

Lord Wilberforce found that the discretionary beneficiary had existing rights and that these meant the interest was "more than a mere spes".[332] The discretionary beneficiary had the right to have his interest protected by equity (the right to due administration) and the right to be considered by the trustees.[333] Overall the discretionary interest had "some degree of concreteness or solidity".[334]

Lord Reid for the majority did not directly comment on whether the interest was a mere expectancy. However, he did agree that the discretionary beneficiary had presently exercisable rights.[335] The High Court of Australia has cited *Gartside* as authority that the discretionary interest is not a mere expectancy.[336] Therefore, the citation of *Gartside* in *Hunt v Muollo* to support the proposition that a discretionary interest is a mere expectancy is inaccurate. The proposition in *Hunt v Muollo* has itself been cited in later cases; however, in my opinion, as no other justification has been given for categorising a discretionary interest as a mere expectancy, these citations add little persuasiveness to the proposition.[337]

As well as *Gartside* a series of cases have held that discretionary beneficiaries have presently enforceable rights against the trustees that they can exercise to protect the possibility that they may receive something from the trust.[338] These cases confirm that a discretionary beneficiary has something more than a mere expectancy.

The conflation in *Hunt v Muollo* of a discretionary interest and the ***spes successionis*** of a nephew who hopes to inherit from an uncle given is also inapposite. The nephew has no

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[331] *Re Brooks' Settlement Trusts* [1939] Ch 993 (Ch) at 997.

[332] *Re Gartside's Will Trust* [1968] AC 553 (HL) at 618.

[333] *Re Gartside's Will Trust* [1968] AC 553 (HL) at 617.

[334] *Re Gartside's Will Trust* [1968] AC 553 (HL) at 618.

[335] *Re Gartside's Will Trust* [1968] AC 553 (HL) at 607.

[336] *Cridland v Federal Commissioner of Taxation* [1977] HCA 61, 140 CLR 330 at [23].

[337] *Johns v Johns* [2004] 3 NZLR 202 (CA) at [31]; *Kain v Hutton* [2008] NZSC 61, [2008] 3 NZLR 589 at [25].

[338] *Re Gestetner Settlement* [1953] Ch 672 (Ch); *Re Gulbenkian's Settlements* [1970] AC 508 (HL); *Re Baden's Deed Trusts* [1971] AC 424 (HL); *Re Manisty's Settlement* [1974] Ch 17 (Ch); *Re Hay's Settlement Trusts* [1982] 1 WLR 202 (Ch); *Karger v Paul* [1984] VR 161 (SC); *Spellson v George* (1987) 11 NSWLR 300 (SC); *Schmidt v Rosewood Trust Ltd* [2003] UKPC 26, [2003] 2 AC 70.

rights against his uncle because his uncle is completely free to do what he likes with his property.[339] This is a bare possibility unconnected to any present legal significance. In contrast, a discretionary beneficiary has presently exercisable rights against the trustee and the trustee is not free to do what it likes with the property. The trustee must consider the beneficiary and make a decision regarding distribution only taking relevant factors into account. Thus the discretionary beneficiary has an interest that is legally significant in the present.

In conclusion, the reasoning in *Hunt v Muollo* that a discretionary beneficiary has no equitable interest in the trust property does not mean that it is a mere expectancy with no legal significance. Not all possibilities can be categorised as either a possibility coupled with an interest or a bare possibility.[340] The conclusion in *Hunt v Muollo* that a discretionary interest is not "assets" is not supported by the reasoning deployed. Thus a discretionary interest might meet the threshold of property by being a legally significant interest in its own right. Although *Hunt v Muollo* is precedential authority for the discretionary interest not being property under r 17.12 of the High Court Rules it should not, in my opinion, be taken as authority on the interpretation of any other statute.[341] A number of cases have repeated the statement that a discretionary interest is a mere expectancy but as they provide no supporting reasoning they add nothing to the argument.[342] A discretionary interest is an "expectancy" but it has a certain amount of legal significance.

B. Legal Significance and Possibilities Subject to Discretions

The second argument against a discretionary interest being of sufficient legal significance to be property is the element of discretion. A discretionary beneficiary will only receive property if the trustee decides to distribute property to that beneficiary. This feature distinguishes the discretionary interest from most other types of possibility.

For example, the possibility of the beneficiary of the unadministered estate is not subject to a discretion. It is subject to the existence of debts incurred by the deceased but these can be objectively established. A distinction can be made between interests that are subject to a freely exercisable discretion and those that are subject to objectively ascertainable contingencies, although there is no clear line between the two.

In some contexts a discretion has been held to have the effect of removing legal significance from the interest. However, in other contexts the presence of a discretion has not

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[339] *Re Gartside's Will Trust* [1968] AC 553 (HL) at 602E per Lord Reid.

[340] See also Charles Sweet *Challis's Law of Real Property* (3rd ed, Butterworth & Co, London, 1911) at 76 which rejects the dual categorisation. It adds a category of bare possibilities which can nonetheless be transmitted on death to the deceased's heir.

[341] See *Petricevic v Legal Services Agency* [2011] 2 NZLR 802 (HC) at [39] where Wylie J accepts that a discretionary interest may be no more than an "expectancy" but that it does not prevent the interest being "income or disposable capital" under the Legal Services Act 2011.

[342] *Foreman v Kingstone* [2004] 1 NZLR 841 (HC) at [41]-[48]; *Johns v Johns* [2004] 3 NZLR 202 (CA) at [31]; *Kain v Hutton* [2008] NZSC 61, [2008] 3 NZLR 589 at [25].

had this effect. The question is whether it can be legally significant in the context of the selected statutes.

i. Discretionary Interests Lacking Legal Significance in the Context of the Interpretation Act 1999

One context where a discretionary interest has been held to have no legal significance is under the Interpretation Acts and the repeal of statutes.[343]

Under s 17 of the Interpretation Act 1999 the repeal of a statute does not affect an "existing right, interest, title, immunity, or duty" that arose under that statute. This requires the courts to decide when rights and interests become legally significant for the purposes of this section. In this exercise the courts have had to interpret the meaning of "right".

The leading case from the Privy Council concerned a builder who had a right under a statute to have a building application considered by the Governor-General. The Privy Council decided that this right did not fall within the meaning of "right" in the equivalent statute, and therefore, survive the repeal of the statute, because it was discretionary.[344]

In *Wellington Diocesan Board of Trustees v Wairarapa Market Buildings Ltd* Cooke J cited the Privy Council: "I think those cases show that an application for a purely discretionary benefit should not be treated, for the purpose of s 20(e)(iii), as giving even an inchoate or contingent right to such a benefit."[345]

This example shows that in some contexts a right that is subject to a discretion is not legally significant. However, it must be remembered that legal significance in this context was solely for the purpose of deciding whether the interest was significant enough to survive the repeal of the statute that granted it. It is not for the purpose of deciding whether the interest is legally significant enough to be property.

ii. Discretionary Interests are Legally Significant in the Sale and Purchase of Land

In contrast to the above example, in the context of conditional contracts, rights that are subject to some discretions are legally significant. This context does not concern the interpretation of a statute but a rule of equity. It concerns the issue of when an equitable interest in land is created by the equitable doctrine of constructive trust operating on a contract for the sale and purchase of land.

Equity provides a rule that when there is a contract regarding the purchase of land the purchaser will at some point receive an equitable interest in that land that can be asserted

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[343] See JF Burrows *Statute Law in New Zealand* (3rd ed, LexisNexis, Wellington, 2003) at 420-426.

[344] *Director of Public Works v Ho Po Sang* [1961] AC 901 (PC).

[345] *Wellington Diocesan Board of Trustees v Wairarapa Market Buildings Ltd* [1974] 2 NZLR 562 (SC) at 571. Section 20 of the Acts Interpretation Act 1924 was the equivalent to the current s 17 of the Interpretation Act 1999.

against others. Essentially, the equitable interest operates to protect the purchaser's future receipt of the legal title. This future, and to some extent uncertain, legal interest is protected by the present equitable interest.

Prior to *Bevin v Smith*[346] an equitable interest in land under purchase was understood to arise at the point the purchaser could sue for specific performance to acquire the legal title. Once the purchaser had a right to specifically enforce the purchase agreement he was seen as having an entitlement to receive the property under that agreement and the courts would enforce that entitlement against strangers in equity through the doctrine of constructive trust. By this mechanism the courts transformed the personal right of the purchaser to force the seller to do that "which ought to be done"[347] into a proprietary right *in rem* in the property being purchased.[348]

The issue is at what point equity will recognise that a personal right against the vendor ought to be protected by being transformed into a proprietary right in the property. The old rule was that there must be no hindrance to the purchaser being able to enforce the transfer of the title to the property. This required the contract to be unconditional and the purchaser to be ready and willing to settle. Any condition in the agreement made the purchaser's rights less certain. However, some conditions did not prevent the personal right being transformed into a proprietary right exercisable against strangers. A condition for the sole benefit of the purchaser could be waived and so did not prevent the purchaser enforcing the agreement. However, a contract that was conditional on the discretion of a third party was understood as introducing too much uncertainty into the question of whether the purchaser would become entitled. For example, in a case where a contract for the purchase of land was subject to approval by a court Callan J said, "until the Land Sales Court had spoken, no one knew whether the property was going to belong to the son, and meantime it belonged to the father."[349]

This changed after *Bevin v Smith*. The Court of Appeal decided that the purchaser's interest could be recognised as a present interest in the land even if the contract was conditional on the discretion of a third party. It recognised a purchaser could have equitable title even when their interest was still only a possibility; that is, while no one knew whether the purchaser would receive the property or not.

The Smiths had contracted to purchase two blocks of land from Bevin. The contract was conditional on consent being obtained from the Land Valuation Tribunal. While the contract was conditional, and Bevin remained the legal owner of the two blocks, Landcorp offered to

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[346] *Bevin v Smith* [1994] 3 NZLR 648 (CA).

[347] *Bevin v Smith* [1994] 3 NZLR 648 (CA) at 659.

[348] See Lionel Smith in "Transfers" in Peter Birks and Arianna Pretto (eds) *Breach of Trust* (Hart Publishing, Oxford, 2002) 111 at 112-119.

[349] *Re Rudge* [1949] NZLR 752 (SC) at 757.

sell him a paper road, which ran between the two blocks. The offer was only made because he owned those blocks of land. Bevin threatened the Smiths that he would use the strip of land to prevent them farming the two blocks as a unit. The plaintiffs argued that under the contract for sale Bevin held the two blocks and paper road on a constructive trust for them as purchasers. The Court of Appeal accepted that if Bevin was a constructive trustee of the two blocks when he acquired the paper road he would be bound to hold it on trust as well. The central issue was whether the conditional contract could grant the Smiths equitable title to the land sufficient to make Bevin a trustee of the two blocks.[350]

The Court decided that the possibility that the Smiths might receive the legal title to the land was sufficient to make Bevin a trustee. The key reason supporting this decision was that the Smiths had rights to protect their purchase of the land. The Court decided that the Smiths acquired equitable rights in the land at the point that they acquired personal rights to prevent Bevin dealing with the land inconsistently to his obligations under the contract.[351] Therefore, Bevin was constructive trustee of both the land and the paper road.[352]

It is important to note that the Land Valuation Tribunal or any other party that might be required to consent to a purchase, such as a mortgagee, has no duty to grant consent. They have a discretion to exercise.

In some Government departments the discretion might be constrained to particular reasons. In this case the Court of Appeal did point out that consents by Government bodies were in many cases "ordinarily given as a matter of course",[353] which is not usually true of trustees' decisions. However, the Court did not base its decision on the quality of the discretion but on the fact that the purchaser could protect his interest by actions in equity. Other contracts for the sale of land may require consent by a party that has no duties under administrative law. On the ratio of *Bevin v Smith* these contracts could not be distinguished.

This example shows that possibilities subject to discretions can have legal significance.

iii. Vested Interests in Trusts Subject to Discretions can be Property

A context much closer to the subject of this thesis is other types of beneficiaries whose interests are also subject to the exercise of the trustee's discretion. These are vested or contingent beneficiaries who will become entitled to any trust property left over at the end of the trust period, in the event the trustee decides not to distribute all the property to the discretionary beneficiaries. They are interests in the residuary trust fund on default of appointment and are called "default" interests.

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[350] *Bevin v Smith* [1994] 3 NZLR 648 (CA) at 657-660.

[351] *Bevin v Smith* [1994] 3 NZLR 648 (CA) at 665.

[352] *Bevin v Smith* [1994] 3 NZLR 648 (CA) at 665.

[353] *Bevin v Smith* [1994] 3 NZLR 648 (CA) at 664.

Default interests are generally accepted to be legally significant and included within property.[354] The High Court of Australia has held that a vested interest under a trust that is in default of a power meets the threshold of property. This was even though it was subject to the discretion of the trustees to distribute the entire trust fund to others, to vary the trust terms and to resettle the trust fund upon other trusts. In these circumstances the Court held that the interest was so unlikely to be realised that it was worth practically nothing, however, it was accepted that it crossed the threshold of property.[355] This suggests that an interest that is completely subject to the decision of the trustee can still be property, even where the trustee has a duty to consider exercising the decision.

The question that these interests raise is whether the legal significance of the discretionary interest is comparable to the legal significance of the default interest. A discretionary interest is the possibility of becoming entitled to property that the trustee appoints or appropriates to that beneficiary. A default interest is the possibility of becoming entitled to property that the trustee does not appoint or appropriate to any discretionary beneficiary.

In my opinion, there is only one distinction between the legal significance of the two interests.[356] The distinction is that one beneficiary's interest will be realised from a decision to exercise the power directly in someone's favour and the other will be realised from a decision to not exercise the power. A discretionary beneficiary will only become entitled to property in the future if the trustee makes a positive decision to appoint property to her. A default beneficiary will only become entitled if the trustee makes a positive decision to not appoint all of the property to the discretionary beneficiaries. Both of these interests depend on a positive decision because the trustee has a duty to consider exercising the discretion so must make a positive decision about whether to do so or not.

Consider the example of a trust, settled by Joan, where there is one discretionary beneficiary, Tony, and one contingent default beneficiary, Sally. Tony is Joan's husband and Sally is Joan's daughter. The trustee (Jim) is authorised to make distributions and provide benefits to Tony in his absolute discretion for a period of 30 years. Provided the property is not appointed to Tony, the capital and income will accumulate until Sally becomes entitled to it in 30 years. Tony's possibility of becoming entitled to property Jim appoints to him is the mirror image to Sally's possibility of becoming entitled to any property Jim does not appoint to Tony.

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[354] *Pearson v Inland Revenue Commissioners* [1981] AC 753 (HL) at 771-775, 781-782, 785-786; *Chief Commissioner of Stamp Duties v Buckle* [1998] HCA 4, 192 CLR 226 at [41]; *Johns v Johns* [2004] 3 NZLR 202 (CA) at [49].

[355] *Chief Commissioner of Stamp Duties v Buckle* [1998] HCA 4, 192 CLR 226 at [41].

[356] There is a distinction in the timing of the possible entitlements. The discretionary beneficiary's may become entitled at some point in the period during which the trustee's power can be exercised. The default beneficiary may only become entitled at the end of that period. This is inconsequential to the legal significance of the two interests.

In my opinion, default and discretionary interests are both possibilities that depend on the trustee's discretion. Tony's interest is a possibility of becoming entitled to property if the trustee makes a positive decision to exercise the power. Sally's interest is a possibility of becoming entitled to property if the trustee makes a positive decision not to exercise the power. If Tony enjoys any benefit it will be "by reason of" both being nominated in the trust deed as the object of the power and having that power exercised in his favour.[357] If Sally enjoys any benefit at the end of the trust period it will be "by reason of" both being given an entitlement in the trust deed to any residue left over in default of the power and the trustee's decision to leave a residuary property in the trust fund. In my opinion this difference is not significant enough that a default interest could be included as property in the same context as the discretionary interest was excluded. Either they are both significant enough to be property or neither is.

However, in contrast to my opinion, is the view that the distinction between these interests is more substantial. As the Court of Appeal once said:[358]

> The crucial difference between contingent and vested interests on the one hand and discretionary interests on the other is that possession of the former interests, if enjoyed at all, is enjoyed as of right; whereas discretionary interests are never enjoyed as of right; their enjoyment is always subject to the discretion of the trustees.

I confess I do not understand this distinction.

The impression of the phrase "as of right" is that it does not depend upon any subsequent event. For example, in planning law an activity can be carried out "as of right" if it is a permitted activity under a district plan and does not require an additional consent.[359] It is true that if a default beneficiary, at the end of the trust period when the trustee's power to appoint ceases to be exercisable, becomes entitled to receive any property left in residue it can be said at that point that the beneficiary is entitled to that property as of right. However, until that point arrives, the entitlement may never be enjoyed at all. In my opinion, a future entitlement is not enjoyed as of right while it is subject to a discretion. And it is difficult to suggest that a default beneficiary's future enjoyment of property is not subject to the discretion of the trustees when it is that discretion that will decide if the default beneficiary becomes entitled to anything.

In my opinion, the phrase "as of right" as used by the Court of Appeal equally validly describes the discretionary interest. It is equally valid to say that the entitlement to property that may arise under a discretionary interest, if enjoyed at all, is enjoyed as of right. Once the

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[357] See *Muir or Williams v Muir* [1943] AC 468 (HL) at 484-485 per Lord Romer [Lord Thankerton, Lord Wright, and Lord Clauson approved Lord Romer's judgment (at 477, 479, 486)]; *Queensland Trustees Ltd v Commissioner of Stamp Duties* [1952] HCA 52, 88 CLR 54 at 64-65.

[358] *Johns v Johns* [2004] 3 NZLR 202 (CA) at [49].

[359] *Arrigato Investments Ltd v Auckland Regional Council* [2002] 1 NZLR 323 (CA) at [31]-[32].

trustee has exercised the power to appoint property in favour of a discretionary beneficiary that beneficiary is entitled to it as of right.

It could be argued that the distinction between the interests is because trustee must choose to directly benefit the discretionary beneficiary whereas the default beneficiary benefits by the trustee's decision indirectly. However, the trustee has a duty to consider exercising the power, which means that before the trustee lets the trust period end without exercising the power he must consider the interests of both the discretionary beneficiaries and default beneficiaries. Any decision to let property remain in residue at the end of the trust period must be a decision to benefit the default beneficiaries in preference to the discretionary beneficiaries. There is no distinction here.

My opinion is supported by the House of Lords, which has pointed out that both default and discretionary interests are subject to the discretion of the trustees. *Pearson v Inland Revenue Commissioners* concerned the interests of three daughters in the income from a trust. Their interests were vested in interest but subject to powers in the trustees to accumulate the income or distribute it to the discretionary beneficiaries. When discussing *Gartside* Viscount Dilhorne said:[360]

> That case concerned a discretionary trust where payment was made to the beneficiaries at the discretion of the trustees. Here the three sisters' entitlement to income was subject to the trustees' power to accumulate. On reaching 21 they had no valid claim to anything. If there was any income from the settled property, they were not entitled to it. Their right to anything depended on what the trustees did or did not do and the receipt of income by them appears to me to have been just as much at the discretion of the trustees as was the receipt in income by the beneficiaries in the *Gartside* case.

Lord Keith said:[361]

> ... I do not consider it to be a satisfactory state of affairs that the question whether a person has an interest in possession should turn on the distinction between the position where his interest derives from his being the object of a discretionary power and that where his interest results in a benefit only failing the exercise of such a power. The practical results as regards the person having the interest are unlikely to be materially different in either case, and I can see no good reason why the distinction should lead to a difference of treatment for purposes of capital transfer tax.

The question in this case was whether the daughter's default interest was an interest in possession, not whether the discretionary interest was legally significant. Therefore, these

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[360] *Pearson v Inland Revenue Commissioners* [1981] AC 753 (HL) at 773F-H [Viscount Dilhorne's judgment was a concurring majority judgment, Lord Russell and Lord Salmon dissented].

[361] *Pearson v Inland Revenue Commissioners* [1981] AC 753 (HL) at 786D-F [Lord Lane agreed with Lord Keith's judgment making it the primary majority judgment].

observations regarding discretionary interests are obiter, however, the comparison between default and discretionary interests is clear.

In my opinion, the distinction made in *Johns v Johns* does not mean that discretionary interests have no legal significance. The Court of Appeal in that case held that the discretionary interest was not a "future interest in the trust property"[362] for the purposes of the Limitation Act 1950. This thesis is not arguing that a discretionary interest is an equitable interest in trust property. It is arguing that the discretionary beneficiary's possibility of becoming entitled to property in the future is a legally significant interest in the present.

The fact that the discretionary beneficiary's possibility is subject to the trustee's discretion means it is less legally significant than other interests. However, the fact that a default interest is subject to the same contingency indicates that this is not determinative of whether it is legally significant enough to be property. If the default interest is legally significant enough to be property then the discretionary interest ought to be as well.

iv. Conclusion

In relation to the repeal of statutes it has been said that "[t]he distinction between what is and what is not 'a right' must often be one of great fineness."[363] A possibility of receiving property that is subject to a discretion is close to the border between a legally significant interest and a non-legally significant interest. However, *Bevin v Smith* and *Buckle* prove that in some circumstances a possibility that is subject to a broad discretion can be legally significant.

The fact that there is a technical distinction between a discretionary interest and a default interest does not mean that a possibility of receiving property in the future that is subject to a discretionary interest cannot be legally significant in the present.

C. Legal Significance and Rights to Protect the Realisation of a Possibility

The most significant indication of the discretionary interest's legal significance is the right to due administration of the trust. A common feature of possibilities that are included as property is that they are associated with presently exercisable rights to preserve the future realisation of the possible benefit. As discussed above, the beneficiary of an unadministered estate has the right of due administration that protects her possibility of receiving property at the end of the administration. The same association was made in *Bevin v Smith*[364] to determine when a purchaser had a beneficial interest in land under a conditional contract.

This connection is established in the negative by *Davis v Angel*.[365] In this case, a Mr Crawcour left his nephew an equitable share in his residuary estate contingent upon the

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[362] Limitation Act 1950, s 21(2).

[363] *Free Lanka Insurance Co Ltd v Ranasinghe* [1964] AC 541 (PC) at 552.

[364] *Bevin v Smith* [1994] 3 NZLR 648 (CA) at 665.

[365] *Davis v Angel* (1862) 4 De G F & J 524, 45 ER 128 (Ch)

nephew's marriage to Mr Crawcour's niece Esther.[366] With Mr Crawcour's blessing the nephew married someone else but Mr Crawcour did not alter his will. When he died the case was brought to preserve the nephew's contingent share. It was argued that, as the nephew's wife might die and the niece was still unmarried, it was possible that in the future the niece and nephew might marry and the nephew could claim his share. The Chancellor held that the nephew's interest was nothing more than a mere expectancy.

The consequence of this finding was that the Chancellor denied the nephew any standing or right to preserve the possibility that he might fulfil the conditions of his interest in the future. "The expectation of a future interest, or rather, of a future event that may give an interest, is not a thing that would justify a Court of Equity in entertaining a suit at the instance of a party having that and nothing more."[367]

The connection between rights to enforce a future possibility of becoming entitled to property and that interest being included as property in the present is again found in more two recent United Kingdom cases.

In *Re Campbell* the question was whether payment of compensation awarded to a former bankrupt, Mrs Campbell, was property. The compensation had been paid to the bankrupt by a Criminal Injuries Compensation Board after she had become bankrupt but for injuries she had suffered several years before she was bankrupted. The judge decided that when Mrs Campbell was bankrupted she had nothing but a hope of compensation that was not a present interest. Kay J did not decide this because her interest was subject to the discretion of the Board. He decided it because Mrs Campbell had "no right either to sue for the award or when the award is made to recover the award."[368] That is, because Mrs Campbell had no right under statute to protect her possibility of receiving compensation that possibility was not legally significant.

The second case is *Abrahams v Trustee of the Property of Abrahams* where the issue was whether a former wife was beneficially entitled to the winnings of a lottery ticket syndicate of which her husband had been a member. The wife argued that the husband's interest in the syndicate beneficially belonged to her. The trustee in bankruptcy of the husband argued on the basis of *Re Campbell* that contractual rights in respect to a lottery ticket could have no significance as property because it was a mere hope of receiving something in the future; therefore, they could not be property that could be held on trust. The Court disagreed and pointed out the crucial difference between the two cases. In *Re Campbell* the injured woman had no existing rights. In this case the husband, as a member of the lottery ticket

[366] This use of trusts for controlling the behaviour of relatives is perhaps typical of the 18th and 19th Centuries. It has been said that powers of appointment between children act "as a distrust upon the children, and for the purpose of ensuring their obedience." (*Boyle v Bishop of Peterborough* (1791) 1 Ves Jun 299 at 309, 30 ER 353 (Ch)).

[367] *Davis v Angel* (1862) 4 De G F & J 524 at 529, 45 ER 128 (Ch)

[368] *Re Campbell* [1997] Ch 14 at 17C.

syndicate, had contractual rights against the other members to have any winnings administered according to the rules of the syndicate. These rights were sufficient to afford the possibility of future winnings legal significance in the present.[369]

The fact that discretionary beneficiaries have the right of due administration to protect their interests, along with the derivative right to have their interests considered, strongly suggests that they are legally significant. On this basis, possibilities that are property can be contrasted with possibilities that are not associated with presently existing rights. For example, the nephew's hope of succeeding to his uncle's property on his death is not associated with any presently existing rights. The nephew has no standing to prevent the uncle from giving all of his property away during his lifetime. This suggests that the nephew's possibility is not legally significant.

This suggestion is further supported by *Schmidt v Rosewood Trust Ltd.*[370] The Privy Council in this case decided that a discretionary beneficiary should be given access to trust documentation under the courts' inherent supervisory jurisdiction. Giving the discretionary beneficiary the means to protect his interest was justified in this case because the particular beneficiary had an exceptionally strong claim on the exercise of the trustee's discretion.[371] He had such a claim because he was the son of a deceased settlor. This exercise of discretion by the Council strongly suggests that being the object of a power of appointment is legally significant.

The Council did say that some discretionary beneficiaries will not deserve access to trust information because they will have a low probability of receiving anything from the trustees. This is a product of beneficiaries' access to information not being a right but subject to the courts' overriding discretionary jurisdiction over the supervision of trusts. It does not detract from the main point, which is that the interest must be legally significant to some degree for him to ever deserve to receive trust information. The courts' inherent jurisdiction is not likely to extend to ordering the trustees to give information to strangers with no legally significant connection to the trust.

D. Conclusion: Legal Significance and Parliament's Intention

The overriding question in relation to discretionary interests is whether the statutory terms chosen by Parliament extend to possibilities of receiving property at the decision of a trustee. The question is whether discretionary interests are legally significant enough for the purposes these statutes fulfil.

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[369] *Abrahams v Trustee of the Property of Abrahams* [2000] WTLR 593 (Ch).

[370] *Schmidt v Rosewood Trust Ltd* [2003] UKPC 26, [2003] 2 AC 70.

[371] *Schmidt v Rosewood Trust Ltd* [2003] UKPC 26, [2003] 2 AC 70 at [68].

The purpose of all of these statutes is to provide economic compensation to certain groups. However, Parliament has provided little direct guidance on what possibilities are legally significant enough to be included as property.

In my opinion, Parliament is unlikely to have intended that a discretionary interest is necessarily excluded from the meaning of property. The degree of legal significance required before something can be property is lower than the degree of legal significance required before it survives the repeal of a statute that creates the interest.

An example of an interest that is established as a legally significant interest but is arguably less legally significant than a discretionary interest is goodwill. Goodwill is the value attributed to the established reputation of a business and includes "every advantage acquired by the proprietor in carrying on his or her business".[372] Goodwill has legal significance sufficient to be property under the Property (Relationships) Act 1976 and Insolvency Act 2006[373] but only if it is attributed to a business and not to an individual's "skills, knowledge, efforts, training, or reputation".[374]

In my opinion, goodwill has less legal significance than a discretionary interest. A discretionary interest has a certain and observable origin in a legal document. A discretionary beneficiary has the right to due administration to protect her interest. The owner of goodwill may have various rights that can be asserted to protect various parts of the goodwill but then again he might not. These rights could include a contractual right under a restraint of trade or rights to enforce trademarks, but in many respects the reputation that makes up the business's goodwill is ephemeral and not able to be protected by legal rights.

In conclusion, in my opinion, discretionary interests are present legal interests, which are significant enough to be property as that concept is used in the selected statutes. Discretionary beneficiaries have a presently exercisable right to protect the possibility that they will receive property in the future. This right to due administration is sufficient to give the discretionary interest legal significance in the present. Therefore, in my opinion, it meets this first threshold requirement for being property.

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[372] *Edwards v O'Connor* [1991] 2 NZLR 542 (CA) at 549-550. See also Bryan A Garner (ed) *Black's Law Dictionary* (9th ed, online ed, Thomson Reuters, 2009) "goodwill *n*"; Catherine Soanes and Angus Stevenson (eds) *The Concise Oxford English Dictionary* (12th ed, online ed, Oxford University Press, Oxford, 2008) "goodwill *n*".

[373] RL Fisher (ed) *Fisher on Matrimonial and Relationship Property* (online looseleaf ed, Lexisnexis, New Zealand) at [10.16]; Paul Heath and Michael Whale *Heath and Whale on Insolvency* (online looseleaf ed, LexisNexis, New Zealand) at [4.13].

[374] Bryan A Garner (ed) *Black's Law Dictionary* (9th ed, online ed, Thomson Reuters, 2009) "personal goodwill *n*". See also Z v Z [1989] 3 NZLR 413 (CA); RL Fisher (ed) *Fisher on Matrimonial and Relationship Property* (online looseleaf ed, Lexisnexis, New Zealand) at [10.16].

II. The Economic Significance of a Discretionary Interest

The second threshold requirement to be property, which applies to each of these selected statutes, is that the interest must be of economic significance. Property under the High Court Rules must be economically significant because it is used to compensate creditors with judgment debts. Property under the Insolvency Act 2006 must be economically significant because it signifies interests that can be used by the Official Assignee to compensate creditors of a bankrupt. Property under the Property (Relationships) Act 1976 must have some economic significance because the purpose of the statute is to fairly divide the economic advantages acquired by the parties. As Griffiths has said a type of interest that can never be valued is unlikely to be property in these contexts.[375]

The question is now whether a discretionary interest can be economically significant. However, as demonstrated by *Pearson*[376] and *Buckle*,[377] not all discretionary interests need to have an identifiable economic value. Some interests meet the threshold requirements of property but have a nominal or nil value. Therefore, the question is whether at least some discretionary interests can be of economic value.

There are two issues with the economic significance of the discretionary interest. First, *Gartside* decided that a discretionary interest in income was not economically certain enough to be property in a taxation statute. Second, Lord Reid in *Gartside* suggested in obiter that the discretionary interest was causally disconnected from any economic benefit that might be received.

These arguments will be countered and followed by the argument that the discretionary interest is economically significant. A number of cases in New Zealand, up to the Supreme Court level, have suggested that a discretionary interest is economically valuable.

A. Gartside and the Economic Significance of a Discretionary Interest

There is a possible argument that the House of Lords in *Gartside* has held that a discretionary interest is not economically certain enough to be property. I agree that was part of the ratio in *Gartside.* However, the context of this case can be clearly distinguished from the contexts of the statutes under consideration.

Gartside concerned a provision in an estate duty statute and whether it applied to a deceased discretionary beneficiary. The statute provided that any property in which the deceased had an interest that ceased on his death would be notionally added to his taxable estate. This also included property in which he had previously had an interest of this nature but that was terminated prior to his death. Part of the trust property in question had been

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[375] Shelley Griffiths "Valuing 'Bundles of Rights' for the Property (Relationships) Act 1976: When Neither Art nor Science is Enough" (2011) 7 NZFLJ 98 at 102.

[376] *Pearson v Inland Revenue Commissioners* [1981] AC 753 (HL).

[377] *Chief Commissioner of Stamp Duties v Buckle* [1998] HCA 4, 192 CLR 226 at [41].

distributed to the deceased's sons, who were also discretionary beneficiaries, while he was alive. The argument for the revenue was that the discretionary beneficiary had an interest in the trust property that had been terminated when it was irrevocably distributed to the other beneficiaries.

The House had to decide whether the discretionary interest was within the meaning of "interest" under the estate duty statute. In interpreting the meaning of this term the first step was whether termination of the discretionary interest resulted in a "benefit accruing or arising".[378] It was the benefit that accrued or arose on the termination of an interest that was to be valued and taxed.[379] For example, if a life interest was terminated before the end of the life a benefit would accrue to the beneficiary entitled subsequently to the life interest. The value of the benefit would be the value of the right to the income from the trust until the former life tenant died.

The next step was whether the termination of a discretionary interest could result in a benefit accruing to someone else. This was determined by reference to words in the statute that required the "interest" to "'extend' either to the whole or to a part of the income of the property in which the right gave to its owner the 'interest.'"[380] For an interest to extend to all or part of the income it required an entitlement to receive a definite part of the income.[381] Thus a discretionary interest was not an interest because it was not entitled to a definite part of the income.

These provisions mean that the interest needed to be a proprietary interest 'in' or 'attached to' the trust property. Part of the ratio of *Gartside* is that a discretionary interest is not an interest in trust property of a definable extent and, therefore, is not an interest in property of the type relevant to the particular estate duty statute. In this case it would not have been effective for the revenue to argue that the discretionary interest itself was property because the deceased still had that interest when he died, but it was very unlikely to be worth anything because the underlying trust property had been given to someone else.

A second part of the ratio of this case is that interpretation of an interest in the trust fund was founded on the statutory context. Lord Reid pointed out that if a discretionary beneficiary was accepted as having an entitlement to all of the income merely because he had the possibility of being distributed all of that income then estate duty would be chargeable on the entire estate on the death of each discretionary beneficiary. Parliament could not have intended to tax the same property multiple times.[382] Lord Wilberforce stated taxes must be

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[378] *Re Gartside's Will Trust* [1968] AC 553 (HL) at 604A.

[379] *Re Gartside's Will Trust* [1968] AC 553 (HL) at 603-604, 616.

[380] *Re Gartside's Will Trust* [1968] AC 553 (HL) at 604B-C.

[381] *Re Gartside's Will Trust* [1968] AC 553 (HL) at 604F, 616E.

[382] *Re Gartside's Will Trust* [1968] AC 553 (HL) at 605C-D.

"ascertained with precision".[383] Therefore, in the context of this taxation statute, even if the discretionary interest was a proprietary right in the trust property, it was not an "interest" because it could not be valued with a high degree of certainty. Uncertain possibilities, such as a discretionary interest, are excluded by the statutory language and context.

In contrast to the taxation context in Gartside, in other contexts interests do not need to be valued with precision to pass the threshold of economic significance. The requirement that an interest be able to be valued is not a single universal test. An interest that cannot be valued for the purpose of the taxation statute in *Gartside* may be able to be valued for other purposes. Failing to meet the requirement for economic significance in *Gartside* does not mean the discretionary interest is not economically significant enough to be valued in other contexts.

Under the Property (Relationships) Act 1976 property does not need to be capable of being valued with precision.[384] Uncertain possibilities are included under this statute. Practical difficulty in placing a value on a possibility does not prevent it being property.[385]

Under the other selected statutes, where property passes to the creditors, Official Assignee or administrators of the deceased estate, it does not need to be valued at all. Therefore, there is no requirement for it to be valued with precision. As long as it is capable of being of some value to the recipients of the interest it should meet the requirement of economic significance.

For example, there is the question of whether a discretionary interest that vests in the Official Assignee will benefit the creditors. (The issue of whether a discretionary interest can pass to the Official Assignee is dealt with below.[386]) It is likely that a trustee will prefer to provide benefits to other beneficiaries than providing benefits to the Official Assignee. This is not because they are economically insignificant but because their significance will drop sharply if the beneficiary becomes bankrupt – a trustee is less likely to decide to distribute to a beneficiary if she knows it will go to his creditors. However, provided that the trustee is authorised to benefit the Official Assignee,[387] the trustee may benefit it and, therefore, the interest may be of economic significance. This will be even more significant if the right to replace trustees also passes to the Official Assignee and it can appoint a trustee who is likely to prefer the interests of the Official Assignee. The same reasoning applies to the other statutes that require an interest to be passed rather than valued.

In conclusion, *Gartside* is not authority that the discretionary interest is never economically significant. It is authority that it is not sufficiently certain enough economically

[383] *Re Gartside's Will Trust* [1968] AC 553 (HL) at 616B-C.

[384] *Reid v Reid* [1980] 2 NZLR 270 (CA) at 272.

[385] Shelley Griffiths "Valuing 'Bundles of Rights' for the Property (Relationships) Act 1976: When Neither Art nor Science is Enough" (2011) 7 NZFLJ 98 at 99; *Haldane v Haldane* [1981] 1 NZLR 554 (CA) at 569-570.

[386] See section III of this Chapter of this thesis.

[387] See section III of this Chapter of this thesis.

to be an interest under the particular taxation statute it was concerned with. However, the House explicitly agreed that it might be an interest in other contexts.[388]

B. Causation and Economic Significance

There is another possible argument from *Gartside*. It is based on an obiter comment by Lord Reid that:[389]

> ... a right to require trustees to consider whether they will pay you something does not enable you to claim anything. If the trustees do decide to pay you something, you do not get it by reason of having the right to have your case considered: you get it only because the trustees have decided to give it to you.

Using this comment it could be argued that the trustee's decision is the only important cause of the beneficiary receiving any property. Therefore, the beneficiary's previous interest, as a nominated object of the power, ought to be completely discounted as a cause of the economic benefit received. That is, it is the trustee's decision that has sole economic significance and the discretionary interest prior to that decision has no significance.

Another way to frame the causation objection is to accept that the right to due administration is property but to suggest that it is economically worthless. This right is legally significant and could fit within a statutory definition of property as a chose in action. However, the right to ensure the trust is administered correctly does not necessarily lead to any economic benefit for the beneficiary.

The discretionary beneficiary's right to due administration can be contrasted to that of a fixed beneficiary, who might be able to exercise the right to force the trustee to provide a benefit; if the fixed beneficiary is given an entitlement to receive property under the trust deed then he can enforce that entitlement through his right to due administration. In contrast, the discretionary beneficiary can only force the trustee to consider benefiting her. As Griffiths has said:[390]

> Enforcement of a right to be considered results only in being considered. It does not necessarily result in anything being distributed to the person who brought the claim. For that reason any monetary value would necessarily be minimal.

The problem with this argument is that the ultimate receipt of property is not in fact causally disconnected from the creation of the discretionary interest. A person is only able to receive distributions from the trust because he is included as an object of the discretionary power. Any eventual receipt of property by a discretionary beneficiary is caused by several

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[388] *Re Gartside's Will Trust* [1968] AC 553 (HL) at 612, 620.

[389] *Re Gartside's Will Trust* [1968] AC 553 (HL) at 607.

[390] Shelley Griffiths "Valuing 'Bundles of Rights' for the Property (Relationships) Act 1976: When Neither Art nor Science is Enough" (2011) 7 NZFLJ 98 at 101.

"links in the recipient's chain of title".[391] The trustee's decision may be just as important or even more important to any realisation of the possibility but it is not a new intervening event that breaks the chain of causation with the prior discretionary interest.[392]

The right to due administration is not separate from the beneficiary's interest as a whole.[393] This right protects the discretionary interest. The discretionary interest is the possibility of receiving property in the future. The right to consideration reinforces this possibility by ensuring it cannot be ignored by the trustee.

Indeed, traditionally the nomination of a discretionary beneficiary as an object of the power has been seen as the most important link in any eventual benefit. The traditional principle was that if a discretionary beneficiary received property he received it "by reason of" the original settlement, not "by reason of" the trustees' decision.[394]

This type of causation argument was attempted in *Raymond Saul & Co (a firm) v Holden*[395] in relation to the interest of a beneficiary in an unadministered estate. The beneficiary accepted that his right to due administration of the estate was property[396] but argued it was casually disconnected from his eventual receipt of property. The court disagreed. It followed Buckley J's proposition in *Re Leigh's Will Trusts*[397] that the purpose of the beneficiary's right to due administration is to protect the interest that the beneficiary hopes to receive in the future. Therefore, there was a direct connection between the right protecting the possibility and the realisation of the possibility.[398]

C. The Case for Economic Significance

The discretionary interest is economically significant because it is a possibility of receiving property in the future. The likelihood of this receipt can be predicted to a certain degree although, like any other prediction, will never be entirely accurate. Where the discretionary beneficiary's possible future benefit is likely the courts have been unable to ignore it.

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[391] *Queensland Trustees Ltd v Commissioner of Stamp Duties* [1952] HCA 52, 88 CLR 54 at 64-65.

[392] See *Queensland Trustees Ltd v Commissioner of Stamp Duties* [1952] HCA 52, 88 CLR 54 at 64-65.

[393] See *Re Gartside's Will Trust* [1968] AC 553 (HL) at 602F per Lord Reid.

[394] See *Muir or Williams v Muir* [1943] AC 468 (HL) at 484-485 per Lord Romer [Lord Thankerton, Lord Wright, and Lord Clauson approved Lord Romer's judgment (at 477, 479, 486)]; *Queensland Trustees Ltd v Commissioner of Stamp Duties* [1952] HCA 52, 88 CLR 54 at 64-65.

[395] *Raymond Saul & Co (a firm) v Holden* [2008] EWHC 2731 (Ch).

[396] Under the Insolvency Act 1986 (UK).

[397] *Re Leigh's Will Trusts* [1970] Ch 277 (Ch) at 281-282.

[398] *Raymond Saul & Co (a firm) v Holden* [2008] EWHC 2731 (Ch) at [51].

The first case is the Court of Appeal in *Walker v Walker*.[399] The Court decided, in obiter and without prompting by counsel, that two discretionary interests were "assets"[400] and "items of property" under the Property (Relationships) Act 1976.[401] The Court described the interests as individual items of property that, along with others interests in the trust including a directorship and shareholding in the corporate trustee, the power to remove and replace directors of the trustee, and a power to remove and replace the trustees formed a "very valuable package, as together they confer control of the company".[402]

On the face of the Court's judgment it appears to have considered the individual interests to be separate items of property rather than a "bundle of rights" that was itself property but made up of non-property interests. Although the package of interests was more valuable than the individual interests there was no suggestion that the interests would not have been property if the other interests had not existed. Therefore, *Walker v Walker* supports a discretionary interest being property.

The Supreme Court has also made comments that suggest the discretionary interest may be economically significant. In *Kain v Hutton* a discretionary beneficiary was also a trustee and had a power to replace the trustees. The Court said that this position ensured, "if she wished it, that the shares would revert to her".[403] The shares held on trust could only have reverted to her by being appointed to her as a discretionary beneficiary. Thus the comment by the Court suggests that this interest is economically significant.

Three other cases directly support the conclusion that the discretionary interest is economically significant. In these decisions the court accepted that the discretionary beneficiary's position was economically advantageous and, therefore, relevant to the exercise of a judicial discretion.

In *Flathaug v Weaver*[404] the Court of Appeal considered a discretion, under the Family Protection Act 1955, to order compensation be paid to a daughter out of a deceased's estate. In deciding the amount of the compensation the Court needed to assess how much the deceased had provided his two sons. The deceased had also left a discretionary trust of which the only beneficiaries were his two sons and their children. The sons argued that provision made under the trust should not be taken into account because they were only discretionary beneficiaries. The Court decided that because the sons and their children were the only beneficiaries, the provision through the trust could be regarded as equivalent to a direct gift to

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[399] *Walker v Walker* [2007] NZCA 30, [2007] NZFLR 772. See also *Harrison v Harrison* [2009] NZCA 68, [2009] NZFLR 687 at [10]; *R v R* [2010] NZFLR 555 (FC) at [10], [61(d)]; *JR v LR (A Bankrupt)* [2011] NZFLR 797 (FC) at [59(xviii)], [59(xv)], [60].

[400] *Walker v Walker* [2007] NZCA 30, [2007] NZFLR 772 at [48].

[401] *Walker v Walker* [2007] NZCA 30, [2007] NZFLR 772 at [49].

[402] *Walker v Walker* [2007] NZCA 30, [2007] NZFLR 772 at [49].

[403] *Kain v Hutton* [2008] NZSC 61, [2008] 3 NZLR 589 at [22].

[404] *Flathaug v Weaver* [2003] NZFLR 730, 22 FRNZ 1035 (CA).

the sons under the will.[405] Considering that one of the sons was in a dire financial situation,[406] regarding the discretionary interest as equivalent to a direct gift must be recognition of its economic value.

In *Matarangi Beach Estates Ltd v Dawson*[407] a vendor applied for specific performance of a contract of sale and purchase. An order for specific performance is discretionary and will not be ordered where there "is no substantial likelihood" that the order will be complied with.[408] The defendants submitted that the order should not be made because they did not have the financial means to comply. However, the defendants were discretionary[409] beneficiaries of a family trust that owned a house. The Court decided that it was unlikely the trustee would disagree to any request from the beneficiaries and that they would, therefore, be able to comply with the order if given time to do so.[410] Again, this is recognition of the economically advantageous position of the beneficiary.

The third case, *Dobbie v Cristal Air Ltd*,[411] concerns the discretion under the High Court Rules to require payment of security for costs. If there is a serious risk that a plaintiff will not be able to pay costs, in the event he is unsuccessful, then the Court can require security. Dobbie had no significant assets in his own name but was the discretionary beneficiary of an asset protection trust holding a family home. The Judge accepted that Dobbie did not appear to be able to pay the costs without support from the trust but, nevertheless, did not consider there was a significant risk to the defendants. The Judge had confidence that the trustee would not let Dobbie go bankrupt[412] and he had proved himself able to find money when necessary in an earlier similar case.[413]

These three cases show that the courts accept that the position of discretionary beneficiary can be of significant economic advantage. This concludes the argument that at least some discretionary beneficiaries are in an economically significant position.

Any beneficiary that has "more than a theoretical possibility of benefit"[414] from the trust has an economically significant interest. In my opinion, Parliament is likely to have intended any legal interest that has been acquired by an individual, and "which some persons have got

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[405] *Flathaug v Weaver* [2003] NZFLR 730, 22 FRNZ 1035 (CA) at [36].

[406] *Flathaug v Weaver* [2003] NZFLR 730, 22 FRNZ 1035 (CA) at [35].

[407] *Matarangi Beach Estates Ltd v Dawson* (2008) 6 NZ ConvC 194,667 (HC).

[408] *Matarangi Beach Estates Ltd v Dawson* (2008) 6 NZ ConvC 194,667 (HC) at [7].

[409] This is implicit in the judgment. If they were not discretionary then there could be no argument that specific performance should not be ordered.

[410] *Matarangi Beach Estates Ltd v Dawson* (2008) 6 NZ ConvC 194,667 (HC) at [17].

[411] *Dobbie v Cristal Air Ltd* HC Auckland CIV-2010-404-7192, 10 June 2011.

[412] *Dobbie v Cristal Air Ltd* HC Auckland CIV-2010-404-7192, 10 June 2011 at [13].

[413] *Dobbie v Cristal Air Ltd* HC Auckland CIV-2010-404-7192, 10 June 2011 at [11].

[414] *Schmidt v Rosewood Trust Ltd* [2003] UKPC 26, [2003] 2 AC 70 at [67].

and others have not got",[415] to be included as property. Therefore, a discretionary interest is both legally and economically significant enough to meet the general threshold of an interest that is property.

III. Does a Discretionary Interest Meet the Requirements of the Statutory Schemes?

The third threshold requirement for an interest to be property is that it must meet the requirements of the statutory scheme. That is, the interest must be capable of being dealt with as property is required to be dealt with under the statute. Here differences appear between the statutes in relation to transferability.

Transferability in relation to discretionary interests is not straightforward. For a discretionary interest to be transferable the trustee must be authorised to exercise the power in favour of the transferee. The basic rule on the exercise of powers is that the "donee"[416] of the power is only authorised to exercise it in favour of the objects nominated by the settlor; the exercise may not exceed the granted authority.[417] However, the settlor may authorise payments to be made to a non-object if that is for the benefit of an object.[418] One aspect of the basic rule is that the donee may only exercise the power in favour of a nominated object if it is in accordance with the purpose of the power. For example, a trustee cannot exercise the power to benefit an object with an ulterior motive of benefiting someone other than the object. Such an exercise is called a fraud on the power although fraud in this context only means an improper purpose not dishonesty.[419] Any argument that the discretionary interest is transferable has to deal with these rules because a discretionary interest will only be assignable if the trustee is authorised to benefit the assignee.

A. The High Court Rules - Can a Discretionary Interest Be Assigned?

In Chapter Two it was argued that an interest can only be property under the High Court Rules if it could have been assigned or charged by the owner. There is a potential argument that a discretionary interest could be charged under the principle in *Don King Productions Inc v Warren*.[420] Charging the discretionary interest depends on how far the New Zealand courts follow that case. At present this is speculative and no conclusion is reached.

In terms of assignability, the prevailing understanding is that the interest is not assignable;[421] traditionally this is because was considered to be a mere expectancy,[422]

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[415] *Starey v Graham* [1899] 1 QB 405 (DivC) at 411.

[416] Donee means the person who holds a legal right which operates as a power. See Chapter Four for more details on the nature of powers.

[417] Geraint Thomas *Thomas on Powers* (Sweet & Maxwell, London, 1998) at [8-11].

[418] *Kain v Hutton* [2008] NZSC 61, [2008] 3 NZLR 589 at [20].

[419] Geraint Thomas *Thomas on Powers* (Sweet & Maxwell, London, 1998) at Chapter Nine.

[420] *Don King Productions Inc v Warren* [2000] Ch 291 (CA). See Chapter Two of this thesis.

[421] See *Schmidt v Rosewood Trust Ltd* [2003] UKPC 26, [2003] 2 AC 70 at [40].

although this reasoning can no longer be supported.[423] The interest can be subject to an agreement to assign for consideration,[424] but this assignment cannot substitute the discretionary beneficiary for the assignee:[425]

> The payment of money consideration cannot make a stranger become the object of a power created in favour of children. He can only claim under a valid appointment executed in favour of some, or one, of the children.

This principle is illustrated by *Re Coleman*[426] and *Public Trustee v Ferguson*.[427] Both cases involved a discretionary beneficiary who assigned their discretionary interest.[428] In *Re Coleman* the Court accepted that any property distributed to the assignor beneficiary would automatically pass under the assignment, however, it suggested in obiter that the trustees could continue to benefit the beneficiary in ways that did not pass property to him. For example, they could pay for him to receive meals at an inn. In *Public Trustee v Ferguson* Fleming J commented that the trustee would be justified in choosing not to pay income to the assignor beneficiary if he knew that it would pass to that beneficiary's assignee and so defeat the settlor's wishes about who would benefit.[429]

The authority of these cases is based on the principle that the trustee is not authorised to exercise a power in favour of an assignee. However, their authority is subject to some reservations.

The High Court of Australia has held a discretionary interest is assignable if the trust deed specifically provides for that to occur. The High Court also suggested in obiter that a discretionary interest might have been assignable even if the settlor had not been specific, because it was more than a mere expectancy.[430]

This can be reconciled with the above cases by a principle that assignability depends on the settlor's intention. Where the settlor intended the discretionary interest to be assignable then the trustee is authorised to exercise the power in favour of assignees. However, if this principle is adopted it leaves open the possibility that a settlor could be inferred to have

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[422] See Maurice C Cullity "Fiduciary Powers" (1976) 54 Can Bar Rev 229 at 283-284

[423] See section I(A)(ii) of this Chapter of this thesis.

[424] See *Re Lind* [1915] 2 Ch 345 (CA) at 360, 364, 365-366, 373-374; *Williams v Commissioner of Inland Revenue* [1965] NZLR 395 (CA) at 399; *Johnstone v Commissioner of Inland Revenue* [1966] NZLR 833 (SC) at 838; *Kelly v Commissioner of Inland Revenue* [1970] NZLR 161 (SC) at 163; *Hadlee v Commissioner of Inland Revenue* [1991] 3 NZLR 517 (CA) at 527-529.

[425] *Daubeny v Cockburn* (1816) 1 Mer 626 at 638, 31 ER 801 (Rolls).

[426] *Re Coleman* (1888) 39 Ch D 443 (CA).

[427] *Public Trustee v Ferguson* [1947] NZLR 746 (SC).

[428] In *Re Coleman* the eldest son of the settlor assigned his interest to a stranger and in *Public Trustee v Ferguson* a daughter assigned her interest to her father the settlor.

[429] *Public Trustee v Ferguson* [1947] NZLR 746 (SC) at 752.

[430] *Cridland v Federal Commissioner of Taxation* [1977] HCA 61, 140 CLR 330 at [23].

intended assignability without being explicit. This could lead to the blanket prohibition on exercising a power in favour of assignees being eroded.

Another reservation is that a discretionary beneficiary may alter the terms of a trustee's power by releasing her interest. In *Re Gulbenkian's Settlement Trusts (No 2)*[431] it was held that release of the interest meant the trustee was no longer competent to grant any benefit to that discretionary beneficiary either directly or indirectly. The discretionary beneficiary's actions altered the terms of the trust.

This is difficult to reconcile with the principle that the trustee remains authorised to exercise the power in favour of the settlor's chosen objects. It allows the discretionary beneficiary to interfere with the scope of the trustee's power contrary to the settlor's expressed intention. If the beneficiary can alter the terms of the trustee's authority by reducing the scope of the trustee's power, then it is conceptually possible for her to alter those terms by substituting one object of the power (herself) for another (the assignee). This step has not yet been taken although it was suggested in obiter by the High Court of Australia.[432]

A third factor is that, if the beneficiaries act collectively, they can assign the entire beneficial interest in the trust property to one person. If they do this then the settlor's intention and the discretionary powers given to the trustee are defeated. The individual assignee can then call for the transfer of the trust property.[433]

This factor can be reconciled with the approach to powers found in *Re Coleman*. The beneficiaries' collective right to end the trust is derived from the principle that the trust is gift of the entire beneficial interest in the trust property to the beneficiaries collectively. Therefore, if the beneficiaries all act together they can end the trusts imposed on that property because they have the overall beneficial ownership. This principle comes from the principle that if the settlor gives a recognised property interest he cannot place fetters on that interest.[434] It does not require the individual discretionary interest to be transferable.

In my opinion, the assignability of discretionary interests depends on whether that accords with the settlor's intentions. If the settlor intended discretionary beneficiaries to be able to assign their interests then she intended the trustees to be authorised to make distributions to the assignees and the assignees will have the right to be considered by the trustees. This intention will have to be inferred from the context of the trust and other objective indicators.

One factor that will have considerable importance is the existence of a power to add new discretionary beneficiaries or remove existing discretionary beneficiaries. If the settlor

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[431] *Re Gulbenkian's Settlement Trusts (No 2)* [1970] Ch 408 (Ch).

[432] *Cridland v Federal Commissioner of Taxation* [1977] HCA 61, 140 CLR 330 at [23].

[433] *Re Nelson* [1928] Ch 920n (CA); *Re Smith* [1928] Ch 915 (Ch).

[434] *Younghusband v Gisborne* (1844) 1 Coll 400, 63 ER 473 (Ch).

has designated a particular person to decide who the eligible objects of the power are at any one time there is a strong inference that he did not intend the objects to be able to assign their interests.

In conclusion, it is accepted that in many if not most cases discretionary interests will not be assignable in a manner that authorises the trustees to distribute to the assignee.[435]

B. The Insolvency Act 2006 - Can a Discretionary Interest Pass on Bankruptcy?

The conclusion in Chapter Two was that the Official Assignee takes every interest of the bankrupt that is economically significant whether it is assignable or not. Heath and Whale state that this includes discretionary interests and that "the Official Assignee can assert the beneficiary's rights to have information about the trust, and to be considered for a distribution."[436]

It could be argued that the Official Assignee is outside the objects of the power and so the trustee is not authorised to make distributions to it. However, in principle the Official Assignee is in the same position as the bankrupt: it "stands in the shoes" of the bankrupt.[437] Therefore, the Official Assignee will not be a stranger to the power but is within the authorised objects of the power because it is identified with the bankrupt.

Alternatively, it could be argued that making distributions to a beneficiary after he is bankrupt would be a fraud on the power because it would not benefit the beneficiary. However, a distribution to the Official Assignee technically does benefit the bankrupt because it satisfies his obligations; the fact that those obligations might be terminated on discharge is, in my opinion, irrelevant. Practically, it will be of material benefit to the beneficiary's reputation for his creditors to be paid, even if only in part. Therefore, there should be no challenge that a distribution to the Official Assignee would be wrong in law.

Therefore, in principle the discretionary interest should pass to the Official Assignee and the trustee will be authorised to make distributions directly to the Official Assignee.

C. Estates – Can a Discretionary Interest Pass to the Administrators?

It was argued in Chapter Two that all of a person's economically significant interests should pass to their estate in the same way they pass to the Official Assignee, unless there was a good reason for their termination on death. This was so that their economically valuable interests would not disappear but benefit those surviving the deceased. With a discretionary interest this concern is reduced because there will be other discretionary or default beneficiaries who will benefit if the deceased's interest ends. Therefore, it is not a particularly strong reason for including the discretionary interest in the estate.

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[435] See *Schmidt v Rosewood Trust Ltd* [2003] UKPC 26, [2003] 2 AC 70 at [40].

[436] Paul Heath and Michael Whale *Heath and Whale on Insolvency* (online looseleaf ed, LexisNexis, New Zealand) at [4.21].

[437] *Official Assignee v Wilson* [2007] NZCA 122, [2008] 3 NZLR 45 at [19], [105].

There is also a line of 18th and 19th century cases that have held that a power cannot be exercised in favour of the personal representatives of the beneficiary. This is based on the principle that if the settlor had intended to benefit the discretionary beneficiary's heirs or children he could have included the representatives as objects of the power. As far as I am aware these cases have not been challenged.[438] Therefore, it is accepted that it is unlikely that discretionary interests will pass to administrators and form part of the deceased beneficiary's estate.

D. The Property (Relationships) Act 1976

Under the Property (Relationships) Act 1976 the issues around whether a power is authorised to be exercised in favour of a transferee do not arise because the discretionary interest does not need to be transferred. The interest can be included as property at the stage the court determines the size and classification of the pool of property subject to the Act. Its value can then be taken into account in determining how the property will be divided but the interest itself will not need to be transferred from the beneficiary who holds it. Therefore, the issue is its valuation.

Including the discretionary interest as property fits with Australian and Canadian family law. In Australia, a majority in the High Court in *Kennon v Spry* held the husband's power as trustee to appoint property to the wife and the wife's discretionary interest were "the property of the parties to the marriage" under s 79 of the Family Law Act 1975 (Cth).[439]

The majority decided that the husband's power as trustee to appoint the wife was property.[440] This was decided on the basis of the specific words: "property of the parties to the marriage".[441] The Court held that these words allowed them to include the husband's trustee power as property when it was combined with the wife's discretionary interest.[442] Essentially they decided that, as the couple had the power to take all of the property for themselves, the combined interest was their collective property. This aspect of the Court's judgment cannot apply in New Zealand because our Act does not refer to "property of the parties" and specifically excludes the husband's powers as trustee from being property.[443]

The Court also held that the wife's discretionary interest by itself was property for the purposes of the Australian Act. This finding was founded on the broad interpretation of "property", which is comparable to the meaning in the New Zealand statute.[444] The Court held

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[438] *Maddison v Andrew* (1747) 1 Ves Sen 57 at 59, 27 ER 889 (Ch); *Boyle v Bishop of Peterborough* (1791) 1 Ves Jun 299 at 305, 310, 30 ER 353 (Ch); *Butcher v Butcher* (1812) 1 V & B 79 at 91-92, 35 ER 31 (Ch).

[439] *Kennon v Spry* [2008] HCA 56, 238 CLR 366 at [74]-[80], [126], contrast Heydon J dissenting at [154].

[440] *Kennon v Spry* [2008] HCA 56, 238 CLR 366 at [62], [126].

[441] Family Law Act 1975 (Cth), s 79.

[442] *Kennon v Spry* [2008] HCA 56, 238 CLR 366 at [54], [126].

[443] Property (Relationships) Act 1976, s 2 [definition of "owner"].

[444] *Kennon v Spry* [2008] HCA 56, 238 CLR 366 at [54], [91], [126].

that wife's right to due administration was property and not merely a "financial resource".[445] In this respect it departed from a previous line of cases that had held that contingent beneficial interests under superannuation trusts were not property but financial resources.[446] French CJ was concerned that the discretionary interest may be difficult to value, as the possibility of benefiting might never be realised, but accepted that valuation might be possible.[447] This difficulty exists with any possibility and is not endemic to a discretionary interest.

In Canada, courts in Ontario and Alberta have accepted that a discretionary interest is property.[448] The cases in Canada accept that discretionary interests can be property as they are a type of contingent interest, albeit the contingency is the exercise of a discretion. In Ontario this means that the courts have decided the discretionary interest falls within the meaning of "any interest, present or future, vested or contingent, in real or personal property".[449] This is a narrower definition than found in the New Zealand Act as it only includes interests *in* property.[450] These cases have also valued the interest as will be discussed in the final Chapter.[451]

IV. Conclusion

There are three thresholds a discretionary interest must meet before qualifying as property under any of the selected statutes. It must be recognised as legally significant. It must be recognised as economically significant in at least some instances. Finally, it must be capable of being dealt with under the statutory scheme.

In my opinion, the discretionary interest meets these thresholds under two of the selected statutes. The fact that the discretionary beneficiary has the present right to due administration of the trust proves that it is a legally significant interest. The fact that many discretionary beneficiaries are likely to receive significant economic benefits from trusts establishes that the interest is economically significant. The fact that the Official Assignee is identified with the bankrupt means that it will be able to benefit under the interest and enforce due administration of the trust under the Insolvency Act 2006. The fact that the interest does not need to be transferred for it to be justiciable under the Property (Relationships) Act 1976 means it can be valued as part of a separating couples property. However, the fact that the

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[445] The Family Court of Australia is authorised to take "financial resources" into account when making orders in relation to "property" under s 79 (see s 79(4)) but is not authorised to make orders in relation to the financial resources themselves (see *Kennon v Spry* [2008] HCA 56, 238 CLR 366 at [89]).

[446] See *In the Marriage of Stay* (1997) 138 FLR 343 (FC) at 355.

[447] *Kennon v Spry* [2008] HCA 56, 238 CLR 366 at [77]-[78].

[448] *Sagl v Sagl* (1997) 31 RFL (4th) 405 (Ontario General Division), 1997 CanLII 12248 (ON SC); *Kachur v Kachur* 2000 ABQB 709.

[449] Family Law Act RSO 1990 c F-3, s 4(1).

[450] See Lorne H Wolfson and Ikka Delamer "The Valuation of Trusts Under the Family Law Act" (2002) 20 CFLQ 97.

[451] Valuation of discretionary interests is Canada is not yet a settled issue (*Spiring v Spiring* 2004 MBQB 55 at [18]).

trustee's power cannot be exercised in favour of assignees or personal representatives means it is unlikely to be property under the High Court Rules, Family Protection Act 1955 or Law Reform (Testamentary Promises) Act 1949.

CHAPTER FOUR: THE THRESHOLD TO PROPERTY – RIGHTS TO REPLACE TRUSTEES

The previous chapter analysed whether a discretionary interest is property. This chapter moves on to the other part of the controlling beneficiary's interest: the right to replace trustees. The question here is whether this right meets the threshold requirements to be property. That is, is it legally significant, economically significant and capable of being dealt with under the statutory schemes?

The terminology "right to replace trustees" is likely to be contentious but has deliberately been used instead of the more usual "power to appoint and remove trustees". This is done for two reasons: first, to avoid confusing the right to replace trustees with a trustee's power to appoint property to beneficiaries and, second, because referring to it as a power implies it is not within the usual broad meaning of "right".

This issue is confronted as part of the first section on legal significance. The first issue is whether a Hohfeldian[452] power is a type of legal interest that can be property. It has been suggested it cannot be property.[453] This is suggested because a power is a right to make a choice that will affect others and can be distinguished from the narrow definition of a "right" as being a "legally enforceable claim that another will do or will not do a given act".[454] However, an equally common meaning of "right" includes all "individual advantages secured by law"[455] or any "power, privilege, or immunity secured to a person by law".[456] This broader understanding of a right justifies calling the power to appoint and remove trustees a "right" and is supported by many cases that have held a power is property. Although Hohfeldian language can increase clarity in the law by improving precision it can also obscure similarities between interests. For convenience the holder of this right will continue to be called a "donee", which is the term used for the holder of a power.

It is the economic significance of this right that is most contentious. This is due to the possibility that the right is fiduciary. If the right is subject to fiduciary duties it can have no economic significance because it cannot be used for the holder's own benefit. The question of when fiduciary duties arise will be investigated in section II and the results applied to the right to replace trustees. It is accepted that this right may be fiduciary but I argue it will be unlikely when it is held by a discretionary beneficiary.

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[452] A power is one of Hohfeld's legal incidents in his famous categorisation; see below (WN Hohfeld "Some Fundamental Legal Conceptions as Applied in Judicial Reasoning" (1913) 23 Yale LJ 16 at 30-32).

[453] See *Kennon v Spry* [2008] HCA 56, 238 CLR 366 at [176] [per Heydon J in dissent]; Anthony Grant "The Bundle of Rights Doctrine: What is the Law?" (paper presented to ADLS Conference: Cradle to Grave, 22 March 2010) at [42]-[48].

[454] Bryan A Garner (ed) *Black's Law Dictionary* (9th ed, online ed, Thomson Reuters, 2009) "right *n* 4".

[455] Stephen R Munzer *A Theory of Property* (Cambridge University Press, Cambridge, 1990) at 20.

[456] Bryan A Garner (ed) *Black's Law Dictionary* (9th ed, online ed, Thomson Reuters, 2009) "right *n* 3".

There is a second issue regarding economic significance and fiduciary duties. This arises from the fact that any replacement trustee appointed under the right will have fiduciary duties to all the beneficiaries, not just the beneficiary that appointed him. There may be a problem with recognising the economic value of a right to appoint a person to a fiduciary position. The problem is that recognising this economic value could be seen as tantamount to sanctioning a breach of duty by the appointed trustee. This issue is explored in section III. It is argued, by analogy with a majority shareholder's power to appoint a fiduciary director, that this will not prevent the economic significance of the right being recognised.

The final section will return to the selected statutes to ascertain whether the power is capable of being dealt with under statutory schemes.

I. Can a Hohfeldian Power be Property?

The first issue is whether a power is a type of legal relationship that can be property. The issue is technical and arises from *Re Armstrong*[457] where Fry LJ stated that powers and property are fundamentally incompatible concepts. This issue requires the dissection of the nature of legal interests.

According to Hohfeld's categorisation of legal interests there are four pairs of correlating legal incidents: claim-rights and duties; powers and liabilities; privileges and no-rights; and immunities and disabilities.[458] Hohfeld's claim-right is a claim against a person to the effect that that person has a duty to do or not do a specific action.[459] The claim-right and the duty are correlative. The term 'right' is sometimes used to refer to a Hohfeldian claim-right and sometimes used in the broader sense of "individual advantages secured by law",[460] which includes powers, privileges and immunities as well. In this thesis "right" is used in the wider sense and "claim-right" for the narrow Hohfeldian meaning.

In contrast with a claim-right a power is the right to change other people's legal relations at one's own volition. It is correlated with other people being under a liability to have their legal relations unilaterally changed.[461] How powers work is illustrated by the right to replace the trustee. With this power there is no relationship of duty or claim-right between the trustee and the donee. If the power is exercised, then the legal position of the trustee will be altered, because the trustee is under a liability correlative to the donee's power. If the right to replace is exercised the trustee will no longer be authorised to exercise the powers of a trustee in relation to the property he owns. Further he is subject to a new liability to pass the

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[457] *Re Armstrong* (1886) 17 QBD 521 (CA).

[458] WN Hohfeld "Some Fundamental Legal Conceptions as Applied in Judicial Reasoning" (1913) 23 Yale LJ 16 at 30-32.

[459] This is also the statutory definition of a "debt" that is assignable under the Property Law Act 2007, ss 48-53.

[460] Stephen R Munzer *A Theory of Property* (Cambridge University Press, Cambridge, 1990) at 20.

[461] WN Hohfeld "Some Fundamental Legal Conceptions as Applied in Judicial Reasoning" (1913) 23 Yale LJ 16 at 44.

trust property to any newly appointed trustee. The exercise of the right to replace creates a second power in the replacement trustee to demand transfer of the trust property. The exercise of this new power imposes a duty on the removed trustee to transfer the trust property. Another familiar example of a Hohfeldian power is an option to purchase. An option to purchase is a power to create a sale and purchase agreement. In this example, the exercise of the power directly creates duties and claim-rights between the vendor and purchaser. Until the power is exercised they do not exist.

The source of the idea that a power cannot be property is *Re Armstrong*.[462] It will be argued that this case is no longer good law. It will also be argued that even if *Re Armstrong* was good law in relation to powers of appointment over property, its authority never extended to powers generally.

A. The Source of the Argument and its Rebuttal

The unanimous result in *Re Armstrong* was that a general power of appointment, over property held by trustees, was not property that passed on bankruptcy. If the case had been under the usual bankruptcy statute the general power would have been specifically included,[463] but because it was decided under the Married Women's Property Act 1882,[464] which did not specifically include powers, the case was decided on the meaning of property as used "in law" and "in equity".[465]

The case is significant because a general power of appointment is a power to direct the trustees to hold property for whomever the donee chooses. Therefore, the donee could exercise the power and take all the trust property for herself or direct that it be given to anyone as she saw fit. It can be compared to a discretionary interest because it is a possibility of receiving property in the future; the difference is that it is subject to the donee's own choice not the trustee's. In terms of economic value there is little difference between the power over property and the ownership of the property subject to it.

Fry LJ decided there was a fundamental distinction between powers and property by comparing powers of appointment and powers to create intellectual property: [466]

> 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 to 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."

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[462] *Re Armstrong* (1886) 17 QBD 521 (CA).

[463] Bankruptcy Act 1883 (UK), s 44.

[464] Married Women's Property Act 1882 (UK) 45 & 46 Vict c 75.

[465] *Re Armstrong* (1886) 17 QBD 521 (CA) at 531.

[466] *Re Armstrong* (1886) 17 QBD 521 (CA) at 531.

This explains the distinction as fundamentally about the nature of powers. However, the reasoning applied by Fry LJ does not justify such a general distinction. In my opinion, his counterfactual using powers to create intellectual property is inappropriate.

I agree that a power to create intellectual property is not property; however, this is not for the reason given by Fry LJ but because it is a right that everyone has equally. All individuals in a legal system have a power to create intellectual property rights by patenting ideas and copyrighting expressions. A right that is held by everyone allows no difference between individuals and, therefore, cannot "constitute the mundane coin of capitalism".[467] As Smith has said, "[i]n a capitalist system, not everyone has the same set of rights. The ones that everyone has are the general law. The ones that not everyone has are what we mean by assets."[468]

In this respect, the power to create intellectual property is comparable to the privilege to trade in a particular area of business, which everyone has in a free market economy. It is economically significant in a broad sense but because everyone has the same privilege it is not usually property.[469] However, the privilege can be included as property if it is connected to identifiable goodwill that has been built up by an individual during a period of trading. Where goodwill in a business's reputation and branding has been built up in a particular area it can be sold by releasing the privilege to trade in that area.[470] The same relationship between general rights and individual rights can be seen in relation to powers. A power held by everyone is not property but a general power of appointment that is held by only one person can be property.

Even before *Re Armstrong* a general power of appointment was treated like property in some circumstances because Chancery would allow the property subject to the general power to be taken by creditors. In *Holmes v Coghill*[471] the Court agreed that if a debtor did not exercise the power then his creditors could not take the property. The reason given was that the debtor with the power, "though bound to pay his creditors, could not be called upon by law to pay them out of an estate, which is the property of another person."[472] This reasoning relied on the principle that default beneficiaries own the trust property.

However, if the donee was a debtor and exercised the power but the exercise was invalid the Court held that the defect could be remedied and the default beneficiary's interest

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[467] Lionel Smith *The Law of Tracing* (Clarendon Press, Oxford, 1997) at 53. See also WN Hohfeld "Fundamental Legal Conceptions as Applied in Judicial Reasoning" (1917) 26 Yale LJ 710 at 718 n 20; *Starey v Graham* [1899] 1 QB 405 (DivC) at 411.

[468] Lionel Smith *The Law of Tracing* (Clarendon Press, Oxford, 1997) at 53.

[469] *Kirby (Inspector of Taxes) v Thorn EMI plc* [1988] 1 WLR 445 (CA) at 452E-F.

[470] *Kirby (Inspector of Taxes) v Thorn EMI plc* [1988] 1 WLR 445 (CA) at 452-456, 459-460; *Z v Z* [1989] 3 NZLR 413 (CA) at 415.

[471] *Holmes v Coghill* (1806) 12 Ves Jun 206, 33 ER 79 (Ch).

[472] *Holmes v Coghill* (1806) 12 Ves Jun 206 at 213, 33 ER 79 (Ch).

overborne. Likewise, if the debtor exercised the power in favour of a stranger equity would interfere and divert the appointed property to creditors.[473] The Court in *Holmes v Coghill* acknowledged that interfering with the power in these circumstances but not interfering when there was no attempt to exercise it was difficult to justify, but accepted it as a matter of authority.[474] This shows that even before *Re Armstrong* equity recognised the property-like characteristics of the general power of appointment.[475]

The principle that an unexercised general power is different from property has been applied inconsistently. Before *Re Armstrong* a general power of appointment was considered to be equivalent to property in some circumstances[476] but was not considered to be property that passed to personal representatives on death.[477] After *Re Armstrong*, one line of cases followed it,[478] but another line of cases, which includes the preponderance of cases in the House of Lords, has held that a general power of appointment is equivalent to property.[479] As

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[473] *Holmes v Coghill* (1806) 12 Ves Jun 206 at 213, 33 ER 79 (Ch).

[474] *Holmes v Coghill* (1806) 12 Ves Jun 206 at 216, 33 ER 79 (Ch).

[475] See also *O'Grady v Wilmot* [1916] 2 AC 231 (HL) at 248, 270; *Re Van Hagan* (1880) 16 Ch D 18 (CA) at 32, 33. On the other hand, *Re Mathieson* [1927] 1 Ch 283 (CA) ignored the principle in *Holmes v Coghill* in the context of dispositions of property prior to bankrtupcy and held that exercise of a general power of appointment was not disposing of property. This contradicts the principle in *Holmes v Coghill* and *O'Grady v Wilmot* that equity should intervene of behalf of creditors where property has appointed to volunteers. *Re Mathieson* was regarded as a "remarkable decision" in *Clarkson v Clarkson* [1994] EWCA Civ 25, [1994] BCC 921 (CA) at 931A-B.

[476] In *Englefield's Case* (1590) 4 Leonard 135, 74 ER 779, resumed at 169, 779 (Ex) a general power of appointment was forfeited to the king; however, the opposite decision was reached in *Smith v Wheeler* (1671) 1 Ventris 128, 86 ER 88 (KB) on the basis that a power of revocation was personal to the donee and could not be transferred. In *Standen v Standen* (1795) 2 Ves Jun 589, 30 ER 791 (Ch) a testatrix disposing of her property was interpreted to include the power "which is as absolutely hers as any other part of her property." In *Barford v Street* (1809) 16 Ves Jun 134, 33 ER 935 (Rolls) a general power of appointment coupled with a life interest was considered equivalent to the entire beneficial interest. The leading text on powers in the early 19th century stated that a general power was tantamount to property because it gave the donee an absolute disposing power over the property and he could "bring it into the market whenever his necessities or wishes may lead him to do so" (Edward Burtenshaw Sugden [Lord St Leonards] *A Practical Treatise of Powers* (8th ed, H Sweet, London, 1861) at 394).

[477] *Drake v Attorney-General* (1843) 10 Clark & Finnelly 257, 8 ER 739 (HL); *Commissioner of Stamp Duties v Stephen* [1904] AC 137 (PC) at 140–141; *O'Grady v Wilmot* [1916] 2 AC 231 (HL) at 248, 270.

[478] *Tremayne v Rashleigh* [1908] 1 Ch 681 (Ch) at 688; *Re Mathieson* [1937] 1 Ch 283 (CA); *Re Kensington (Deceased)* [1949] NZLR 382 (CA) at 390, 393, 396; *Morgan v Inland Revenue Commissioners* [1963] Ch 438 (CA) at 452, 455, 458 [per Upjohn and Diplock LJJ, Lord Denning MR dissenting]; *Re Silk (deceased)* [1976] VR 60 (SC) at 63-64 [affirmed on the different ground that a general power over property meant that the donee was "competent to dispose" of that property in *Equity Trustees Executors & Agency Co Ltd v Commissioner of Probate Duties* [1976] HCA 34, 135 CLR 268]; *Re Burton* [1994] FCA 1146, 126 ALR 557 at 559-560; *Z v Z (No 2)* [1997] 2 NZLR 258 (CA) at 278 [obiter]; *Kennon v Spry* [2008] HCA 56, 238 CLR 366 at [176] [per Heydon J in dissent]; *Public Trustee v Smith* [2008] NSWSC 397 at [108].

[479] *Charlton v Attorney-General* (1879) 4 App Cas 427 (HL) at 439, 446; *Re Van Hagan* (1880) 16 Ch D 18 (CA) at 32, 33; *Re Byron's Settlement* [1891] 3 Ch 474 (Ch) at 479; *Re Park* [1932] 1 Ch 580 (Ch) at 584; *Grey v Federal Commissioner of Taxation* [1939] HCA 14, 62 CLR 49 at 63; *Muir or Williams v Muir* [1943] AC 468 (HL) at 483; *Tatham v Huxtable* [1950] HCA 56, 81 CLR 639 at 647, 654; *Re Churston Settled Estates* [1954] Ch 334 (Ch) at 344; *Re Triffitt's Settlement* [1958] Ch 852 (Ch) at 861; *Re Beatty (dec'd)* [1990] 1 WLR 1503 (Ch) at 1506; *Clarkson v Clarkson* [1994] EWCA Civ 25, [1994] BCC 921 (CA) at 931A-B; *Melville v Inland Revenue Commissioners* [2001] EWCA Civ 1247, [2002] 1 WLR 407 at [21], [30], [39].

property has more than one meaning deciding something is equivalent to property is a decision that it is property in that context.[480]

The issue has finally been settled against *Re Armstrong* by a recent case in the Privy Council.[481] The Privy Council was deciding whether a settlor's power to revoke a trust was property that could be transferred to a receiver on behalf of creditors. A power to revoke a trust differs from a general power of appointment in that the donee can only divert the property to the settlor rather than to anyone in the world. However, when the settlor is the donee it is practically the same as a general power.[482]

The Privy Council concluded that the power to revoke was property that could be transferred to the receiver. It overruled *Re Armstrong* and held there was no general rule distinguishing between a power and property and that the ordinary meaning of property could include powers.[483] The manner in which the power was transferred was by delegation.[484] The Council made one reservation, which was that a fiduciary power could not be property.[485] Therefore, the argument that the right to replace trustees cannot be property because it is a Hohfeldian power cannot succeed.

B. Other Instances of Powers Being Property

Apart from powers of appointment there are a number of other types of Holfeldian powers that have been held to be property. One of the most traditional is options. An option is the power to create the relationship of vendor and purchaser. Options are accepted as choses in action[486] and can be assigned.[487] They are accepted as property.

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[480] See *Tasarruf Mevduati Sigorta Fonu v Merrill Lynch Bank and Trust Company (Cayman) Limited* [2011] UKPC 17, [2011] BPIR 1743 at [33].

[481] *Tasarruf Mevduati Sigorta Fonu v Merrill Lynch Bank and Trust Company (Cayman) Limited* [2011] UKPC 17, [2011] BPIR 1743.

[482] A power to revoke will be equivalent to a general power because the property can be transferred to anybody in the world by taking two steps rather than one; the number of steps taken is immaterial. This reasoning was taken in *Re Penrose* [1933] 1 Ch 793 (Ch) at 807 which did not involve a power to revoke but a special power of appointment which was limited to a select group which included the donee of the power.

[483] *Tasarruf Mevduati Sigorta Fonu v Merrill Lynch Bank and Trust Company (Cayman) Limited* [2011] UKPC 17, [2011] BPIR 1743 at [60].

[484] *Tasarruf Mevduati Sigorta Fonu v Merrill Lynch Bank and Trust Company (Cayman) Limited* [2011] UKPC 17, [2011] BPIR 1743 at [61]. The Council considered the argument that if the power was unassignable then the Court would have been precluded from ordering that the power to be exercised in a particular way (this argument was made in reliance on *Thorpe v Goodall* (1811) 17 Ves Jun 388, 460, 34 ER 150 (Ch) at 460) and decided that it was unnecessary to answer; however, the Council did strongly criticise the reasoning of this argument (at [63]).

[485] *Tasarruf Mevduati Sigorta Fonu v Merrill Lynch Bank and Trust Company (Cayman) Limited* [2011] UKPC 17, [2011] BPIR 1743 at [62]; *Re Triffitt's Settlement* [1958] Ch 852 (Ch) at 861.

[486] *Abbott v Philbin* [1961] AC 352 (HL); *Griffith v Pelton* [1958] Ch 205 (CA); *Beesly v Hallwood Estates Ltd* [1960] 1 WLR 549 (Ch); *Re Button's Lease* [1964] Ch 263 (Ch).

[487] *Wright v Morgan* [1926] AC 788 (PC).

Another example was the right to demand interest on a debt in *Re Marshall*.[488] This right was a Hohfeldian power because until the demand for interest was made there was no duty to pay; the duty to pay only came into existence upon the exercise of the power. It was on this basis that North P, in dissent, decided it could not be a debt as "these rights did no more than arm the late Mr Marshall with the power to create choses in action if he saw fit."[489] However, McCarthy and McGregor JJ disagreed. They held that although the right to demand was not a debt it was a valuable chose in action.[490]

In conclusion, in my opinion, the technical argument that a Hohfeldian power is not a type of interest that can be property is wrong. As Lord Atkin once said, the ordinary meaning of property includes "rights and powers of any description."[491] As Cooke J has said when interpreting the term "right" when found in a statute: "The precision of Hohfeld's analysis is not to be expected of Parliament."[492]

II. Is the Right to Replace Trustees Bound by Fiduciary Duties?

If the right to remove trustees is fiduciary then it cannot be property of economic significance.[493] A fiduciary right is not of economic significance because it is a duty to act for and on behalf of another to the exclusion of one's own interest.[494] It is a duty to be loyal to another so that one must put their interests ahead of one's own.[495] A fiduciary right cannot be transferred or released by the donee.[496] For example, the rights held by a trustee are fiduciary and must be used for the benefit of the beneficiaries, not for the benefit of the trustee.[497]

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[488] *Re Marshall (Deceased)* [1965] NZLR 851 (CA).

[489] *Re Marshall (Deceased)* [1965] NZLR 851 (CA) at 856.

[490] *Re Marshall (Deceased)* [1965] NZLR 851 (CA) at 860, 863.

[491] *Nokes v Doncaster Amalgamated Collieries Ltd* [1940] AC 1014 (HL) at 1033.

[492] *Wellington Diocesan Board of Trustees v Wairarapa Market Buildings Ltd* [1974] 2 NZLR 562 (SC) at 571.

[493] *Tasarruf Mevduati Sigorta Fonu v Merrill Lynch Bank and Trust Company (Cayman) Limited* [2011] UKPC 17, [2011] BPIR 1743 at [62].

[494] PD Finn *Fiduciary Obligations* (The Law Book Company Limited, Sydney, 1977) at [6], [15], [19]; Matthew Conaglen *Fiduciary Loyalty: Protecting the Due Performance of Non-Fiduciary Duties* (Hart Publishing, Oxford, 2010) at 260. Conaglen argues that the only truly fiduciary duties are the duties against conflicts and making profits (at 39-40). However, he then argues that fiduciary duties arise when there is a legitimate expectation that the "fiduciary will 'act for and on behalf of' the other party in the relationship—'in the interests' of that party—and will do so to the exclusion of his own interest" (at 260). This suggests that a fiduciary duty is also what the other party can legitimately expect the fiduciary to do. The inference drawn is that the duties against conflict and profits are manifestations of the duty to act on behalf of another to the exclusion of oneself. Thus it is arguable that Conaglen's understanding of the fiduciary duty is similar to Finn's.

[495] *Chirnside v Fay* [2006] NZSC 68, [2007] 1 NZLR 433 at [15].

[496] See *Re Triffitt's Settlement* [1958] Ch 852 (Ch); Geraint Thomas *Thomas on Powers* (Sweet & Maxwell, London, 1998) at [15-03]-[15-04]. Contrast Robin Lance Congreve "The Nature and Extent of Trustees' Powers of Appointment, Selection and Disposition" (PhD Thesis, University of London, 1973) at [2-18].

[497] A trustee's legal interest does not "carry with it the right of the owner to enjoy the fruits of it or dispose of it for his own benefit" (*Ayerst v C & K (Construction) Ltd* [1976] AC 167 (HL) at 177). This is the reason that a trustee's legal interests do not qualify as property in equity. Before the unification of equity and law a trustee's interest could be executed at law by a creditor but the creditor would be bound by the beneficial interest in equity. See *Burgh v Francis* (1670) 1 Eq Ca Abr 320, 21 ER 1074 (Rolls); *Medley v Martin* (1673) Finch 62, 23

Not all rights found in trust deeds are fiduciary. Beneficial rights include general powers of appointment and the power of revocation mentioned above. They are not fiduciary because they can be exercised by the donee in favour of himself. The current question is whether the right to replace trustees is a fiduciary right or a beneficial right.[498]

A. When does a Fiduciary Duty Arise?

Before it can be said whether a fiduciary duty attaches to a right to replace trustees it must be understood when such a duty arises.

In his recent book on the subject of fiduciary duties, Conaglen says there is no easy answer to this question. He says it is a matter of when a party can legitimately expect a duty of loyalty from another.[499] He suggests three relevant considerations: analogies with other relationships where judges have decided such a duty should apply, the value that society places on particular relationships, and the effectiveness of other mechanisms to regulate the parties' relationship.[500] The leading case in New Zealand is *Chirnside v Fay*[501] where the Court decided a joint venture relationship was fiduciary. The reasoning took into consideration previous cases that held joint ventures were fiduciary and comparison with the established fiduciary relationship of partnership,[502] which supports the first of Conaglen's relevant considerations.

However, these three considerations do not give a complete picture because they do not include the settlor's intention, which Conaglen deals with in another chapter. A fiduciary relationship will only be imposed if the person who established the relationship[503] apparently

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ER 33 (Ch); *Finch v Earl of Winchelsea* (1715) 1 P Wms 277, 24 ER 387 (Ch); *Zinck v Walker* (1777) 2 Black W 1154, 98 ER 681 (KB); *Foley v Burnell* (1783) 1 Bro C C 274 at 278, 28 ER 1125 (Ch); *Farr v Newman* (1792) 4 TR 621, 100 ER 1209 (KB); *Taylor v Plumer* (1815) 3 M & S 562, 105 ER 721 (KB); *Re Beattie* (1887) 5 NZLR 342 (SC); *Motor Vehicle Dealers Institute Inc v UDC Finance (1991) Ltd* [1994] 1 NZLR 659 (CA) at 663; *Isolare Investments Ltd v Fetherston* HC Auckland CIV 2002-404-1791, 15 September 2006 at [8]; *R v Williams [Instrument Forfeiture Order]* HC Rotorua CRI-2009-063-5871, 22 July 2011 [property held by a trustee not subject to the Criminal Proceeds (Recovery) Act 2009]; *Gill v Gill* [1995] NZFLR 550, 13 FRNZ 427 (HC) [property held by a trustee not subject to the Property (Relationships) Act 1976].

[498] A beneficial interest can still be subject to duties. Not all duties are fiduciary. An interest subject to non-fiduciary duties can still be exercised for the benefit of the owner. For example, the holder of a mortgage has duties to comply with in exercising her interest but they do not prevent her from using it for her own benefit (Property Law Act 2007, ss 150-151, 155-156, 160-166, 167 and 173).

[499] Matthew Conaglen *Fiduciary Loyalty: Protecting the Due Performance of Non-Fiduciary Duties* (Hart Publishing, Oxford, 2010) at 260.

[500] Matthew Conaglen *Fiduciary Loyalty: Protecting the Due Performance of Non-Fiduciary Duties* (Hart Publishing, Oxford, 2010) at 268.

[501] *Chirnside v Fay* [2006] NZSC 68, [2007] 1 NZLR 433.

[502] *Chirnside v Fay* [2006] NZSC 68, [2007] 1 NZLR 433 at [14].

[503] In relation to trusts, the settlor's intention is the only intention relevant in imposing the fiduciary duties required to found a trust obligation. The trustee's intention is only relevant to the extent that that particular trustee has agreed to be subject to the trust obligation. If the trustee has not agreed then there is still a trust obligation and the courts will act to appoint a replacement so that the obligation can attach to someone. Even Langbein agrees that in regard to the duty to dispose of property to others only the settlor's intention is relevant (John H Langbein "The Contractarian Basis of the Law of Trusts" (1995) 105 Yale LJ 625 at 652). As Palmer has said the debate about the need for mutual intention in the doctrine of sham is not necessarily relevant to the

intended it to be fiduciary.[504] That is, if a person creates a legal relationship but does not intend to impose an obligation of loyalty on either party then no fiduciary duties will be imposed. Alternatively, a settlor may intend to limit the scope of the fiduciary duties so that a fiduciary will be authorised to act for his own benefit to a certain extent. However, in my opinion, authorisation must be limited for fiduciary duties to survive; if the fiduciary is authorised to benefit himself to the complete exclusion of others then he is no longer a fiduciary.[505]

An example of authorisation is a trustee who is authorised to pay herself under a right to remuneration. She has fiduciary duties to the beneficiaries but they are limited by the power to act in her own interests to a limited extent. To the extent that her remuneration is reasonable she can pay herself in priority to, and without considering, the beneficiaries' interests.

An example of authorisation that overrides any potential fiduciary duties is found in *Re Penrose*.[506] Here a power of appointment had been given by the settlor to her husband who was not otherwise a trustee. It was argued that this right was fiduciary because it could only be exercised in favour of the descendants of the husband's father. Such a limited or "special power of appointment" implies that the settlor intended the donee to act in the interests of that that group.[507] However, the argument could not succeed because it was clear that the settlor had authorised the husband to exercise the power in favour of himself – the husband was a descendant of his father. It was concluded that fiduciary duties could not attach to the power

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intention to create trust obligations (Jessica Palmer "Theories of the Trust and What They Might Mean for Beneficiary Rights to Information" [2010] NZ L Rev 541 at 544). In the doctrine of sham the intention which needs to be proved is a dishonest subjective intention. Where the context concerns whether the settlor has intended to impose a fiduciary obligation only the objectively apparent intention must be proven. This means that a trust could simultaneously be proven valid by the settlor's objective intention but proven invalid as a sham by the settlor and trustee's dishonest subjective intentions. See also Nicola Glover and Paul Todd "The Myth of Common Intention" (1996) 16 LS 325.

[504] *Westdeutsche Landesbank Girozentrale v Islington London Borough Council* [1996] AC 669 (HL) at 705D-E per Lord Browne Wilkinson. Authorisation may be express or implied. A common example of implied authorisation is where the settlor puts a trustee in a position where there is a conflict between their duty to the beneficiary and their personal interest (or duty to another beneficiary). The fiduciary is under a duty not to be in such a position of conflict (*Aberdeen Railway Co v Blaikie Bros* (1854) 1 Macq 461, 149 RR 32 (HL)). However, where it is the settlor who knowingly puts the person in such a position of conflict then that particular duty is removed (*Tempest v Lord Camoys* (1888) 58 LT 221 (Ch) at 223; *Hordern v Hordern* [1910] AC 465 (PC) at 475; *Princess Anne of Hesse v Field* [1963] NSWR 998 (SC) at 1009-1010; *Sarris v Clark* [1994] SCLR 927, [1995] SLT 44 (IH (2 Div)) at 46-48; *Jones v Firkin-Flood* [2008] EWHC 2417 (Ch) at [266]-[267]).

[505] See Matthew Conaglen *Fiduciary Loyalty: Protecting the Due Performance of Non-Fiduciary Duties* (Hart Publishing, Oxford, 2010) at 204-205: "The principal may bring an end to the fiduciary relationship completely, thereby releasing the former fiduciary from the strictures of the fiduciary conflict principle, or the principal may alter the fiduciary's non-fiduciary duties in respect of a particular transaction so that, for that specific transaction, there is no longer any conflict between those non-fiduciary duties and the fiduciary's personal interest"; HAJ Ford and William Lee A *Principles of the Law of Trusts* (2nd ed, Law Book Company Limited, Sydney, 1990) at [503].

[506] *Re Penrose* [1933] 1 Ch 793 (Ch).

[507] This type of power is often contrasted with a general power which can be exercised in favour of anyone in the world and, therefore, implies that a fiduciary duty is not owed because it makes no sense to owe a duty of loyalty to the whole world.

because it was clear that the husband was not obliged to exercise the power on behalf of others and to the exclusion of his own interest.[508]

In conclusion, in my opinion, fiduciary duties will be imposed on new types of interests where those interests are similar to established fiduciary interests and there is a legitimate expectation of loyalty. However, they will not be imposed on an interest where that would be contrary to the settlor's intention. The settlor's intention may be explicit but is usually implied from the nature of the interest conferred and the context. Therefore, an interest that is fiduciary in one trust will not necessarily be fiduciary in another trust of the same type; it is context specific.[509]

B. In Principle Does a Fiduciary Duty Attach to a Right to Replace Trustees?

Applying these principles to the right to replace trustees does not provide a clear conclusion. There are arguments either way; it ultimately depends on the facts.

Analogies can be drawn between the donee of this right and other fiduciary positions. The donee of a right to fill vacant trusteeships has traditionally been held to be fiduciary.[510] The difference is that the latter donee cannot remove trustees; he can only replace those that leave due to other causes. A comparison can also be made with trusts that divide the trustee's responsibility between two fiduciaries that are accountable to each other. For example a unit trust has a manager who operates the trust and a trustee who owns the trust fund and has a duty to act as a check upon the manager's actions.[511] It is accepted that the right to replace trustees is reasonably comparable to other rights that are bound by fiduciary duties.

Therefore, the crucial issue is whether the donee of this right is intended by the settlor to be subject to a fiduciary duty in favour of the beneficiaries. This intention can be inferred from the context.

Consider a settlor who keeps the right for himself. He might have intended to keep it so that expensive court procedures could be avoided if a trustee needed to be replaced; however, this is not likely. If this was his true intention he could have retained a right to fill vacant trusteeships, which, by statute, includes the right to replace trustees who can no longer perform their duties.[512] A more likely inference is that he retained it in case his views and the trustee's views diverged in the future. If the trustee's views diverged the trustee could be replaced with someone who was more likely to carry out the settlor's wishes. From these facts alone there is no clear inference on whether the settlor intended to bind himself with fiduciary

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[508] See also *Re Triffitt's Settlement* [1958] Ch 852 (Ch).

[509] See *Montifiore v Guedalla* [1903] 2 Ch 723 (Ch) at 726.

[510] *Re Skeats' Settlement* (1889) 42 Ch D 522 (Ch) at 526. Contrast PD Finn *Fiduciary Obligations* (The Law Book Company Limited, Sydney, 1977) at [644].

[511] Unit Trusts Act 1960, s 12(1)(c).

[512] Trustee Act 1956, s 43.

duties or not; however, the addition of one more fact does allow a reasonable inference to be made.

If the settlor retains the right and is a settlor-beneficiary it can be inferred that he intended his right to be beneficial; although, the inference is not irrefutable. In my opinion, it is difficult to believe that a person, who retains both the possibility of receiving trust property and a means to influence the likelihood of that possibility being realised, intended to bind himself with fiduciary obligations to the other beneficiaries. He may well have intended to establish the trust primarily for the benefit of those other beneficiaries rather than himself but provided he intended to retain some personal benefit from his interests it is unlikely that he also intended to be bound by duties to others when choosing the trustee.

This explanation fits with Patterson's view as a leading trust expert that the right was designed to give settlors comfort that their needs and wishes would continue to be met from the trust.[513] A right that is intended by a settlor to give comfort in relation to her own well-being cannot be intended to be fiduciary.

This conclusion can also be reached through the lens of legitimate expectation. Consider a trust that is settled by Jethro. Jethro appoints Cheryl as trustee and selects himself and all his brothers and sisters as the discretionary beneficiaries. Jethro retains the right to remove Cheryl and replace her with someone else. Can Jethro's siblings legitimately expect Jethro to only exercise that right on behalf of them and to the exclusion of his own interest? If Jethro's interests lay in appointing Tracy as trustee, because she was more likely to provide a benefit of Jethro, could his siblings legitimately expect him to be obliged to appoint someone else? In my opinion, there is little to support for such an expectation.

The fact dependence of this inference is shown by varying the example. Consider the same trust but settled by Wolfgang, who is the father of Jethro and his siblings, but where Jethro is still given the right to replace. Here it may be possible to infer that Wolfgang intended to bind Jethro to exercise his rights in the interests of his siblings collectively rather than his own interests. This inference is possible because it is a reasonable inference that Wolfgang intended the trust to benefit all his children not just Jethro. If this was Wolfgang's intention then Jethro's siblings have a legitimate expectation that Jethro will act in their interests and not appoint Tracy as trustee.

In contrast to the discussion this far, it could be argued that a controlling beneficiary's right to replace can be fiduciary because the beneficiary is acting in dual capacities. For example, it could be argued that a settlor who retains both the right to replace and a discretionary interest is obliged to choose the trustee in the interests of the beneficiaries, including himself in the capacity of beneficiary, but excluding his own interests in the capacity of settlor.

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[513] Bill Patterson "Fog, Resettlements and Fraud on a Power" (paper presented to the New Zealand Law Society Trusts Conference, June 2009) 211 at 211.

This argument cannot succeed. The settlor has only one legal personality irrespective of what capacities or roles he is acting in.[514] Bob who acted as settlor is the same person as Bob acting as beneficiary who is the same person as Bob acting as donee. To be a fiduciary Bob must have a duty to benefit people who are not Bob and to the exclusion of Bob's interest. Bob's capacities or "hats" as beneficiary and donee do effect what rights, powers and duties he has. However, Bob's different capacities cannot be artificially separated when assessing his overall legal position.[515]

A final question is, where a trustee can be chosen by a beneficiary acting in his own interests, is there in fact a trust at all? On the assumptions set out in Chapter One the answer must be affirmative. The appointed trustee is still a trustee of the property. Provided that she is independent, she is obliged to hold the trust property for the benefit of the beneficiaries to the exclusion of her own benefit. Further, I have assumed that the right to choose the trustee does not alter the trust deed. Therefore, any appointed or replacement trustee must hold the trust property on the trusts contained in the deed. That is, he must consider the interests of all the beneficiaries, but has the power to make distributions to one or more to the exclusion of the others. The issue of a non-fiduciary appointing a fiduciary is returned to in section III.

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[514] See generally Ngaire Naffine *Law's Meaning of Life: Philosophy, Religion, Darwin and the Legal Person* (Hart Publishing, Portland (OR), 2009).

[515] The concept of separate capacities having an effect on a person's legal position originates in the idea of a trustee having separate hats or capacities. However, even a trustee does not have separate legal personalities depending on capacity. A trustee who is also a beneficiary is the same legal person. Three trust law principles would be violated by the idea that a trustee has two separate legal capacities or personalities:

If a trustee's capacities were treated separately the trustee as a private person would not be liable for the trustee's trust-related debts. However, it is settled law that a trustee is personally liable for debts and expenses incurred on behalf of the trust (Lionel Smith "Trust and Patrimony" (2009) 28 ETPJ 332 at 338-342; *Levin v Ikiua* [2010] NZCA 509, [2011] 1 NZLR 678 at [125]-[126]).

Likewise if a trustee's capacities were treated separately then she would be able to contract with herself in her different capacities. However, the common law holds that a contract must be between two separate legal persons not one person operating in two legal capacities. It is settled law that one of the original rules against a trustee selling trust property to himself is that there is no contract by which title can be passed if the contract purports to be between the same person acting in two different capacities (BH McPherson "Self-dealing Trustees" in AJ Oakley (ed) *Trends in Contemporary Trust Law* (Clarendon Press, Oxford, 1996) 135).

Finally, if a person's capacities as trustee and beneficiary were truly separate then she ought to be able to set up a trust where she is the sole trustee and the sole beneficiary. If she can owe a fiduciary obligation in her capacity as trustee to herself in her capacity as beneficiary then she should be able to have this type of trust. However, it is settled law that a person cannot be trustee for himself alone (*Selby v Alston* (1797) 3 Ves Jun 339, 30 ER 1042 (Ch); *Goodright v Wells* (1781) 2 Dougl 771, 99 ER 491 (KB); *Brydges v Brydges* (1796) 3 Ves Jun 120, 30 ER 926 (Rolls)); *DKLR Holding Co (No 2) Pty Ltd v Commissioner of Stamp Duties (NSW)* [1982] HCA 14, 149 CLR 431 at 463.

There are some authorities which provide mixed levels of support for the idea of a trustee having a separate legal capacity: *Hosken v Danaher* [1911] VLR 214 (SC) at 226; *Re Heberley* [1971] NZLR 325 (CA) at 332; *Robertson v Official Assignee* [2008] NZCA 500 at [20]-[21]; *Dalton v Piper* HC Auckland CIV-2005-004-2746, 4 March 2008; *Kontopos v Araboglos* HC Wellington AP247/97, 13 May 1999; *AMP Finance Ltd v Linecorp Investments Ltd* HC Auckland CP351/90, 14 June 1991 at 6.

On the other hand, other authorities provide more substantial support for the contrary proposition: *Commissioner of Inland Revenue v Chester Trustee Services Ltd* [2003] 1 NZLR 395 (CA) at [36]-[37]; *Levin v Ikiua* [2010] NZCA 509, [2011] 1 NZLR 678 at [111]; *Te Wharua Ltd v Buddle Findlay* HC Auckland CIV-2007-404-6193, 16 February 2010 at [6], [16] and [21]; *Harrison v Harrison* (2008) 27 FRNZ 202 (HC) at [20]; *Cadman* v *Visini* HC Auckland CIV-2009-404-7925, 30 May 2011; *Scott v Ellison* [2011] NZSC 100.

In conclusion, where a beneficiary has authorised himself to choose the trustee, who will then decide whether the beneficiary will benefit, there is a strong inference that he can make that choice to benefit himself. This inference might be refuted but it is argued this will only be the case where he did not intend to retain the possibility of future benefit at all. For example, a settlor who settles a trust with the intention to benefit her children and exclude herself, but who retains a discretionary interest on the advice of their solicitor, could argue that they intended their right to replace to be fiduciary because they never actually intended to benefit from the trust.

C. Cases on the Fiduciary Qualities of the Right to Replace Trustees

On balance, cases concerning the right to replace trustees support the propositions that the settlor's intention is the primary consideration and that a donee who is also a beneficiary, like a controlling beneficiary, is unlikely to be a fiduciary. However, three cases contradict these propositions: *Inland Revenue Commissioners v Schroder*,[516] *Re Burton*,[517] and *Mudgway v Slack*.[518]

Inland Revenue Commissioners v Schroder concerned a right retained by a settlor to appoint new members to a committee that in turn held a right to replace trustees exercisable by a majority of the committee. It was technically possible for the settlor to pack the committee with additional members who would then be more likely to exercise the right to replace in accordance with his wishes. Vinelott J decided that the right to appoint new members was fiduciary on the authority of *Re Skeats' Settlement*;[519] the right "could not properly be used to 'pack' the committee to ensure that the settlor has a majority".[520] This case can be distinguished from the controlling beneficiary by the difference between the right of the settlor to appoint new members to a committee and the controlling beneficiary's right to replace trustees. However, in my opinion, Vinelott J approached the issue incorrectly. He should have considered whether the settlor objectively intended to impose a fiduciary duty upon his exercise of his right.

In *Re Burton*[521] Davies J decided that a right to replace trustees held by a beneficiary of the trust was a fiduciary power that prevented it being property in the context of a bankruptcy. The only ground given by Davies J supporting this conclusion was that the right was found in a trust deed and must, therefore, be exercised in the interests of the beneficiaries.[522] This

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[516] *Inland Revenue Commissioners v Schroder* [1983] STC 480 (Ch).

[517] *Re Burton* [1994] FCA 1146, 126 ALR 557.

[518] *Mudgway v Slack* HC Auckland CIV-2010-404-2058, 26 July 2010.

[519] *Re Skeats' Settlement* (1889) 42 Ch D 522 (Ch).

[520] *Inland Revenue Commissioners v Schroder* [1983] STC 480 (Ch) at 500-501.

[521] *Re Burton* [1994] FCA 1146, 126 ALR 557.

[522] *Re Burton* [1994] FCA 1146, 126 ALR 557 at 559-560.

reasoning is insufficient. Many rights are found in trust deeds but are not fiduciary.[523] Again, this decision did not consider the intention of the settlor in retaining the right.

Mudgway v Slack was an unopposed application to the High Court to remove a trustee and to remove a right to replace the trustee. The application was part of a wider separation dispute that involved a house that was held on trust. The husband was the settlor with the right to replace. The original trustee had agreed to let the wife and children live in the house, but a few days later he was removed and replaced with the husband's insurance broker who evicted the wife with the assistance of the husband's employee. The husband also attempted to remove his separated wife and children as beneficiaries of the trust. The Court decided that the insurance broker ought to be removed and a properly independent trustee appointed. It also decided that in the interests of the children as final beneficiaries the right to replace ought to be removed from the husband and vested in the Public Trustee.

This case could be seen as proving that the husband's right was fiduciary and could be removed because he breached his duty to act in the best interests of the final beneficiaries, his children. However, it could equally be explained by the fact that the trustee he appointed appeared to breach his fiduciary duties to the beneficiaries and that the husband appeared to assist that breach. The day the trustee was appointed he evicted the children[524] and did so in the company of the husband's employee. Although there was no direct finding on whether this was a breach of trust[525] it was regarded as suspicious.[526]

The explicit ground for making the order in *Mudgway* was the principle, taken from *Clifton v Clifton*,[527] that the court has the inherent jurisdiction to modify an administrative power that could be used to the detriment of the beneficiaries. In my opinion, the principle in *Clifton* is not universally applicable. In *Clifton* the father of the final beneficiaries had the right to remove trustees but he was not a beneficiary himself. There could be no inference that this right was beneficial. In fact, *Clifton* supports the argument that a donee of the right to replace who is not a beneficiary can be inferred to be a fiduciary. The statement in *Clifton* that "the Court must have a supervisory jurisdiction to modify an administrative provision which has been shown can be used in a manner which may be to the detriment of the infant beneficiaries"[528] ought not to apply to a beneficial right unless the donee has assisted, or likely to assist, in a breach of trust. If Patterson is correct that the purpose of the right to replace trustees is to comfort the settlors then it is more than an administrative provision but is

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[523] *Re Penrose* [1933] 1 Ch 793 (Ch); *Re Triffitt's Settlement* [1958] Ch 852 (Ch) at 861, 864.

[524] He had no time to properly consider the decision to evict the beneficiaries. Compare with *McNulty v McNulty* HC Dunedin CIV-2010-412-810, 30 September 2011 at [123] where it was considered arguable that the trustee had breached its duties because it had made a decision on the same day it was appointed as trustee.

[525] *Mudgway v Slack* HC Auckland CIV-2010-404-2058, 26 July 2010 at [32].

[526] *Mudgway v Slack* HC Auckland CIV-2010-404-2058, 26 July 2010 at [27], [34].

[527] *Clifton v Clifton* HC Auckland CIV-2004-404-4185, 5 November 2004.

[528] *Clifton v Clifton* HC Auckland CIV-2004-404-4185, 5 November 2004 at [43].

an integral part of the trust and should not be removed under the High Court's inherent jurisdiction.[529]

Therefore, in my opinion, the High Court in *Mudgway* ought not to have removed the right to replace trustees without first finding that the husband had assisted in a breach of trust or was likely to abuse the right. In my opinion, this inference would not have been difficult to make. In any event, the authority of *Mudgway* is limited because the Court did not ask if the right was fiduciary and the decision was unopposed.

In contrast to the above cases, there are a number of cases that support the argument in the previous section. The Supreme Court in *Kain v Hutton* decided that the purpose of setting up a "sophisticated discretionary trust" to receive shares, which included reserving the right to replace trustees to the primary discretionary beneficiary, was to ensure that "if she wished it, that the shares would revert to her".[530] This implies that the discretionary beneficiary was authorised to exercise this right in her own interest.

A more direct authority is *P v P*,[531] which involved mirror trusts set up by a husband and wife for the purposes of asset protection.[532] The wife challenged her removal as trustee of one of the two trusts by the husband.[533] The purpose of the removal was so the husband could appoint himself as trustee and resettle the trust property onto a new trust from which the wife was excluded. This was for the personal benefit of the husband who held the right to replace. The wife argued that the right to replace was fiduciary on the basis of *Re Skeats' Settlement*[534] that had held that a right to fill vacant trusteeships was fiduciary.

The High Court distinguished *Skeats* as being from a time when powers to remove trustees were unknown[535] (at least outside of bare trusts[536]). The conclusion was that if the husband owed any fiduciary duties at all their extent was limited to a duty not to commit a fraud on the power.[537] This duty is not fiduciary and applies to all powers.[538] In any event, the husband had breached no duties because the purpose of granting the right was to allow the husband to act for his own benefit. In the words of Associate Judge Christiansen:

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[529] See *Chapman v Chapman* [1954] AC 429 (HL).

[530] *Kain v Hutton* [2008] NZSC 61, [2008] 3 NZLR 589 at [22].

[531] *P v P* HC Christchurch CIV-2004-409-1368, 29 October 2004.

[532] *P v P* HC Christchurch CIV-2004-409-1368, 29 October 2004 at [1].

[533] *P v P* HC Christchurch CIV-2004-409-1368, 29 October 2004 at [5]-[6].

[534] *Re Skeats' Settlement* (1889) 42 Ch D 522 (Ch) at 526.

[535] *P v P* HC Christchurch CIV-2004-409-1368, 29 October 2004 at [41]. See also *Charman v Charman (No 4)* [2007] EWCA Civ 503, [2007] 1 FLR 1246 (Fam) at at [55(e)].

[536] *London and County Banking Company v Goddard* [1897] 1 Ch D 642 (Ch).

[537] *P v P* HC Christchurch CIV-2004-409-1368, 29 October 2004 at [50].

[538] Geraint Thomas *Thomas on Powers* (Sweet & Maxwell, London, 1998) at [9.01]; Matthew Conaglen *Fiduciary Loyalty: Protecting the Due Performance of Non-Fiduciary Duties* (Hart Publishing, Oxford, 2010) at 50.

> It is to be remembered that Mr & Mrs Pe both received an identical power of appointment under the terms of their respective family trusts. It follows there was an expectation that each could, in exercising their respective powers of appointment of trustees, be able to take into account his or her own best interests. Why otherwise would those powers have been conferred separately upon them? The power was conferred not only to ensure that the office of trustee would be filled by a person having legal capacity, but also to ensure the trustees would be persons of whom he/she approved, and who would likely to effect his/her wishes, as those wishes are disclosed by the trusts' deeds.

This is a clear authority for determining the question by reference to the intention of the settlors.

In *Kilkelly v Arthur Watson Savage Legal*, also in the High Court and where the purpose of the trust was also asset protection,[539] the husband reserved a sole right to replace the trustees. Counsel for the husband argued that this right was for the purpose of ensuring the "smooth administration of a trust and not to preserve any control to a particular person."[540] Nevertheless, Chisholm J found that the solicitors' who set up the trust were negligent for failing to advise the wife that the husband could use the right for the purpose of removing her as trustee and would have a detrimental effect to her negotiating position if the husband and wife ever split.[541] This decision implies that the husband could in fact have used the right for this purpose without breaching any fiduciary duty to the beneficiaries.

The clearest reasoning is found in Australia. *Fitzwood Pty Ltd v Unique Goal Pty Ltd (in liq)*[542] involved a challenge to the removal of a trustee by the unitholders in a unit trust. The removal was challenged on the basis that the unitholders exercised their right to remove on the basis of incorrect information. In the course of discussion Finkelstein J made the following finding:[543]

> I am prepared to accept that a power of removal of a trustee may be a fiduciary power that must be exercised for the benefit of the beneficiaries and not for the benefit of the donee of the power, at least when the donee is not a beneficiary, although much will depend upon the terms of the trust instrument: *Re Skeats' Settlement* (1889) 42 Ch D 522 at 526; [1886-90] All ER Rep 989 at 990; *Inland Revenue Commissioners v Schroder* [1983] STC 480 at 500. However, it is not likely that such an obligation will be imposed when it is the beneficiary that has been given the power of removal. In that circumstance it may usually be assumed that the beneficiary is entitled to act in his own interests when exercising the power. Unitholders are not trustees for the trust or for one another, and the relations between them cannot be compared with the relations between fiduciaries such as

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[539] *Kilkelly v Arthur Watson Savage Legal* HC Invercargill CIV-2006-425-148, 23 July 2007 at [5].

[540] *Kilkelly v Arthur Watson Savage Legal* HC Invercargill CIV-2006-425-148, 23 July 2007 at [37].

[541] *Kilkelly v Arthur Watson Savage Legal* HC Invercargill CIV-2006-425-148, 23 July 2007 at [56].

[542] *Fitzwood Pty Ltd v Unique Goal Pty Ltd (in liq)* [2001] FCA 1628, 188 ALR 566.

[543] *Fitzwood Pty Ltd v Unique Goal Pty Ltd (in liq)* [2001] FCA 1628, 188 ALR 566 at [98].

> trustee and beneficiary, partners, principal and agent, and so on. However, while a beneficiary may act in his own interests, I do accept that there should be some limitations on the exercise of a power of removal. One restriction that I would adopt is that the power must not be exercised fraudulently. There may be other limitations as well.

This statement strongly supports the argument from principle made above.

The Family Court of Australia has taken a different approach to the right to replace. In *In the Marriage of Davidson*, Simpson, Nygh and Murray JJ held that the husband was free to appoint a trustee who was compliant with his wishes.[544] In *In the Marriage of Goodwin and Goodwin-Alpe* Nicholson CJ, Simpson and Finn JJ held that the husband could use the right of removal to control the trustee for his own benefit.[545]

These cases go further than the argument in this thesis and are based on the alter ego doctrine, which does not apply in New Zealand.[546] This thesis assumes that the right to replace does not affect trustees' duties. Therefore, the trustee has a duty not to be compliant but to make her own decisions; the right to remove does not allow the donee to control the trustee; and the right cannot be used to further a breach of trust.

Finally, in the High Court of Australia in *Kennon v Spry* French CJ made a comment that Dr Spry's powers to appoint and remove trustees were not fiduciary even though he was also a trustee. The other Judges did not comment.[547]

In conclusion, apart from the first three cases, there is considerable support for the argument that the determination of whether a right to replace is fiduciary is to be determined by the intention of the settlor. Support is also shown for inferring that the right to replace will not be fiduciary where the right is held by a beneficiary. The next issue concerns the fiduciary position of the trustee rather than that of the donee.

III. Can a Right to Replace a Fiduciary Officer be Property?

This issue is whether a right to choose who occupies a fiduciary position can be property. The question is not so much whether the right to choose is of economic value, but whether any value it has can be legitimately recognised. The concern is that any economic value to the controlling beneficiary must be a product of the trustee preferring the interests of

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[544] *In the Marriage of Davidson* (1990) 14 Fam LR 817 (FamCA) at 824.

[545] *In the Marriage of Goodwin and Goodwin-Alpe* [1990] FamCA 147, 14 Fam LR 801 at 805. See also *In the Marriage of Ashton* (1986) 11 Fam LR 457 (FamCA); *BP v KS* [2002] FamCA 1454, (2004) 31 Fam LR 436 at [58].

[546] *Official Assignee v Wilson* [2007] NZCA 122, [2008] 3 NZLR 45 at [72].

[547] *Kennon v Spry* [2008] HCA 56, 238 CLR 366 at [46].

the controlling beneficiary and breaching his duties to the other beneficiaries. As Griffiths says:[548]

> To say there is value (in the sense in which we are interested) in a power of appointment of a trustee in a discretionary trust, one must assume that the appointor will appoint a trustee who will prefer the interests of the settlor as beneficiary to the interests of any other beneficiaries. Thus such a value is predicated on a trustee not discharging his or her duties as trustee and on exercising the discretion inappropriately. To say there is monetary value in the right to appoint someone to breach his or her fiduciary duties is at the very least troublesome. There might be a value in it in the sense that I value my children's happiness or I value my relationships with friends. It might be something I am pleased or gratified to have but to give it a value in currency terms is unfortunate. To ascribe a value to such a power assumes that trustees will act in breach of duty before any breaches are demonstrated and probably that they will do so at the direction of the appointor.

It is acknowledged that there is a tension between the right to replace a person and the fact the replacement must carry out duties to others. This is the internal tension in modern trust law. However, the assumption that the controlling beneficiary would use the right to replace to direct the trustee to breach his duties is not necessarily true. This thesis argues that the replacement trustee is bound by the same trusts as the original trustee and that the donee is prohibited from using the right to induce the trustee to breach their duties to the beneficiaries. There is a tension but does not necessarily mean that there will be a breach or that the economic significance of the right cannot be recognised.

A. Responding to the Tension Inherent in a Right to Replace a Fiduciary Officer

The first response is that it is not a breach of trust to prefer one or more discretionary beneficiaries to the others. The trustee's absolute power to appoint trust property explicitly authorises the trustee to prefer some beneficiaries over others. There is no duty of even-handedness between discretionary beneficiaries.[549]

Second, a trustee who is nominated by a settlor-beneficiary is entitled to prefer the interests of the settlor over the interests of the other beneficiaries. Indeed, the trustee's duty is formed around the object of carrying out the settlor's wishes. The trustee has no duty to treat the settlor, the settlor's family and charities impartially and equally.[550] The trustee must consider factors that are relevant and the settlor's intention in establishing the trust is a relevant factor. If the settlor's intention was primarily to benefit himself then the trustee is entitled, although not obliged, to carry out that intention.

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[548] Shelley Griffiths "Valuing 'Bundles of Rights' for the Property (Relationships) Act 1976: When Neither Art nor Science is Enough" (2011) 7 NZFLJ 98 at 100.

[549] See also *Schmidt v Rosewood Trust Ltd* [2003] UKPC 26, [2003] 2 AC 70 at [33], [67], [68] where the Privy Council held that discretionary beneficiaries have varying strength claims on the trustee's discretion.

[550] See Chapter One of this thesis.

The third response is to the concern that any replacement trustee will almost definitely breach the duty to consider the beneficiaries and make a genuine decision. There is certainly a notorious history of controlling beneficiaries abusing their right by appointing trustees who are not aware of their duties and who consequently breach them.[551] However, there is a principle in trust law that a trustee is assumed to have complied with her duties until proven otherwise.[552] This applies to replacement trustees as well as original trustees.

The fourth response is that if the controlling beneficiary does use the right to appoint a compliant trustee equity already provides a remedy. Using the power to appoint a trustee who will breach the trusts can be prevented as it would be prohibited as an improper use of the power.[553] Further, any donee who abuses his right to replace in order to induce a breach of trust will be liable for assisting a breach of trust.[554]

From these responses, it cannot legitimately be assumed that any exercise of the right to replace will lead to a breach of trust. However, the concern about economic value still exists. If it must be assumed that the replacement trustee will carry out his duties like the original trustee, is there any economic benefit to be gained by being a controlling beneficiary? In my opinion the answer must be positive.

The trustee is entitled, but not required, to prefer the interests of one beneficiary over another, provided he complies with his duties to the other beneficiaries. This places him in a powerful position. For example, the original trustee is entitled to prefer the interests of the settlor-beneficiary but may also decide to prefer the interests of other beneficiaries. If the settlor replaces the original trustee and the replacement trustee prefers his interests over those of the other beneficiaries that is something the replacement is entitled, but not required, to do. Because the trustee is in such a powerful position vis-à-vis the beneficiaries the identity of the trustee is all-important. The range of actions that the trustee may take while perfectly complying with her duties is so large that the identity and preferences of the trustee will have a significant effect on the decisions that she makes and the benefits that beneficiaries receive.

Therefore, the right to choose the identity of the trustee is a tool that has a significant economic effect on all the beneficiaries. It is not a tool that can legitimately be used to interfere with the trustee's discretions and duties but it can legitimately be used to alter the identity of the trustee and consequently the preferences that the trustee will bring to the decision making process. As Associate Judge Christiansen said, it gives the ability to choose a

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[551] For example see *Mudgway v Slack* HC Auckland CIV-2010-404-2058, 26 July 2010; *Clifton v Clifton* HC Auckland CIV-2004-404-4185, 5 November 2004.

[552] PD Finn *Fiduciary Obligations* (The Law Book Company Limited, Sydney, 1977) at [88]-[89]; *Edmonds v Millett* (1855) 20 Beav 54, 52 ER 522 (Rolls); *Re Brittlebank* (1881) 30 WR 99 (Ch) at 100; *McNulty v McNulty* HC Dunedin CIV-2010-412-810, 30 September 2011 at [108]-[112].

[553] *P v P* HC Christchurch CIV-2004-409-1368, 29 October 2004 at [50]; *Fitzwood Pty Ltd v Unique Goal Pty Ltd (in liq)* [2001] FCA 1628, 188 ALR 566 at [98].

[554] See *Royal Brunei Airlines Sdn Bhd v Tan* [1995] UKPC 22, [1995] 2 AC 378; *Barlow Clowes International v Eurotrust International* [2005] UKPC 37, [2006] 1 WLR 1476.

trustee who is more likely to effect the donee's wishes. Provided the controlling beneficiary can predict what a potential trustee's preferences are likely to be the right to replace will be an economic advantage. It allows him to choose a trustee whose preference is to benefit him before the other beneficiaries, but not to the pre-meditated exclusion of those others.

A further point is that denying that the right to replace can be used to enhance the economic position of a discretionary beneficiary would be contrary to the purpose of the right. The right was designed to give comfort to settlors or other controlling beneficiaries that their needs would continue to be met by the trustees.[555] An argument that denies there is any economic benefit is denying that the right can be used for its designed purpose. If the original controlling beneficiary can use it for its intended purpose then it would be inconsistent to deny that use to any others who might receive the right from the controlling beneficiary. The purpose of the right is a means of controlling the trustee's decision-making but only by choosing the person who makes the decision not by directing the decision.

B. Comparing the Right to Replace a Trustee and a Right to Replace a Director

The issue of whether a right to choose a fiduciary officer is property is not endemic to asset protection trusts. Directors are fiduciaries and the right to replace them is an important part of the property held by a majority shareholder. This right is, like the right to replace trustees, a power according to Hohfeld's categories. The position of directors and trustees are comparable, although not identical, in relation to this issue.

Majority shareholders have the right to replace the directors,[556] however, the directors' duties are not owed to the majority shareholders but to the company and the shareholders as a whole.[557] Only where the shareholder is a holding company or the shareholders are in a joint venture are the directors specifically authorised to put the interests of the shareholders before the interests of the company.[558] Directors owe a few duties to the shareholders directly but most of their statutory duties are owed to the company.[559] Minority shareholders have the right to seek relief if the directors are acting in the interests of the majority in an oppressive or discriminatory manner.[560]

The directors' duties to the company and other shareholders does not prohibit them acting in the interests of the majority shareholders, but they are not required to do so. Directors are specifically authorised to prefer the interests of employees and creditors over the

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[555] Bill Patterson "Fog, Resettlements and Fraud on a Power" (paper presented to the New Zealand Law Society Trusts Conference, June 2009) 211 at 211.

[556] Companies Act 1993, s 156.

[557] Companies Act 1993, s 131(1).

[558] Companies Act 1993, s 131.

[559] Companies Act 1993, s 169.

[560] Companies Act 1993, s 174.

interests of shareholders.[561] The fact that directors are not obliged to act exclusively on behalf of the shareholders is part of the long running debate about whether shareholders or management control companies.[562] Directors can even make donations of company property if they consider it to be in the company's interests.

The broad discretion to make decisions either preferring the majority shareholders or not preferring them is comparable to the broad discretion of the trustee in benefiting the beneficiaries. Neither directors nor trustees have to give reasons for their decisions.[563] However, both must meet certain standards in the process of decision-making. There are dicta that directors must take relevant considerations into account when making decisions.[564] They must not act capriciously,[565] must make their own decisions and not act under the direction of the shareholders.[566] These duties are comparable to those of a trustee.[567]

The shareholder's right to replace a fiduciary director who must comply with duties to the company is a valuable item of property. The right is an integral part of the property contained in a share. The shareholder's other rights are the right to a pro rata share in any dividend and in the assets of the company if it is wound up. However, these rights may never produce any property. The directors may decide to neither declare dividends nor wind up the company. The shareholders may sell their shares but this is not a benefit received from the company, and the directors might refuse to register the transfer. The only influence the shareholders have over directly receiving benefits from the company is through the right to replace the directors.

The right to choose the director affects the majority shareholder's possibility of receiving property in the future through dividends or selling her share for an increased price. A majority shareholding is worth more than a minority shareholding.[568] Voting rights to replace directors are themselves valuable property in their own right.[569] The comparison between the shareholders' right and the controlling beneficiary's right shows there is no inherent difficulty in including these rights as property. It is the shareholders' property because it is a means of control over the constitution of the board of directors, not because it gives control over the directors' decision-making.

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[561] Companies Act 1993, ss 132, 135, 136.

[562] The leading text in this debate is Adolf A Berle and Gardiner C Means *The Modern Corporation and Private Property* (The MacMillan Company, New York, 1934).

[563] Peter Watts *Directors' Powers and Duties* (LexisNexis, Wellington, 2009) at 131.

[564] *Hedley v Albany Power Centre Ltd (In Liquidation)* [2005] 2 NZLR 196 (HC) at 210.

[565] Peter Watts *Directors' Powers and Duties* (LexisNexis, Wellington, 2009) at 147.

[566] See *Mason v Lewis* [2006] 3 NZLR 225 (CA) at [58], [83]; PD Finn *Fiduciary Obligations* (The Law Book Company Limited, Sydney, 1977) at [42].

[567] See Chapter One of this thesis.

[568] *Holt v Holt* [1990] 3 NZLR 401 (PC) at 403-405.

[569] *Re Burgess Homes Ltd* [1987] 1 NZLR 513 (CA).

Like the right to replace trustees, the right to replace the directors is not a direct economic advantage to the majority shareholders. Its economic significance is the influence it has over the likelihood of other interests producing direct economic advantages.

The similarity between the right to replace the director and the right to replace the trustee is reflected in their common history of being abused. Shareholders have used their rights to appoint ignorant directors that they can exploit,[570] just as controlling beneficiaries have used their rights to appoint trustees they can exploit.[571] The fact that a majority shareholder may illegitimately use the right to replace directors cannot be taken into account in the valuation of those shares. On the other hand, the fact that it might happen does not prevent the right being included as part of the shareholder's property. Equity will not allow the majority shareholder's right to replace directors to be abused[572] and, likewise, will not allow the right to replace trustees to be abused.[573]

The key difference between a director and a trustee is that the director cannot alter shareholders' entitlements to income and capital but the trustee with an absolute discretionary power of appointment can. Therefore, the controlling beneficiary's right to replace the trustee is even more significant and valuable than the majority shareholder's right to replace directors. The controlling beneficiary's right does not have the limiting factor that the trustee must make distributions equally.

The comparison between the controlling beneficiary's right to replace the trustee and the majority shareholder's right to replace the board of directors supports the argument that the economic significance of the controlling beneficiary's right can legitimately be recognised.

C. Conclusion: Economic Significance

It is argued that if this right is not affected by fiduciary duties then it must be recognised as economically significant. However, it is not inherently valuable. It is only valuable indirectly.

The first way it can be valuable is when it is held by a discretionary beneficiary. The controlling beneficiary can use the right to choose a trustee who is likely to prefer her interests to those of the other beneficiaries; but who will also comply with all the duties of a trustee. That is, the controlling beneficiary can use the power to increase the likelihood that she will receive property under her discretionary interest.

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[570] *Official Assignee v Sanctuary Propvest Ltd* HC Auckland CIV-2009-404-852, 11 June 2009 at [25]; *National Bank of New Zealand v Ram* (1992) 4 NZBLC 102,618 (HC).

[571] *Mudgway v Slack* HC Auckland CIV-2010-404-2058, 26 July 2010; *Clifton v Clifton* HC Auckland CIV-2004-404-4185, 5 November 2004.

[572] *Holt v Holt* [1990] 3 NZLR 401 (PC) at 404.

[573] *P v P* HC Christchurch CIV-2004-409-1368, 29 October 2004 at [50]; *Fitzwood Pty Ltd v Unique Goal Pty Ltd (in liq)* [2001] FCA 1628, 188 ALR 566 at [98].

The second way is if the right can be sold. If it can be sold then it does not matter whether it is of value to the person holding it. They can obtain economic value by selling it to someone for who it is valuable. In this case, the right will be valuable whenever it can be sold to a discretionary beneficiary. This is related to whether the right is assignable.

IV. Does the Right to Replace Trustees Fit the Statutory Schemes?

The final question is whether the right to replace trustees is capable of meeting the requirements of the statutory schemes.

The first issue is whether the right is assignable. If it is assignable then if it could be ordered to be sold under the High Court Rules or sold by the administrators of the deceased beneficiary's estate. If it is not able to be sold then it might not be property in these contexts for the same reasons discussed in relation to the discretionary interest. Although there is still the potential argument that it is chargeable under *Don King Productions Inc v Warren*.[574]

The question whether the right to replace can be assigned is much the same as the question of whether a contractual right can be assigned. Powers are assigned by delegating the exercise of the power to another, but this cannot be distinguished from ordinary assignment of a right. Whether delegation is possible depends on the interpretation of the trust deed to determine whether delegation was authorised by the settlor.[575] In many trust deeds the intention regarding assignment is clear as they are often made assignable by deed or will. Where assignment is not explicitly covered the intention of the settlor regarding assignment must be inferred from the circumstances.

Where the right to replace is not fiduciary the likely inference is that the settlor intended it to be delegable. If the settlor intended the right to be used for the benefit of the donee then it reasonable that she intended the donee to be able to transfer it to others.[576] The Privy Council has held that a non-fiduciary power of revocation can be delegated by the donee. It acted upon its finding by agreeing to order the holder of the power to delegate it to a receiver for benefit of his creditors.[577]

Contrary to this conclusion, there is one case in the Family Court that decided a right to replace trustees was not property under this Act because it was not inherently transferable. In *S v S*[578] the parties had agreed that a husband would transfer his right to the wife as part of a

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[574] *Don King Productions Inc v Warren* [2000] Ch 291 (CA). See Chapter Two of this thesis.

[575] *Re Triffitt's Settlement* [1958] Ch 852 (Ch) at 861. The same principle applies in regard to the assignability of contractual rights (*Shayler v Woolf* [1946] Ch 320 (CA) at 321-322; *J Miller Ltd v Laurence & Bardsley* [1966] 1 Lloyd's Rep 90 (Ch); *New Zealand Payroll Software Systems Ltd v Advanced Management Systems Ltd* [2003] 3 NZLR 1 (CA)). See also Marcus Smith *The Law of Assignment: The Creation and Transfer of Choses in Action* (Oxford University Press, Oxford, 2007) at Chapter 12.

[576] *Re Triffitt's Settlement* [1958] Ch 852 (Ch) at 864.

[577] *Tasarruf Mevduati Sigorta Fonu v Merrill Lynch Bank and Trust Company (Cayman) Limited* [2011] UKPC 17, [2011] BPIR 1743 at [61].

[578] *S v S* (2006) 25 FRNZ 863 (FC).

separation agreement. The Judge was asked by the parties to interpret the agreement and enforce it, but she questioned the basis on which she could enforce it. This was because she held that the right was not property. Her reasoning was that the right must be freely transferable to be property and that this right was not freely transferable because it could only be transferred according to provisions in the deed that allowed it to be transferred by a particular process.[579] This reasoning is a unique understanding of the meaning of property and contradicts the Court of Appeal in *Z v Z (No 2)*.[580] Indeed, the facts and result of the case undermine the reasoning applied by the Judge.

The Judge enforced the transfer of the right by ordering the husband to specifically perform the agreement.[581] What the Judge in fact did was to enforce the assignment for consideration of the right under a property relationship agreement. Contrary to the Judge's reasoning this result supports the power being included as property. The Judge herself said that the right could be property if it was saleable[582] and assignment for consideration is a sale. There is no reasonable basis for holding the right is not assignable merely because its assignment is governed by the trust deed.

In relation to the Insolvency Act 2006 and Property (Relationships) Act 1976 this right does not need to be assignable to be property. It only needs to be legally and economically significant. This conclusion is supported by the Court of Appeal in *Walker v Walker*.[583] The Court stated in obiter that powers to appoint and remove trustees were "assets"[584] and "items of property" under the Property (Relationships) Act 1976.[585] Together with other interests, including discretionary interests, it made up a valuable package.

V. Conclusion

The first conclusion reached in this chapter was that a Hohfeldian power like the right to replace trustees is able to be property even though it is not a claim-right. This power is a right in the common and broad sense of "right". This establishes that the right to replace is a legally significant interest.

To cross the threshold of economic significance the right cannot be fiduciary. If it is fiduciary it cannot be used to economically advantage the donee. Whether or not it is fiduciary depends on whether it was intended to be used for the benefit of the donee or the

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[579] *S v S* (2006) 25 FRNZ 863 (FC) at [62]-[65].

[580] *Z v Z (No 2)* [1997] 2 NZLR 258 (CA).

[581] *S v S* (2006) 25 FRNZ 863 (FC) at [86].

[582] *S v S* (2006) 25 FRNZ 863 (FC) at [59].

[583] *Walker v Walker* [2007] NZCA 30, [2007] NZFLR 772. See also *Harrison v Harrison* [2009] NZCA 68, [2009] NZFLR 687 at [10]; *R v R* [2010] NZFLR 555 (FC) at [10], [61(d)]; *JR v LR (A Bankrupt)* [2011] NZFLR 797 (FC) at [59(xviii)], [59(xv)], [60].

[584] *Walker v Walker* [2007] NZCA 30, [2007] NZFLR 772 at [48].

[585] *Walker v Walker* [2007] NZCA 30, [2007] NZFLR 772 at [49].

donee was intended to be obliged to use it for the benefit of the other beneficiaries. Where this right is granted to a discretionary beneficiary, it can be inferred from that fact alone, but subject to facts indicating otherwise, that it was intended to be beneficial not fiduciary.

The fact the right is only a means of control over the constitution of the office of trustee and is not a means of control over the trustee's decision making does not prevent it being economically significant. However, it does prevent the donee from interfering with the trustee's duties to the other beneficiaries. Recognising the right's economic significance does not require an assumption that the trustee will breach her duties. The trustee is comparable to a director who can be removed by the majority shareholders but must nonetheless carry out his duties to the company and minority shareholders. The right to choose a trustee who is more likely to carry out the controlling beneficiary's wishes is likely to be a valuable economic interest as it enhances the value of that beneficiary's discretionary interest.

The economic significance of this right is in its ability to increase the likelihood that a discretionary beneficiary will receive a distribution of property. Therefore, it might only be of sufficient economic significance to qualify as property when it is associated with a discretionary interest. However, if it can be assigned then it might have a subsidiary economic significance by being able to be sold to a discretionary beneficiary. This issue affects the interest under the estate claim statutes and the High Court Rules but not under the Insolvency Act 2006 and Property (Relationships) Act 1976 where the right to replace trustees can remain associated with the discretionary interest.

CHAPTER FIVE: VALUATION

The previous two chapters argued that the discretionary interest and right to replace trustees can be property, at least under the Insolvency Act 2006 and Property (Relationships) Act 1976. After an interest has been found to be property under these Acts it can be used to economically compensate somebody other than the current owner. In insolvency, compensation is achieved by the Official Assignee using the interest to create a gain for creditors. In a relationship separation this is achieved by valuing the interest. Valuation of an interest is not strictly necessary in insolvency, but the valuation process can be used to give an indication of how much the creditors might gain from the interest.

The first point to be made is the relation between the discretionary interest and the right to replace the trustees. I have argued that they can both be property in their own right. However, the value of the right to replace is dependent on the valuation of the discretionary interest. If the right is held by a controlling beneficiary then it enhances the value of her discretionary interest; if it is not held by a controlling beneficiary then its value is in being sold to a discretionary beneficiary. This means that the valuation process for these two interests is connected.

Valuation of the discretionary interest and right to replace trustees is not fundamentally different from the valuation of any other possibility. For example, the bundle of interests that make up a non-preference shareholding can be valued even though the shareholder has no right to receive any dividends or have the company wound up.[586] In all valuations there are two aspects to be considered. The first is the object of valuation; the second are the methods by which the object is achieved.

The overriding object of valuation is to find the best estimate of what people think that interest is worth; that is, what price would be paid for that interest if it were saleable and it was sold.[587] An important framing tool for this objective is the classic mantra[588] of value equalling the price that would be paid "on the basis of a hypothetical sale by a willing but not anxious seller to a willing but not anxious buyer."[589] A controversial aspect of valuing the present interests is the assumptions that are made when framing this hypothetical transaction.

In contrast to the object, the methods of valuation are merely tools that assist in estimating the price that would be paid in the transaction. They include the estimated future

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[586] Shelley Griffiths "Valuing 'Bundles of Rights' for the Property (Relationships) Act 1976: When Neither Art nor Science is Enough" (2011) 7 NZFLJ 98 at 99.

[587] *Hatrick v Commissioner of Inland Revenue* [1963] NZLR 641 (CA) at 661-662.

[588] This test originated in 19th century England (see Bernard Marks "Valuation Principles in the Income Tax Assessment Act" (1996) 8 Bond LR 114 at 118-120).

[589] *Haldane v Haldane* [1981] 1 NZLR 554 (CA) at 562.

cash flow method and the deemed realisation method. These two aspects of valuation will be examined and then applied to the discretionary interest and right to replace trustees.

I. The Concept of Market Value

The goal of finding the value of an interest, without actually ordering a sale, requires imagining what would happen if there was a sale. The market value test assumes a hypothetical marketplace with hypothetical participants. Finding the market value is an exercise in estimating the probabilities in this hypothetical transaction.

A controversial issue is the assumptions made about the hypothetical participants in the transaction. For example, if it was assumed that the buyer and seller were contract law's 'reasonable people' then the market value test would be to assess what the reasonable person would be willing to pay for the property. The reasonable person would be likely to pay very little for a discretionary interest because the reasonable person has no significant claim on the exercise of the trustee's discretion.

However, the object of valuation is not to estimate how much a 'reasonable' person would pay for an interest. The object is to estimate, within certain parameters, the price that would be paid in the real world if the property was really being sold. Therefore, the hypothetical sale takes into account real world factors. The most reliable valuations exist where there is a thriving market for the property that allows those real world factors to be accurately estimated – as in real estate.

Thus the hypothetical transaction includes estimates of the price real world people might pay for reasons that are unique to them.[590] For example, if an interest in land is for sale and a neighbour would pay a higher price than anyone else because she could use it to enhance the value of her own land then the possibility of acquiring that higher value is included in the market value (although it is not treated as a certainty because the neighbour may not buy for other reasons). Lord Hoffmann explains this in the context of assessing capital transfer tax:[591]

> The practical nature of this exercise will usually mean that although in principle no one is excluded from consideration, most of the world will usually play no part in the calculation. The inquiry will often focus on what a relatively small number of people would be likely to have paid. It may have to arrive at a figure within a range of prices which the evidence shows that various people would have been likely to pay, reflecting, for example, the fact that one person had a particular reason for paying a higher price than others, but taking into account, if appropriate, the possibility that through accident or whim he might not actually have bought.

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[590] *Coleman v Myers* [1977] 2 NZLR 225 (CA) at 335; *Holt v Holt* [1987] 1 NZLR 85 (CA) at 89, 92, 96; *Holt v Holt* [1990] 3 NZLR 401 (PC); Bernard Marks "Valuation Principles in the Income Tax Assessment Act" (1996) 8 Bond LR 114.

[591] *Gray (surviving executor of Lady Fox deceased) v Inland Revenue Commissioners* [1994] STC 360 (CA) [accessed online].

More contentious is whether the real world vendor, in this case the current discretionary beneficiary, should be included in the hypothetical transaction. Lord Hoffmann made this distinction in the same case:[592]

> The hypothetical vendor is an *anonymous* but reasonable vendor, who goes about the sale as a prudent man of business, negotiating seriously without giving the impression of being either over-anxious or unduly reluctant. The hypothetical buyer is *slightly less anonymous*. He too is assumed to have behaved reasonably, making proper inquiries about the property and not appearing too eager to buy. But he also reflects reality in that he embodies whatever was actually the demand for that property at the relevant time.

If Lord Hoffmann's assumption that the seller is anonymous is applied to discretionary interests then the unique value that the current discretionary beneficiary places on retaining their interest cannot be included in the valuation.

However, it is clear that in New Zealand Lord Hoffmann's formula is not followed. The real world vendor is included in the hypothetical transaction.[593] This was conclusively established by the Court of Appeal in the relationship property context in *Z v Z*.[594] The issue was whether goodwill should be valued on the assumption that the husband would accept a restraint of trade in any hypothetical sale. This would increase the goodwill's value from $25,000 to $80,000. Richardson J was explicit: "The test is the value of the property on a hypothetical sale, and on that hypothetical sale the husband may be included in the classes of hypothetical sellers and hypothetical buyers."[595] Casey J also included the real world seller. He considered what price the real world seller would pay if he was able to purchase the property from himself.[596] Inclusion of the actual owner of the interest in the hypothetical transaction is supported in a number of other Court of Appeal cases.[597]

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[592] *Gray (surviving executor of Lady Fox deceased) v Inland Revenue Commissioners* [1994] STC 360 (CA) [accessed online, emphasis added].

[593] Contrast Shelley Griffiths "Valuing 'Bundles of Rights' for the Property (Relationships) Act 1976: When Neither Art nor Science is Enough" (2011) 7 NZFLJ 98 at 102.

[594] *Z v Z* [1989] 3 NZLR 413 (CA).

[595] *Z v Z* [1989] 3 NZLR 413 (CA) at 415.

[596] *Z v Z* [1989] 3 NZLR 413 (CA) at 417.

[597] In *Haldane v Haldane* the Court of Appeal was concerned with the value of an interest under the husband's superannuation scheme in the context of a husband and wife separating. Richardson J held that the value was to be determined by a realistic appraisal of the present value of future benefits, and that the realistic appraisal would have to take into account what price the current owner would realistically accept to give up the interest (*Haldane v Haldane* [1981] 1 NZLR 554 (CA) at 562). Cooke J also included factors unique to the individual in valuing the interest. These factors included the husband's prospects of promotion and salary increases which would increase his pension entitlements. If the husband was involved in a hypothetical sale he "would naturally and justifiably stress these prospects and advantages" (*Haldane v Haldane* [1981] 1 NZLR 554 (CA) at 558). Somers J stated that the appropriate test of value was "the sum which, on the supposition that such a course was possible, a willing but not anxious husband would accept from the management of the fund in exchange for a surrender of all his present and future claims" (*Haldane v Haldane* [1981] 1 NZLR 554 (CA) at 569).

Walker v Walker is also in the relationship property context and a discretionary interest was one of the relevant items of property to be valued. The Court held that the interest, along with other rights and interests, was

It has been suggested that this approach to value is not a market value test at all but a conceptually different "value to owner" test.[598] This suggestion is contrary to the New Zealand cases.[599] The value to the current owner is logically part of the test of market value. Where the property has a unique financial value for the seller he would not accept a price in the market that does not compensate him for that special value. For example, consider the owner of a patent in a particular technology who also is the only person in the industry who has the human capital necessary to exploit the patent for profit. It is worth more to the owner than to other firms in the industry; therefore, those other firms would not be willing to pay the high price that the owner would require before selling it. In this situation the market value cannot be the value to purchasers who cannot use the property; the true value is the price that would be required by the owner before it would sell.[600] In my opinion, market value naturally includes the value to the owner.

Notwithstanding the above, the market value test does exclude some real world factors; for example, in valuing property that cannot be transferred. In the real world no one would pay for the property and the vendor could not expect to receive anything. The fact of non-transferability needs to be ignored and property valued as if it were transferable.[601]

Another real world factor that is ignored is personality or emotional state. A vendor or potential purchaser who is depressed, compulsive or has a sentimental attachment to property that would affect the price they pay is assumed not to have those traits. All market participants are assumed to be rational self-interested, utility-maximizers.[602] This is significant in the valuation of the right to replace.

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valuable because the husband would have paid a considerable amount to keep those interests (*Walker v Walker* [2007] NZCA 30, [2007] NZFLR 772at [49]).

The approach is also accepted when valuing interests outside the relationship property context. In *Coleman v Myers* there was a takeover offer where the offeror was accused of misleading and fraudulent conduct by the shareholders because he did not tell them that he was preparing to break up the company and sell off some of its valuable assets. Valuation was relevant because the High Court judge considered that the misleading conduct did not result in any loss because the parties received the proper valuation for their shares in any event. The Court of Appeal disagreed and took a different approach to valuation. The Court said that the offeror omitting to disclose his true plans in regard to the company concealed important information that the shareholders would have used in assessing whether to accept the takeover offer. Cooke J held that the shareholders were not limited to assessing the value of the shares to themselves but would have taken into account the value of the shares to the offeror (*Coleman v Myers* [1977] 2 NZLR 225 (CA) at 335).

See also *Holt v Holt* [1990] 3 NZLR 401 (PC); *Cole v Cole* (1982) 5 MPC 17 (HC); RL Fisher (ed) *Fisher on Matrimonial and Relationship Property* (online looseleaf ed, Lexisnexis, New Zealand) at [10.11].

[598] See Shelley Griffiths "Valuing 'Bundles of Rights' for the Property (Relationships) Act 1976: When Neither Art nor Science is Enough" (2011) 7 NZFLJ 98 at 102; Margaret R O'Sullivan "Valuation Issues and Discretionary Trusts" (2008) 28 ETPJ 75 at 83.

[599] See *Z v Z* [1989] 3 NZLR 413 (CA) at 415.

[600] *Holt v Holt* [1990] 3 NZLR 401 (PC).

[601] See *Haldane v Haldane* [1981] 1 NZLR 554 (CA) at 569.

[602] *Holt v Holt* [1987] 1 NZLR 85 (CA) at 90; *Holt v Holt* [1990] 3 NZLR 401 (PC) at 402-403; *Gray (surviving executor of Lady Fox deceased) v Inland Revenue Commissioners* [1994] STC 360 (CA) [accessed online]; Michael K O'Connor and Charles Haccius "The Valuation for Estate Duty Purposes of Private Company

Taking the above into account, the controlling beneficiary's interests can be valued according to the economic value they have for the beneficiary and not the value to a stranger. Secondly, the controlling beneficiary is assumed to be a rational self-interested, utility-maximizer who will act to extract the most value out of her interest as she can. In a hypothetical sale she would take into account the uncertainties about whether the trustee will make a distribution to her but will not discount it so far that selling it would be to her detriment.

II. Valuation Methods and Practical Difficulties

Applying the market value test always gives an approximate value and can never be exact, even in relation to property like real estate. Applying the market value test to discretionary interests will be more difficult than real estate because there are more variables that need to be estimated. Practical difficulty in valuing an interest does not equate to conceptual impossibility.[603]

In my opinion, the only appropriate method of valuation for a future possibility is the capitalised value of the estimated future cash flow.[604] This method commences by estimating the financial cash flows expected to be derived from the interest in the future. Then, it converts those cash flows into a lump sum. Third, it discounts the lump sum to allow for uncertainties and the fact that money in the present is worth more than money in the future. This final sum is what the rational owner would be willing to sell his interest for.

Deemed realisation is an alternative method. It estimates the value that could be extracted if the trust was terminated. This is commonly used to value shares in closely held companies where a purchaser will have the choice to wind up the company and extract the value of its assets.[605]

The latter method was applied in a Canadian case *Sagl v Sagl*[606] that valued a discretionary and capital beneficiary's interest as an equal share in the trust fund on the basis that is what he would have received if the trust had been terminated. This has been

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Shareholdings" (1970) 2 DULR 27 at 29; Bernard Marks "Valuation Principles in the Income Tax Assessment Act" (1996) 8 Bond LR 114 at 119.

[603] Shelley Griffiths "Valuing 'Bundles of Rights' for the Property (Relationships) Act 1976: When Neither Art nor Science is Enough" (2011) 7 NZFLJ 98 at 99; *Haldane v Haldane* [1981] 1 NZLR 554 (CA) at 569-570.

[604] Shelley Griffiths "Valuing 'Bundles of Rights' for the Property (Relationships) Act 1976: When Neither Art nor Science is Enough" (2011) 7 NZFLJ 98 at 99; Michael K O'Connor and Charles Haccius "The Valuation for Estate Duty Purposes of Private Company Shareholdings" (1970) 2 DULR 27 at 31-32; Vanessa Van Coppenhagen "The Valuation of Copyright" (2004) 16 SA Merc LJ 535 at 359-361; G Ovens "The Valuation of Private Companies and Other Properties for Succession Duties and Similar Purposes" (1953-1958) 2 *University of British Columbia Legal Notes* 61 at 66.

[605] See Michael K O'Connor and Charles Haccius "The Valuation for Estate Duty Purposes of Private Company Shareholdings" (1970) 2 DULR 27.

[606] *Sagl v Sagl* (1997) 31 RFL (4th) 405 (Ontario General Division), 1997 CanLII 12248 (ON SC).

criticised.[607] This method is not appropriate for a purely discretionary trust because no beneficiary has the power to terminate. Therefore, a deemed realisation has little relationship to the actual economic value anyone would place on the interest.[608]

Another Canadian case, *Kachur v Kachur*,[609] adopted the cash flow method. It concerned the value of the discretionary interest of the husband. The Kachurs had set up a trust to hold shares in a company. Mr Kachur, his children and his grandchildren were the discretionary beneficiaries. It decided that the whole of the trust property was likely to either go to Mr Kachur or his children so the question was how much was likely to go to each of them. In estimating Mr Kachur's future cash flow the court took into account the following factors:

1. The intention of the settlor: the unchallenged evidence was that the trust was set up to benefit the Kachur's children.[610]

2. The reason why Mr Kachur had been granted a discretionary interest: the unchallenged evidence was that the only reason was an escape clause in case it later became inappropriate to distribute all the property to the children.[611]

3. The pattern of distributions from the trust: all distributions had been made to the children equally, none to Mr Kachur.[612]

4. The likelihood and circumstances of the trustees making a distribution to Mr Kachur: the Judge accepted that there was no realistic prospect of Mr Kachur receiving a distribution in the future.[613]

The conclusion was that Mr Kachur's discretionary interest was worth nothing but the children's interests did have value.

This reasoning supports the argument that the discretionary interest should be valued according to the estimated future cash flow. It shows that in some cases a discretionary interest will have no value because the likelihood of any future distributions is nominal. It also shows that in other circumstances discretionary interests can be valued because the likelihood of property being received in the future is high.

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[607] Shelley Griffiths "Valuing 'Bundles of Rights' for the Property (Relationships) Act 1976: When Neither Art nor Science is Enough" (2011) 7 NZFLJ 98 at 101; Lorne H Wolfson and Ikka Delamer "The Valuation of Trusts Under the Family Law Act" (2002) 20 CFLQ 97.

[608] See also RL Fisher (ed) *Fisher on Matrimonial and Relationship Property* (online looseleaf ed, LexisNexis, New Zealand) at [10.11]-[10.14].

[609] *Kachur v Kachur* 2000 ABQB 709.

[610] *Kachur v Kachur* 2000 ABQB 709 at [36].

[611] *Kachur v Kachur* 2000 ABQB 709 at [35].

[612] *Kachur v Kachur* 2000 ABQB 709 at [35].

[613] *Kachur v Kachur* 2000 ABQB 709 at [40].

III. Valuing a Discretionary Interest

The factors that are likely to be taken into account in estimating the future cash flow from a discretionary interest include:

1. The intentions of the settlor;
2. The fiduciary duties of the trustees;
3. The number of beneficiaries;
4. The manner in which the power has been exercised in the past;[614]
5. The size of trust fund;
6. Any criteria, including a letter of wishes, provided by the settlor in relation to the exercise of discretion by the trustees;
7. The number and identity of default beneficiaries;
8. The existence of any other powers such as a power to reduce or enlarge the class of discretionary beneficiaries; and
9. The relationship of the beneficiaries to the settlor and the trustees.[615]

The last factor is likely to be the most influential. The main reason that an existing beneficiary would put a higher value on his interest than a stranger to the trust is that the beneficiary is likely to have a stronger claim on the trustee and the trustee is, therefore, more likely to exercise her discretion in the beneficiary's favour. There will also be differences between the strength of claims of different beneficiaries. For example, a couple who settle a trust initially for their own benefit will have a stronger claim on the trustee's discretion than their children. Their children in turn will usually have a stronger claim than any charities that are included under the typically broad charities class.

Basing a valuation of an interest on the claim of a beneficiary against the trustee's discretion invites the argument that this is not a relevant consideration because it is not a legal claim. This argument cannot succeed because it overlooks the basis of the market value test. The market value test looks at any considerations that are "likely materially to affect the mind of a vendor or of a purchaser."[616] Market value is not determined by legal niceties but by economic facts; it does not distinguish between legal facts and other facts. For example, in

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[614] These first four are from a presentation by Marcus Cullity cited by Lorne H Wolfson and Ikka Delamer "The Valuation of Trusts Under the Family Law Act" (2002) 20 CFLQ 97.

[615] These last factors are taken from IJ Hardingham and R Baxt *Discretionary Trusts* (2nd ed, Butterworths, Sydney, 1984) at [711].

[616] *Hatrick v Commissioner of Inland Revenue* [1963] NZLR 641 (CA) at 661.

valuing a house, legal facts such as the power to sell are no more relevant than non-legal facts such as its view.

My conclusion is supported by *Schmidt v Rosewood Trust Ltd*,[617] where the Privy Council held that the son of the settlor had an exceptionally strong claim to be considered by the trustees.[618] The possibility that the beneficiary would receive property was more than theoretical.[619] The strength of the beneficiary's claim meant that the Council saw it as worth protecting by the disclosure of documents. A claim that is worth protecting is one that can have economic value placed on it.

However, the necessity for contingencies to be taken into account means that even a discretionary beneficiary with the strongest possible claim will not have an interest equal to the entire value of the trust assets. There will always need to be some discount for the possibility that the trustee will distribute the property to someone else. Even if there was only one discretionary beneficiary the interest would have to be discounted for the possibility of the trustee accumulating the income and keeping capital for the default beneficiary. In practice, the contingencies and uncertainties in estimating a future exercise of a power will be considerable. However, the example of *Kachur v Kachur* shows it is not so difficult that it is impossible.

In conclusion, the value of the discretionary interest will usually be the price that the beneficiary would pay to keep that interest. The beneficiary would calculate that amount by estimating how much they are likely to receive from their interest in the future taking into special consideration the strength of their claim on the exercise of the trustee's discretion. However, because of the extensive contingencies that would need to be taken into account the discretionary interest will always be significantly discounted. In practice the value of the discretionary interest will never match the value of the assets of the trust.

IV. Valuing a Right to Remove Trustees

Putting a value on a right to remove trustees when it is held by a discretionary beneficiary or can be sold to a discretionary beneficiary is conceptually straightforward. It is conceptually the same as placing a value on the difference between the shares of majority and minority shareholders.

The economic value of the power is the difference between the estimated future cash flows from the same beneficiary's discretionary interest in two different states. The first state is the estimated future cash flow where the trustee is replaced with a trustee who does not prefer the beneficiary's interests. For example, if Ben is the beneficiary, the estimate in the first state is what he would expect to receive if the right to replace trustees is held and

[617] *Schmidt v Rosewood Trust Ltd* [2003] UKPC 26, [2003] 2 AC 70.

[618] *Schmidt v Rosewood Trust Ltd* [2003] UKPC 26, [2003] 2 AC 70 at [68].

[619] *Schmidt v Rosewood Trust Ltd* [2003] UKPC 26, [2003] 2 AC 70 at [67].

exercised by Jenny in her own interests rather than his. The second state is the estimated future cash flow from Ben's discretionary interest if Ben is able to replace the trustee with one who prefers his interests to Jenny's. The value of the right to replace is the difference in estimated future cash flows between these two states.

In one state Ben is unlikely to receive very much at all as his claim on the trustee's discretion is likely to be little more than theoretical. In the other Ben will have a strong claim on the trustee's discretion. Of course, depending on the other factors in any particular case the difference could change. For example, if the settlor of the trust set out in the letter of wishes that the purpose of the trust was to benefit Ben before any of the other beneficiaries then the cash flow Ben could expect in the first state will be somewhat more than minimal. However, because the settlor's wishes cannot bind the trustee, the identity of the trustee will still significantly affect the estimate of future cash flow.

In my opinion, the degree to which a right to replace the trustees will increase the value of the discretionary interest will be inversely related to how many discretionary beneficiaries there are. If the range of discretionary beneficiaries is very large then the likelihood of the trustee distributing to other beneficiaries is probably lower than if the range is small. For example, if there are only two beneficiaries then the trustee is likely to give each of them more than minimal benefits from the trust regardless of who has the right to replace the trustee. On the other hand, if the range includes everyone in the world, except for the trustee, then the trustee is much more likely to only benefit the controlling beneficiary as the claims of any other individual will be diluted by the sheer number of other beneficiaries.

There is one more additional point that will be very important in valuing the combination of a right to replace trustees and a discretionary interest rather than just a discretionary interest alone. This point is that in valuing the discretionary interest the discretionary beneficiary is passive. He has little influence over the estimated future cash flow, apart from requesting that it be exercised in his favour. In contrast, the discretionary beneficiary with a right to replace the trustee becomes an active figure – the controlling beneficiary. The fact that the controlling beneficiary can act to increase the likelihood of receiving property in the future means that valuation must include the future action that might be taken.

When the interest is more than passive the assumption that the hypothetical purchasers and vendors are rational self-interested wealth-maximisers is critical. The value of an interest to an owner is the value that could be extracted from that interest by a rational self-interested wealth-maximiser who takes reasonable steps to ensure she does not lose any value.

This means that the estimate of how much the future cash flow would increase due to a discretionary beneficiary having the right to replace the trustee does not involve estimating what that beneficiary is actually likely to do with the right to replace. The actual controlling beneficiary may be happy to let the trust continue and obtain no personal gain from it, but a

rational self-interested wealth-maximiser would use the right to appoint a trustee who is independent but who is likely to prefer her interests to those of the other beneficiaries. A financially responsible controlling beneficiary would not choose to retain an uncertain discretionary interest but would seek to derive a real financial return from it.

This is an important assumption when considering trusts where the controlling beneficiary was the settlor. Such trusts are commonly intended to benefit the controlling beneficiary / settlor while he is alive and then benefit his children, relatives, friends or charities after he dies. Part of the purpose in having a trust is to eventually transfer property to others; while the settlor is alive the position of controlling beneficiary gives him comfort that his needs will continue to be met to the extent necessary. However, if this settlor / controlling beneficiary is assumed to be a rational self-interested wealth-maximiser then any intention he has that his children or others are to eventually receive the trust property is irrelevant to the value the controlling interest has in the present. For as long as the settlor retains an interest that he can use to increase his own benefit the fact that he may intend to be generous in the future is disregarded for the purpose of valuing his present interest.

This was made clear in *Holt v Holt* in relation to the valuation of shares in a company that owned a farm when a couple separated. The husband owned a single A share and the remaining 999 B shares were held on trust for the couple's children. The single A share had the majority of voting rights and gave the husband control over the company and farm, which he operated. From this structure it appears that the couple intended the A share and the farm company to eventually pass to their children; however, this was not taken into account in valuation:[620]

> Because the inquiry is into the intrinsic or abstract worth of the A share no regard can be paid to personal desires of the husband as to the future of the company or the welfare of his family or other matters of sentiment which would no doubt affect him if he were indeed minded to sell the share.

The result in the case was that the single controlling A share was valued at $150,000 rather than the $640 that was its pro rata value. The value of the share to the husband was so high because he could actively use the power of control for his own benefit by employing himself to operate, and live on, the farm.

In my opinion, this valuation assumption is entirely reasonable when applied to discretionary trusts with a controlling beneficiary. The fact is that such a beneficiary has the ability to benefit and the ability to prefer her own interests. The fact that she may only intend to use those interests to benefit herself in the event of some unforeseen emergency does not change the real economic value that those interests give her. The fact that she may intend her children to benefit in the future has no more relevance to valuation in the present than the

[620] *Holt v Holt* [1987] 1 NZLR 85 (CA) at 96.

intention of a house owner who intends to give her house away to charity has on the valuation of that house.

This means that a settlor who settles a trust with the sole intention of benefiting her children should not retain both a discretionary interest and a right to replace the trustees. If she does she is likely to be reducing the benefit she is providing to her children. The settlor in this situation should retain a discretionary interest or the right to replace but not both.

V. Conclusion

In conclusion, the controlling beneficiary's interests can have a monetary value placed on them. The market value test requires that the value of the interests to all relevant persons including the current owners is considered. This means that market value can be estimated by estimating the future cash flow value of the discretionary interest to the current owner and prospective purchasers.

The valuation of these interests is conceptually the same as any other valuation. The practical difficulties will be more difficult because there are more variables.[621] However, the courts must attempt to place a valuation on these interests. Discretionary trusts were invented to obscure interests and expectations[622] but the as the Privy Council has said, the inclination to let that lack of transparency prevent discretionary beneficiaries enforce the trusts must be resisted.[623] The same principle suggests that courts should not give in to the inclination to avoid placing a value on the interest. The case of *Kachur v Kachur* shows how this can be done.

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[621] Shelley Griffiths "Valuing 'Bundles of Rights' for the Property (Relationships) Act 1976: When Neither Art nor Science is Enough" (2011) 7 NZFLJ 98 at 101.

[622] *Schmidt v Rosewood Trust Ltd* [2003] UKPC 26, [2003] 2 AC 70 at [34].

[623] *Schmidt v Rosewood Trust Ltd* [2003] UKPC 26, [2003] 2 AC 70 at [36].

CONCLUSION

This thesis is primarily about one type of asset protection trust. It is about trusts where a discretionary beneficiary is given the right to replace the trustees. However, the implications of the arguments apply to all discretionary beneficiaries.

This thesis engages with the issue of the effect that these trusts have on areas of law outside of trust law. The controlling beneficiary does not have any property rights 'in' or 'attached to' the trust property but is in an advantageous position economically because he can both receive property by the trustee's decision and decide the identity of the trustee making that decision. The question for this thesis was whether or not the controlling beneficiary's position could be "property" as that term is used in these areas of law. The null hypothesis was that these positions were of such a nature that they could not be included within "property". If the null hypothesis was correct then controlling beneficiaries would be in privileged economic positions but not be subject to the usual responsibilities of those who own property.

The thesis argument was divided into four parts. The first part concerned the meaning of "property". The second part was whether a discretionary interest could fit within that meaning. The third part was whether the controlling beneficiaries' right to replace the trustees could be property. The fourth part was how to value these interests, if they could be property. Each of these parts had a number of issues that had to be worked through if the thesis argument was to be successful.

The chapter on property started by selecting statutes where the term "property" was used and where a space in the existing remedies meant that the thesis argument would be significant. The issue was what meaning Parliament intended this term to convey. First, I concluded that there was an implicit assumption about property as a legal concept that it is limited to rights and interests that are recognised as legally significant. Second, in all the selected statutes Parliament's purpose in determining outcomes based on property was economic. Economic significance does not mean every instance of the interest must be valuable but only that the type of interest is capable of being valuable. Third, I concluded that the first two conclusions could be modified by the particular scheme that Parliament used that might exclude certain legally and economically significant interests from being property in a particular context. A significant feature here was whether or not the interest needed to be capable of being transferred independently of the legislation. My final conclusion was that these three considerations made up the threshold requirements to be met before an interest could be considered to be property under the selected statutes.

The conclusions in relation to the meaning of property were then applied to the discretionary interest. The first issue here was whether a discretionary interest could be legally significant in the present even though it is only an uncertain possibility of becoming

entitled to property in the future. I concluded that it was legally significant because the discretionary beneficiary has presently exercisable rights. The rights to due administration and consideration protect the possible realisation of the possibility of future entitlement and indicate it is legally significant in the present.

The second issue was whether the discretionary nature of the possibility – the fact that it depended on the active decision of another party – meant that it could not qualify as property. This quality of the discretionary interest pushed it close to the line between interests that are legally recognisable and those that are not, however, the comparison with other interests that were also subject to discretions but recognised as legal interests demonstrated that this was not determinative. I concluded that the discretionary interest was legally significant enough to be property despite being subject to a discretion.

The third issue was the economic significance of the discretionary interest. Because the interest is only a possibility it is inherently uncertain. In some contexts such as taxation uncertainty may mean that the interest is not considered to be economically significant. However, in the contexts selected in this thesis certainty in estimating economic value is not a necessity. I concluded that a discretionary interest could be recognised as economically significant and had been recognised as such in a number of cases. I also concluded there was no causal disconnection between the right to due administration and the eventual receipt of property because this right was only a part of the larger discretionary interest, which was essentially the possibility of receiving that property.

The fourth issue was how well discretionary interests fit within the specific statutory schemes. The question here was whether discretionary interests could be transferred. I concluded that they likely could not be transferred by the holder under the current law, which meant that they would be excluded from being property under some of the selected legislation: the High Court Rules, the Family Protection Act 1955 and the Law Reform (Testamentary Promises) Act 1949. However, the Property (Relationships) Act 1976 and the Insolvency Act 2006 have mechanisms that mean an interest does not need to be transferable by its owner to be property. Therefore, discretionary interests can be property under these statutes. This conclusion applies all discretionary beneficiaries, including settlor-beneficiaries, not just controlling beneficiaries.

The fourth chapter concerned the right to replace trustees. Here the first issue was whether the fact the right was a Hohfeldian power meant it could not be property. This issue was determined by a series of precedents that have held powers are not conceptually distinct from property. The second issue was whether the right was bound by fiduciary duties to the beneficiaries. If the right was so bound then it could not be exercised by the controlling beneficiary in her own interest. I concluded that the answer to this question would depend on the facts of the individual case as the imposition of fiduciary duties depended on the settlor's intention in granting the right. It appeared that an intention to impose such a duty would be unlikely to be found where the right was given to a discretionary beneficiary. A related

question was whether or not the right to appoint a trustee, who has fiduciary duties, could ever be property. The issue here was whether recognising this right as property would be tantamount to sanctioning a breach of trust. I concluded that no breach of trust needed to be implicated in such a relationship. The right to replace the trustee is conceptually the same as a right to replace directors that is held by shareholders and is an integral part of the property in a share.

The final part of the argument was valuation. The issue here was whether the principles of valuation could be applied to discretionary and controlling interests. My conclusion was that there was no conceptual difficulty with this process. Valuation involves estimating the future cash flow from a particular interest and factoring in uncertainties. Although the uncertainties in relation to these interests may be significant, and the estimates not as accurate as for other types of interests, valuation of them is not impossible. Two important principles of valuation in New Zealand which are sometimes overlooked are that the value of the interest to the owner of the interest can be taken into account and that the owner is assumed to be a rational self-interested, utility-maximizer.

The case *Genc v Genc*,[624] as used in the introduction, can be used again as an example of how the thesis argument would work in practice. Mr Genc was a controlling beneficiary of the trust he settled prior to his marriage to Mrs Genc. Under the Property (Relationships) Act 1976 "property" is not restricted to interests 'in' or 'attached to' the trust property so the fact that Mr Genc had no present entitlement to any of the trust property is irrelevant. He had a possibility, as a discretionary beneficiary, of becoming entitled to property and benefits in the future. He would become entitled if he and his solicitor agreed as trustees to distribute a benefit to him. The economic significance of this possibility was more than theoretical; the trustees let Mr Genc live in the house and operate his former business. Mr Genc's discretionary interest ought to have been included as property under this Act.

Mr Genc also had the right to replace the trustees. Because Mr Genc gave himself this right when establishing the trust it is unlikely that he intended his exercise of the right to be restricted by fiduciary duties to any of the other beneficiaries. It is unlikely that the other beneficiaries could legitimately expect Mr Genc to exercise the right in their favour and in exclusion of his own interest. The fact that Mr Genc's right was to appoint a new trustee who would have fiduciary duties to the beneficiaries does not mean the exercise of the right would involve a breach of trust. If Mr Genc did abuse this right by appointing someone to act in breach of trust then Mr Genc would be liable as a knowing assistant. Mr Genc could exercise the power to alter the likelihood that he received property but not to override the trustee's duties. This right could also be property.

These two interests could be valued. Their value would need to take into account the value they had to Mr Genc. Together the value of these interests would be high. It would be

[624] *Genc v Genc* [2006] NZFLR 1119, 26 FRNZ 67 (HC).

possible to estimate how likely it was that Mr Genc would receive benefits from the trust in the future and the likely value of those benefits. From that baseline it would also be possible to estimate how much Mr Genc could increase the value of that estimate by replacing his solicitor with a trustee who was more likely to prefer Mr Genc's interests to the other beneficiaries. As the assumption is that Mr Genc is a rational, self-interested, utility-maximiser the valuation would assume that Mr Genc would do whatever he was legitimately able to do to maximise the benefit he received from the trust without compromising the trustee's duties. This means that any gratuitous intention Mr Genc had to benefit his children or other relatives would have to be ignored for the purposes of the valuation. However, the value of the controlling interest would have to be somewhat discounted from the value of the trust property to account for the fact that all replacement trustees would have to consider the interests of the other beneficiaries as well as Mr Genc.

Mr Genc acquired his interest prior to his relationship so it would have initially been separate property under the Property (Relationships) Act 1976.[625] However, Mrs Genc would have had a claim against this separate property under s 9A of the Act if her contributions or application of relationship property had contributed to any increase in its value. It is possible that Mrs Genc's contributions did do this because she worked in the trust business and contributed domestically enabling Mr Genc to work in his business.[626] If the trust business increased in value then Mr Genc's controlling interest would also increase in value because the estimated future cash flow from his position as controlling beneficiary would increase as well. Mrs Genc could have claimed this increase in value upon separation.[627] The result would have left Mrs Genc with some avenue to compensation but would not equal her claim if the trust did not exist because Mr Genc's interest as beneficiary could not be classified as a family home.

This thesis has important implications for the use of asset protection trusts in New Zealand. The first implication is that the argument presented in this thesis will not eliminate asset protection strategies or attempts to avoid the consequences of legislation that determines outcomes based on ownership of property. There will always be a grey area if ownership and responsibility for property is sufficiently vague. However, the argument will eliminate the current perception that asset protection trusts allow people to both protect their property and have enjoy the benefit of it as and when they wish. The purpose of asset protection trusts with controlling beneficiaries is to allow the beneficiaries the comfort and certainty that their needs will be met from the trust. The implication of this thesis is that the more material certainty and comfort a person has, the more likely it will be that they have property with which they are obliged to satisfy their responsibilities to others.

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[625] Property (Relationships) Act 1976, s 8-9.

[626] *Rose v Rose* [2009] NZSC 46, [2009] 3 NZLR 1.

[627] Property (Relationships) Act 1976, s 9A.

The second implication of this thesis is that, unlike the extension of a direct remedy, it does not disrupt the many thousands of trusts in New Zealand. The argument it contains does nothing to alter the duties and powers of trustees. It only affects the duties and responsibilities of discretionary beneficiaries. However, it will disrupt many thousands of beneficiaries' expectations of their trusts. Those beneficiaries who expect a trust to protect their assets while they remain in an economically advantageous position will be disappointed. On the other hand, those beneficiaries and settlors who expect their trust to provide a convenient and flexible means of passing assets to later generations will not be affected.

The third implication is that legislative intervention in this area may not be necessary – at least in relation to the external issue with asset protection trusts.[628] In my opinion, the argument presented in this thesis is a flexible and nuanced remedy to the unfairness caused by asset protection trusts. Unlike the remedies that allow trust property to be directly removed from trusts it does not disrupt people's private ordering of their own affairs. Further, it is guided by established principles of statutory interpretation and valuation. In contrast the Law Society has proposed a much vaguer remedy in the relationship property context for the courts to be able to ignore trusts depending on "whether it would make sense for a trustee to say 'no' to the person holding the real power".[629] This sort of development is entirely novel and likely to be more arbitrary than the argument presented here as there are no clear principles to guide its application.

The research in this thesis raises a number of related issues that would be worth investigating. These issues are either tangential to this thesis or there was not enough space to engage with them.

The legal position of those who are appointed both trustees and discretionary beneficiaries needs clarification. For example, Mr Genc was nominated as a trustee in the deed and in that position was given the power to benefit himself to the exclusion of all of the other beneficiaries. However, it is questionable whether Mr Genc was in fact subject to the fiduciary obligations of a trustee. As trustee he had the power, jointly with the other trustee, to give himself all of the trust property. This means that Mr Genc could not be said to be under an obligation to use the trust property to benefit others and to the exclusion of his own interest. A question worth investigating is whether a duty to *consider* benefiting others in preference of oneself is sufficient for a trust obligation.

Another area that could be worth investigating is the effect of other rights that are commonly given to beneficiaries. For example, rights to add extra discretionary beneficiaries

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[628] Legislative or judicial intervention would be necessary if it was considered that the existence of controlling beneficiaries or settlor-beneficiaries needed to be reformed. The Law Commission is investigating this issue as part of its review of trust law. Legislative reform could follow or it is possible that the courts could intervene under the inherent jurisdiction over the administration of trusts, although this is less likely.

[629] Submission by Andrew Gilchrist to the Law Commission regarding *Some Issues with the Use of Trusts in New Zealand: Review of the Law of Trusts Second Issues Paper* (NZLC IP20, 2010) (3 May 2011) at 17 [available at <http://www.lawsociety.org.nz/publications_and_submissions/submissions>]).

or to make existing discretionary beneficiaries ineligible to benefit or requirements that trustees obtain beneficiaries' consent.

One area that was not able to be explored in this thesis was jointly held rights. Often the right to replace trustees is held jointly by a couple who set up a trust together. Usually jointly held interests can be severed in equity like any other jointly held property. However, there is precedent that suggests that jointly held powers might not be treated like other jointly held property. Although, in my opinion, these precedents are unlikely to survive the recent acceptance that powers are not conceptually distinct from property this needs to be investigated further.

APPENDIX A: DATA ON TRUST INCOME TAX RETURNS

The data for Figure 1 in Chapter One was mostly obtained from publicly available data on the websites of the Australian Tax Office,[630] the Inland Revenue Department,[631] HM Revenue & Customs,[632] Statistics New Zealand,[633] the Australian Bureau of Statistics[634] and the Office for National Statistics.[635] The data on New Zealand Trust and Estate income tax returns was supplemented for the years 1994 to 2000 by data supplied by the Inland Revenue Department under an Official Information Act 1982 request.[636] The data is set out in the following tables:

Trust and Estate Income Tax Returns			
Date	New Zealand[637]	Australia[638]	United Kingdom[639]
March 1994	92,800*	-	-
March 1995	101,800*	-	-
March 1996	103,400*[640]	-	-
March 1997	112,900	-	-
March 1998	123,900	-	-
March 1999	131,900	-	-
March 2000	147,000	-	-
March 2001	164,700	447,625	-
March 2002	177,800	455,980	-

[630] www.ato.gov.au

[631] www.ird.govt.nz

[632] www.hmrc.gov.uk

[633] www.stats.govt.nz

[634] www.abs.gov.au

[635] www.ons.gov.uk

[636] Letter from Sandra Watson to Tobias Barkley regarding the number of tax returns filed by trusts and estates for the years 1990-2000 (23 April 2012, Obtained under Official Information Act 1982 Request to the Inland Revenue Department).

[637] Inland Revenue Department – Number of IR6 Trust or Estate Income Tax returns filed for the preceding income year.

[638] Australian Tax Office – Number of Trust Income Tax returns filed for the preceding income year.

[639] HM Revenue & Customs – Number of Trust and Estate Full Assessment Returns Table 13.1.

[640] Data for the years 1994 to 1996 is based on an 11% sample which has been scaled up. It also excludes returns which were filed more than two years late (Letter from Sandra Watson to Tobias Barkley regarding the number of tax returns filed by trusts and estates for the years 1990-2000 (23 April 2012, Obtained under Official Information Act 1982 Request to the Inland Revenue Department)).

March 2003	192,300	470,945	-
March 2004	205,400	501,860	-
March 2005	219,500	533,268	-
March 2006	223,100	569,593	210,000
March 2007	239,200	609,915	203,500
March 2008	239,700	660,324	200,500
March 2009	236,900	663,392	193,000

Estimated Resident Populations			
Date	New Zealand[641]	Australia[642]	United Kingdom[643]
1994	3,611,400		
1995	3,663,700		
1996	3,723,400		
1997	3,775,200		
1998	3,811,200		
1999	3,833,000		
2000	3,855,900		
2001	3,876,900	19,360,200	-
2002	3,935,700	19,605,300	-
2003	4,013,300	19,846,800	-
2004	4,078,700	20,083,700	-
2005	4,126,600	20,338,600	-
2006	4,176,100	20,637,900	60,584,300
2007	4,222,700	20,988,500	60,985,700
2008	4,263,600	21,397,300	61,398,200

[641] Statistics New Zealand, Infoshare,Table: Estimated Resident Population by Sex (1991+) (Annual-Mar) (Estimated population as at March of the stated year).

[642] Australian Bureau of Statistics – Australian Demographic Statistics, Table One, Estimated Resident Population, Catalogue 3101.0 (Estimated population as at March of the stated year).

[643] Office for National Statistics - Table A Mid-1971 to Mid-2010 Population Estimates: total persons for United Kingdom and constituent countries; estimated resident population.

2009	4,305,700	21,859,300	61,792,000

One potential confounding factor in comparing the data from Australia is that the Australian Tax Office only reports income tax returns by trusts not estates. However, there is no difference because executors of deceased estates in Australia must file trust tax returns.[644] The data from the United Kingdom includes returns from estates. All jurisdictions include returns from charitable trusts.

There are two more important confounding factors. The first is that this data includes all types of trusts. It includes fixed trusts, family trusts, asset protection trusts and charitable trusts. The change in incidence of trusts in the last decade cannot be attributed to asset protection trusts as it could be partially or completely due to changes in the quantity of other types of trusts. The second is that this data does not include all trusts. It only includes trusts that report income to taxation authorities. There are estimated to be many thousands of trusts in New Zealand that hold assets that do not earn income, for example, a residential home that beneficiaries are allowed to live in rent free.[645]

[644] See www.ato.gov.au under Tax Topics A-Z > Deceased Estates > Taxation of the Deceased Estate.

[645] See See Law Commission *Some Issues with the Use of Trusts in New Zealand: Review of the Law of Trusts Second Issues Paper* (NZLC IP20, 2010) at [2.1]-[2.7].

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