TRUSTS & ESTATES LAW

Changes are on the way for trusts ...

By Anthony Grant, Trusts & Estates Litigator

After decades of inaction, the law of trusts is coming under the legislative spotlight.

There are three developments:

1. the Trusts Bill has been introduced into Parliament;
2. the Law Commission has produced its report on the review of the *Property (Relationships) Act 1976* (PRA); and
3. the Tax Working Group is currently preparing proposals for a comprehensive Capital Gains Tax (CGT) that will apply to, among other assets, trust-owned property.

I understand that, if a CGT is enacted, it is likely that family homes owned by trusts will be subject to CGT, whereas homes owned by individuals will not be. As many trusts are created for the primary purpose of protecting the family home, the attraction of trusts for this purpose will diminish.

What of the Law Commission's proposals for trusts?

The major change is a proposal that section 44C of the PRA should be enlarged "to provide a single, comprehensive remedy that will enable a court to grant relief when a trust holds property that was produced, preserved or enhanced by the relationship".

If this change is enacted, the devices that the courts have been using to access relationship property that has ended up in trusts will survive, but may not be needed. I refer, for example, to the bundle of rights "doctrine", the sham trust doctrine, the illusory trust theory, and the liberal use of constructive trusts.

A second major change that the Law Commission proposes is the abolition of section 182 of the *Family Proceedings Act 1980*. This is the section that started life in the mid-19th century and which is now interpreted as allowing the courts to modify "nuptial settlements" (a term which the courts interpret to include trusts) in any way that the courts like.

This provision applies to couples who have been married or who have had a civil union, but not to people in de facto relationships. The section is rightly regarded by the Commission as a "relic from the past" which ought to be repealed.

One of the intentions of an enlarged section 44C is to enable the courts to provide relief where trust property has been "preserved" or "enhanced" by relationship property or relationship labour. This includes the property of trusts settled by third parties.

If parents settle assets on a trust of which their children are beneficiaries, and the children preserve or enhance the value of the assets, the trustees will be liable to compensate them.

The law of constructive trusts can be used to achieve this purpose at present. Parents who make trust property available to their children and who don't want to face such claims are well-advised to ensure that, before the children gain access to the trust's assets, they provide a written disclaimer in which they say that, in return for access to the assets, they will not make any claim of a constructive trust.

Whether such a disclaimer would be effective in relation to claims of that nature that are made under an enlarged section 44C is another matter.

When Parliament enacted the PRA, it recognised that the imposition of a standardised set of rules for dividing relationship property should be tempered by the ability for people to choose other arrangements that they consider to be more appropriate.

A major weakness with the current "contracting-out" regime is that it can be ignored by the courts if enforcement of the agreement would cause "serious injustice" because the agreement is considered to have "become unfair or unreasonable". This provision is inherently unfair as no one can have any certainty that a contracting-out agreement will be upheld by a court.

I know of people who are unable to have relationships of more than three years because of their concerns that a contracting-out agreement will be set aside. These are people who have substantial wealth. No civilised government should enact laws that prevent people from being able to live in productive relationships, but our law does exactly that.

Unfortunately, the Law Commission makes no proposals for imposing a test that is substantially higher than the lowly "unfair and unreasonable". In fact, it goes the other way and proposes that such agreements can not only be set aside if a judge considers they have "become unfair or unreasonable", but they can be set aside if it is considered to be "in the best interests of any minor or dependent children".

Will the Law Commission's proposals be enacted? Parliament has generally been unwilling to turn the Commission's recommendations into law but, in the present case, the extent of public consultation that has gone into this report suggests that there should be a greater prospect of parliamentary adoption than is usual with such reports.

One outcome of the proposals may be an increased awareness of the need for people who disagree with the proposed changes to draw up contracting-out agreements that reflect the alternative arrangements for property that they prefer.

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