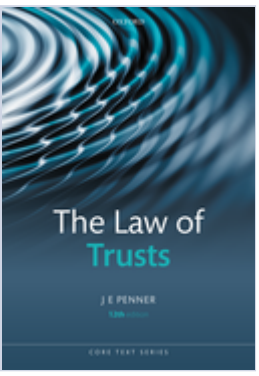

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J E Penner

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4. Modern discretionary trusts

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Abstract

Titles in the Core Text series take the reader straight to the heart of the subject, providing focused, concise, and reliable guides for students at all levels. This chapter focuses on modern discretionary trusts (MDTs), in which property is typically distributed by way of powers of appointment, not by the trustees' distributing property under fixed or discretionary trusts. It identifies common features of MDTs, including letters of wishes and protectors. Next, doctrinal developments which contributed to the development of the MDT are considered. Following that, the standing of objects to enforce the MDT and rights to information are examined. Finally, broader issues concerning how MDTs fit in with the broader law of trusts are taken in turn: MDTs and the law of charities; determining the 'true intended beneficiaries'; *Saunders v Vautier* issues; the status of letters of wishes, and MDTs as 'chameleon trusts'.

Keywords: powers of appointment, discretionary trusts, protectors, letters of wishes, certainty of objects, locus standi, beneficiaries' rights to information, charities, Saunders v Vautier

Summary

Foundations

4.1 Trusts like those in Examples 1 to 4 in **Chapter 3** (**3.1**) are still created, but there is an important modern trend moving away from settling those kinds of trusts. Having examined them and the law governing them, we are now in a position to begin our examination of the modern wealth management discretionary trust, or MDT (modern discretionary trust) for short. Such trusts typically have the following features:

- An initial trust of income and capital, with an intermediate power to add to or delete from the class of income beneficiaries. The capital beneficiaries will often be termed 'default', 'residuary', or 'final' beneficiaries;
- A power or a duty to accumulate income (**3.18**);
- Extensive powers, sometimes called 'overriding powers' to apply up to the entire income or capital for the benefit of members of the class of income beneficiaries;
- A period for the duration of the trust is set out (**3.85**), typically the longest period allowed by the law governing the trust, but it will be made clear that the trust may be brought to an end at any time prior to the end of the trust period by the trustee exercising powers to distribute all the trust assets;

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- Typically, the trust will be accompanied by a 'letter of wishes', a document prepared by the settlor and given to the trustees, the purpose of which is to give non-legally binding guidance to the trustees on the exercise of their very extensive discretions;
- Possibly, and perhaps these days typically, the trust instrument will provide for the office of 'protector', who will possess more or less extensive powers in relation to the trustees' exercise of their discretions.

4.2 Here is a simplified example of such a trust.

Example 5

'Beneficiaries'

1. *The 'Beneficiaries' means*
   (i) *Unless removed under (iii) below the children and descendants of the settlor, and their spouses, widows, and widowers (whether or not remarried);*
   (ii) *Any person, other than the Trustee or the settlor, nominated by the Trustee in writing.*
   (iii) *During the Trust Period the trustees may at any time in writing remove any person who is a beneficiary under (i) or (ii) above, though any such person removed under this clause may at any later time be nominated as a beneficiary under (ii) above.*

'Trust Income'

2. *Subject to the 'Overriding Powers' below:*
   (i) *The Trustees may accumulate the whole or the part of the income of the Trust Fund during the Accumulation Period. That income shall be added to the Trust Fund.*
   (ii) *The trustees shall pay or apply the remainder of the income to or for the benefit of any Beneficiaries, as the Trustees think fit, during the Trust Period. 'Overriding Powers'*

'Overriding Powers'

3. *Power of Appointment*
   (i) *The Trustees may appoint that they shall hold the whole or any part of the Trust Fund for the benefit of any Beneficiaries on such terms as the Trustees think fit.*
   (ii) *An appointment may create any provisions and in particular discretionary trusts and or dispositive or administrative powers exercisable by any person.*
   (iii) *An appointment shall be made by deed and may be revocable or irrevocable.*
4. *Transfer of the Property to a new settlement*
   (i) *The Trustees may declare by deed that they hold any Trust Property on trust to transfer it to trustees of a Qualifying Settlement, to hold on the terms of that Qualifying Settlement, freed and released from the terms of this Settlement.*
   (ii) *A 'Qualifying Settlement' means any settlement, wherever established, under which every person who may benefit is (or would if living be) a Beneficiary of this Settlement.*

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5. *Power of Advancement*

   The Trustees may pay or apply any Trust Property for the advancement or benefit of any Beneficiary.

'Default Clause'

> 6. *Subject to the provisions 1 to 5 above, the Trust Fund shall be held on trust for such charitable objects and in such amounts as the Trustees shall in their absolute discretion think fit. [Clauses of this kind are found, eg, in Millar v Millar (2018), [6]; Foreman v Kingstone (2004), [87].]*
>
> ***'Trust Period'***
>
> 7. *The Trust is to continue for a maximum period of 125 years (the Trust Period), and shall be determined and the Trust Fund and all property of the Trust distributed not later than upon the expiry of the Trust Period, or in the alternative shall be determined and distributed to one or more of the Beneficiaries at such earlier time as the Trustees in their absolute and uncontrolled discretion shall decide.*

4.3 The first thing to notice about the terms of this trust is that those named as 'Beneficiaries' are not objects of the trust of the capital at all; the capital beneficiaries, those entitled to the trust property unless the powers of appointment found in clauses 3, 4, and 5 are exercised, are found in clause 6, the so-called 'Default Clause'. Clause 6 is a discretionary trust for charitable objects. As we will examine in detail in **Chapter 18**, besides trusts for persons, the law allows trusts for charitable purposes. Under the discretionary trust of capital in clause 6, the trustees have a discretion to devote the capital to charities of their choice.

4.4 As regards to being objects of a trust, the 'Beneficiaries' are objects only of the trust of income in clause 2(ii), although even here under clause 2(i) the trustees can decide not to pay them any income, but to accumulate it instead and add it to the capital. So, if the beneficiaries are to receive any capital, they will receive it as objects of the powers of appointment given in clauses 3 to 5. On the other hand, under this form of modern trust, it is fully intended and expected that all the capital will be distributed under clauses 3 to 5; the charities are expected to get nothing. Another version of this form of trust can be found as an appendix at the end of the NZSC decision *Clayton v Clayton* (2016), in which two different but overlapping classes of 'Discretionary Beneficiaries' were set out, the trustee having powers to appoint both income and capital prior to the 'Vesting Day' to the first class, and upon the Vesting Day to distribute the assets under a discretionary trust to the second class.

4.5 To summarise, then, under this form of trust, the main way in which property will be distributed is by way of powers of appointment, not by the trustees' distributing property under fixed or discretionary trusts. Why would a trust be structured in this way, with essentially 'dummy' capital beneficiaries (the charities which will likely receive nothing), and all capital distributions made by way of powers of appointment? While certain tax considerations have played their part (see Nolan (2017), 152–154), the main reason is maximum flexibility. What this form of trust does is that it creates a class of objects, which can be expanded or contracted at will (clause 2(ii) and (iii)), and the provisions for distribution of both income and capital give the trustees an unfettered discretion to appoint as much or as little as they want to the clause 2 'Beneficiaries'. The
p. 82 trustees are expected to hold onto the fund of assets so long as they think it best to do so, distributing income or capital from time to time to the 'Beneficiaries', but when the time is right (eg all the infant beneficiaries have grown up and act responsibly) and definitely before the end of the 'Trust Period' when the capital beneficiaries under the Vesting Day and Default Clauses would become entitled, they will distribute all the

capital amongst the income beneficiaries by the exercise of the 'overriding' powers of appointment, bringing the trust to an end. Because of these features Lionel Smith calls these 'massively discretionary trusts' (Smith (2017)).

Letters of wishes

4.6 Because of the wide discretions given to the trustees of an MDT, it is very common for settlors of MDTs to provide the trustee with a 'letter' of wishes. The purpose of the letter is to provide guidance to the trustee in exercising those discretions, in particular its dispositive (**3.3**) discretions. The letter is almost invariably expressed not to be legally binding upon the trustees, (though the effect of the letter is always a matter of construction (**5.69**, *Chen v Ling* (2000)), so in principal they can decide whether or not to follow the guidance). It would seem, though there is no decisive case law on this, that the trustee should be legally bound at least to consider it (Lewin (2020), [21-066]). Even so, the discretions remain the trustees', and they must use their own judgement in exercising them, and certainly not slavishly follow the letter of wishes. Letters of wishes are also normally expressed to be confidential as between the settlor and trustee, and so may not normally be disclosed to the objects of the trust.

Protectors

4.7 There is nothing in theory to prevent a settlor from giving extensive dispositive and administrative duties and powers to non-trustees (see Nolan (2018)), but for obvious reasons this is a dangerous thing to do if they are given to named individuals. Those named individuals may perish, or be otherwise uncooperative, and so a settlement that runs smoothly only if named third parties do their job is a precarious one. This, in general, is why most of the powers and duties needed to make the trust run are given to office holders, ie the trustees.

4.8 However, in the last 40 years or so, a new animal has appeared, the 'protector', whom we have already encountered (**3.39**). As the name suggests, protectors monitor the trust, and by the exercise of powers given to them under the trust, it is hoped that they can 'protect' the trust (ie ensure that its administration by the trustees is up to the expected standard and in keeping with the settlor's original purposes for setting it up). The protector's powers may be more or less extensive, but they typically include powers to give or refuse consent to the trustee's exercise of various of its powers and discretions.

4.9 As a default, the protector should normally be regarded as a 'quasi-trustee', who is a fiduciary toward the beneficiaries (the Jersey Royal Court has affirmed this in a number of decisions: *In re Frieburg Trust* (2004); *Re the Representation of Centre Trustees (CI) Ltd* (2009); *In re A and B Trusts* (2012), and see Nolan (2016), 480–83), although in principle the trust instrument might specify or be construed such that the powers are merely personal, or that the protector holds them as fiduciary powers in favour of the settlor, to be exercised in the settlor's best interests (which raises the interesting question of whether this makes the settlor a beneficiary of some kind (and what kind?) under the trust). If there are provisions for a replacement protector, that strongly indicates that, like a trustee, the protector holds an office, and that the powers are held in a fiduciary capacity.

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Nevertheless, this will not invariably be so. In JSC *Mezhdunarodniy Promyshlenniy Bank v Pugachev* (2017), the court found that on the facts of the case, the powers given to the settlor, though in his position as a 'protector' of the trust, were not fiduciary, and he held those powers to use as selfishly as he wished for his own interests.

4.10 In some jurisdictions, trust legislation contains provisions concerning protectors (eg Bahamas Trustee Act 1988, ss 2, 81–83), but where this is not the case, as in England, the effect of the grant of such powers and possibly duties must be determined by the court interpreting the terms of the trust (see further Waters (1996); Matthews (1995c)).

4.11 We must now examine two related doctrinal developments which contributed to the development of MDTs.

McPhail v Doulton and the certainty of objects test

4.12 Up until the decision of the HL in *McPhail v Doulton* (1971) it was a fairly simple matter to distinguish between the way in which the court would enforce the trustees' compliance with a discretionary trust and the way in which it would oversee the exercise of powers of appointment. In the case of both, any distribution in violation of the terms of the trust or power, ie any misfeasance, would be invalid. The chief difference lay in the effects of *nonfeasance*. With respect to discretionary trusts, if the trustees failed to exercise their discretion and distribute the property, the court would order a distribution. Before *Kemp v Kemp* (1795), the court would, in rare cases, exercise the trustees' discretion itself to distribute the property unequally to the objects, but following that decision the practice became to apply the maxim 'Equality is equity' and distribute the property equally amongst them. In the case of powers, by contrast, the case of nonfeasance presented no problem. There was no duty for the court to enforce.

Certainty of objects

4.13 What changed in *McPhail* was the test of certainty that applied to the objects of discretionary trusts. Normally, much of what follows is covered in trust books in the chapter on 'Certainty' (in this book, **Chapter 5**), but I included it here because it concerns the enforceability of discretionary trusts and powers, and the rights of the objects under them, more than it does certainty per se. Certainty of objects is a requirement of both trusts and powers, and means nothing more than that the terms of the trust or power have to indicate with sufficient precision who is in the class of objects.

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The 'complete list' test and the 'is or is not' test

4.14 The historical test for certainty of objects for trusts, whether fixed or discretionary, was that, for a trust to be valid, one had to be able to draw up a complete list of the objects. In a discretionary trust for the settlor's children, for example, this could be easily accomplished since it was clear that the class of objects comprised the settlor's children and no one else. Whether or not the 'complete list' test was applicable to mere powers of appointment was not clearly established until *Re Gestetner Settlement* (1953). The power in question was a power to appoint property to a large and fluctuating group of objects including the settlor's former employees

and their surviving spouses. As with many of the cases that followed, the trust was essentially a private pension trust, created by a rich industrialist prior to the extensive regulation of occupational pension schemes.

4.15 It was held that the power was valid even though a complete list of the possible objects of the power could not be drawn up at any one time. Harman J stated (at 688):

> *[T]he document on its face shows that there is no obligation on the trustees to do more than consider—from time to time, I suppose—the merits of such persons of the specified class as are known to them and, if they think fit, to give them something ... I cannot see [that] such a duty [makes] it essential for these trustees, before parting with any income or capital, to survey the whole field, and to consider whether A is more deserving of bounty than B ... there is no difficulty ... in ascertaining whether any given postulant is a member of the specified class. Of course, if that could not be ascertained the matter would be quite different, but of John Doe or Richard Roe it can be postulated easily enough whether he is or is not eligible to receive the settlor's bounty.*

4.16 Thus was born the 'is or is not' test for certainty of objects: since the power holder has no duty to distribute the property, all that matters is misfeasance, ie if he appoints property at all, he must be sure to appoint only to those within the class of objects and not those outside it; all he need know with certainty is whether any particular person is within the class or not; in particular he does not need a complete list of all objects who are eligible to receive.

4.17 In *IRC v Broadway Cottages Trust* (1955), the CA had to decide whether the same test should apply to a discretionary trust for a similarly large and fluctuating class including the settlor's employees and their wives and widows. In summary, the arguments against the 'is or is not' test, and in favour of the 'complete list' test, were these: starting from the principle stated by Lord Eldon in *Morice v Bishop of Durham* (1805) that in order to be valid, a trust must be one that the court can control and execute, various factors made the court's control and execution of such a trust impossible. We can look first at the arguments against.

4.18 One objection is 'conceptual' in the sense that it contravenes the concept or logic of the trust. It concerns the nature of the obligation owed by the trustees to the beneficiaries: the trustee must know or be able to ascertain all the objects whom he might select, otherwise he is merely selecting from *some* members of the
p. 85 class, in which case he is not carrying out the terms of the trust, ie to exercise his discretion to select from amongst *all* of the objects. In other words, the settlor has set the trustee an impossible task, and so the trust must fail.

4.19 Second, but along the same lines, in the absence of a complete list only a subset of the whole class can be identified and a subset only of all the beneficiaries cannot in principle 'claim execution of the trust' because the trustees have no duty to distribute to any subset of the whole class; as a result, where the whole class of objects cannot be identified the trustees' duties are 'illusory'.

4.20 Finally, it is not at all clear in such a case that the beneficiaries as a group are genuinely together entitled to the trust assets; there clearly is no possibility for them together to call for the trust property under the principle in *Saunders v Vautier* (1841), since not knowing who they all are, they cannot act together under the rule.

4.21 The other arguments against the trust were essentially practical, regarding the role of the court in its ability to execute the trust if the trustees failed to do so, a possibility that, on principle, could not be ruled out. In particular, the court had no power to mend the invalidity of a trust of this kind by imposing an arbitrary distribution amongst only some of the whole unascertainable class; to create a certain class to replace the uncertain one chosen by the settlor would amount to imposing a different trust.

4.22 The essence of the argument in favour of the 'is or is not' test is that no practical difficulty in effectively controlling the execution of the trust would arise.

- Having undertaken the trust, the trustees can be assumed to be willing and able to carry it out.
- With respect to malfeasance by the trustees: the 'is or is not' test allows the trustees to ensure that only qualified beneficiaries take benefits, and so the trustees can distribute within the terms of the trust. Conversely, distribution to non-objects can be determined with certainty, and could be restrained by the court on the suit of any qualified member of the class.
- With respect to nonfeasance by the trustees: at the suit of any object, recalcitrant trustees could be replaced, and this process could be repeated. 'The possibility that not only the original trustees but every set of trustees appointed in their place would fail or refuse to do this is so remote that it can, for practical purposes, be disregarded.' In the unlikely event this occurred, the court could declare a trust in default of distribution for a modified class of whose members a complete list could be made.

4.23 The trust failed. Jenkins LJ had this to say (at 35):

> *We confess to some sympathy for the appellants' argument, which has an attractive air of common sense, but we do not think that it can be allowed to prevail. We think the submissions ... to the effect that the trust is not one which the court could control or* ↵ *execute, and that this objection cannot be met by urging the improbability of assistance by the court ever becoming necessary, are well founded. We also agree that ... the court would not be executing the trust merely by ordering a change in trusteeship.*

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At this time, then, one important distinction between discretionary trusts and powers of appointment was their respective tests for certainty of objects, which directly reflected the court's consideration that discretionary trusts, being trusts, required possibilities of precise enforcement in the case of nonfeasance which did not apply to powers of appointment.

McPhail v Doulton

4.24 Thus, the matter stood until *McPhail v Doulton* (1971), which similarly concerned a discretionary trust for a large class comprising employees and ex-employees of a large company and their dependents and relations. Although about a year before the HL in *Re Gulbenkian's Settlement Trusts* (1970) had confirmed obiter that while

the 'is or is not' test was appropriate for powers, the complete list test remained the appropriate test for discretionary trusts, a different panel of their Lordships in *McPhail v Doulton* decided 3:2 that the 'is or is not' test was appropriate for discretionary trusts as well. The majority decision, given by Lord Wilberforce, essentially recognised the 'common sense' arguments put in *Broadway Cottages Trusts*, accepting that in practice trusts for large classes of beneficiaries could be adequately enforced.

4.25 Lord Wilberforce emphasised that the difference between the practical tasks facing trustees who held a mere power of appointment and those of trustees who held property on a discretionary basis was a matter of degree (at 449):

> *Any trustee [holding a mere power] would surely make it his duty to know what is the permissible area of selection and then consider responsibly, in individual cases, whether a contemplated beneficiary was within the power and whether, in relation to other possible claimants, a particular grant was appropriate. Correspondingly a trustee with a duty to distribute, particularly among a potentially very large class, would surely never require the preparation of a complete list of names, which anyhow would tell him little that he needs to know. He would examine the field, by class and category; might indeed make diligent and careful inquiries, depending on how much money he had to give away and the means at his disposal, as to the composition and needs of particular categories and of individuals within them; decide on certain priorities or proportions, and then select individuals according to their needs or qualifications. If he acts in this manner, can it really be said that he is not carrying out the trust? ... Such distinction as there is would seem to lie in the extent of the survey which the trustee is required to carry out; if he has to distribute the whole of the trust fund's income, he must necessarily make a wider and more systematic survey than if his duty is expressed in terms of power to make grants. But just as, in the case of a power, it is possible to under-estimate the fiduciary obligation of the trustee to whom it is given, so, in the case of a trust (trust power), the*
> p. 87 *danger lies in overstating what the trustee requires to know or to enquire ↵ into before he can properly execute his trust. The difference may be one of degree rather than of principle ...*

4.26 It is not, with respect, correct to assume that a trustee of a discretionary trust will have a wider survey to conduct than a trustee whose task is to consider exercising a power of appointment. The reverse is actually the case, for the interests of the objects of the power must be weighed against those who would take in default of appointment: the trustee therefore has two classes of objects to survey, not one. Of course, the width of the survey will vary on a case by case basis, depending on the size of the classes, the settlor's intentions in creating the trust and powers, and so on.

4.27 As regards the court's enforcement of the trust, Lord Wilberforce thought that no conclusions could be drawn from the fact that in large trusts of this kind, equal division was not a possible means of enforcement (at 456–457):

> *As a matter of reason, to hold a principle of equal division applies to trusts such as the present is certainly paradoxical. Equal division is surely the last thing the settlor ever intended; equal division among all may, and probably would, produce a result beneficial to no one.*
>
> *Rather, enforcement should be tailored to the particular trust or power, and the practicalities of the situation must be borne in mind: Assimilation of the validity test does not involve the complete assimilation of trust powers with powers. As to powers … although the trustees may, and normally will, be under a fiduciary duty to consider whether or in what way they should exercise the power, the court will not normally compel its exercise. It will intervene if the trustees exceed their powers, and possibly if they are proved to have exercised it capriciously. But in the case of a trust power, if the trustees do not exercise it, the court will; … the court, if called on to execute the trust power, will do so in the manner best calculated to give effect to the settlor's or testator's intentions. It may do so by appointing new trustees, or by authorising or directing representative persons of the classes of beneficiaries to prepare a scheme of distribution, or even, should the proper basis for distribution appear, by itself directing the trustees so to distribute.*

4.28 It should be borne in mind that *McPhail* does not appear to alter the traditional enforcement of discretionary trusts where the class of objects is small: if there are no clear indications as to how the trustee ought to exercise his discretion, the court will order an equal division amongst all the objects.

4.29 It is also to be noted that this line of cases is unlikely to be relitigated. As noted above, *McPhail*-like trusts were created by magnanimous industrialists to provide a kind of pension benefit to their employees, their employees' dependents, and so on, before the introduction of statutory pension schemes. Furthermore, at the time the validity of intermediate powers to appoint members to a class was not established, but had it been, the use of these powers would have obviated the problem these trusts posed. We could begin with a complete list of employees, as in clause 2(i) of Example 5, and if the trustees wished to appoint to individual
p. 88 others, like employees' spouses or dependents, they could just be appointed to the class of beneficiaries under a power like that in clause 2(ii). (As we shall see, whether the concept of 'relative' or 'relation' passes the 'is or is not' test of certainty is a trickier issue (**5.47** et seq)).

Objects' standing to enforce the trust and rights to information

4.30 As we have seen, Lord Wilberforce insisted that his judgment in *McPhail* did not 'assimilate' discretionary trusts and powers of appointment, and so one might conclude that the rights and duties of objects of discretionary trusts and objects of mere powers of appointment remained distinct. But it is not clear this is so in two important respects: first, whether the objects of trusts rather than objects of mere powers have different 'standing', or *locus standi* to use the Latin, that is rights to enforce the trust in court against the trustees, for example when trustees have allegedly done something improper; and second, the right against the trustees to information about the trust and the trustees' performance of their duties. It is to these issues we now turn.

Standing to enforce the trust

4.31 Prior to the rise in frequency of MDTs, there was a conventional understanding that whilst objects of fixed trusts had standing to enforce the trust obligations against the trustee, objects of mere powers of appointment did not. The standing of objects of discretionary trusts seems to be somewhat in between, but there is very little clear authority on the point; see Turner (2018), 247–250; for the position in Australia see Hudson (2021). The rationale for this conventional understanding is clearly stated by Smith ((2017), 22):

> *Objects of powers do not have any right to any property. Perhaps less obviously, they do not have a right to enforce the [trustee's trust obligations]. This is just saying the same thing in a different way, because the [trustee's trust obligations] [are] the obligation[s] relating to the benefit of the trust property, and by definition, [those] obligation[s] [are] owed to the beneficiaries ... and not to the objects of any discretionary powers. Or in other words, since objects of powers do not have any right to any trust property, they cannot enforce obligations owed by the trustees in relation to the benefit of the trust property.*

4.32 As we have already seen (**3.32**), objects of mere powers of appointment do have some minimal rights against the trustee. As Megarry VC put it (at 793) *Re Hay's Settlement's Trusts*, a case decided post-*McPhail*:

> *[T]he duties of a trustee which are specific to a mere power seem to be threefold. Apart from the obvious duty of obeying the trust instrument, and in particular of making no appointment that is not authorised by it, the trustee must, first, consider periodically whether or not he should exercise the power; second, consider the range of objects of the power; and third, consider the appropriateness of individual appointments.*

The question is whether these minimal duties owed to the objects of mere powers are significant enough to give these objects a general standing to enforce the trust, and prior to the rise of MDTs it was not clear that anyone thought so.

p. 89 **4.33** Indeed, the conventional understanding stated by Smith just above probably drove, in part, the development of trust structures like that in Example 5: settlors worried about their objects haranguing the trustees for benefits under the trust, or bringing actions against the trustees, would, on this conventional understanding, have given these objects no rights of enforcement, or relatedly as we shall now see no rights to be provided information by the trustees, such as the trust accounts (**2.21**) or other trust documents.

Beneficiaries' rights to information

4.34 The issue of standing almost always arises when an object brings an action against the trustee to require them to provide information about the trust, usually documents like the trust instrument, the trust accounts, and the letter of wishes if any (**4.6**). If an object has standing to enforce the trust, then obviously he would be in need of this sort of information to make that right to enforce the trust practically effective.

4.35 In *Armitage v Nurse* (1998), Millett LJ said (at 253):

> *If the beneficiaries have no rights enforceable against the trustees, there are no trusts.*

Remember that the settlor has no power to enforce the trust; it is the beneficiaries alone who are entitled to call the trustee to account in respect of his stewardship of the trust property. But the beneficiaries cannot enforce such a right if they have no information as to how the trustee has carried out the trust.

The right to be informed that one is a beneficiary

4.36 Beneficiaries of vested interests (certainly absolute vested interests) have a right to be informed of their interest (*Hawkesley v May* (1956)), and it is within the court's discretion in an appropriate case (namely where it is reasonable to assume that such beneficiary had a genuine likelihood or expectation that a dispositive discretion might be exercised in his favour) to require settlers to provide the names and addresses of trustees even to a discretionary beneficiary (*Re Murphy's Settlements* (1998)). In *Valard Construction Ltd v Bird Construction Ltd* (2018) the SCC held ([19]):

> *In general, wherever 'it could be said to be to the unreasonable disadvantage of the beneficiary not to be informed' of the trust's existence, the trustee's fiduciary duty includes an obligation to disclose the existence of the trust.*

In *Enright v Enright* (2019) the NZHC held ([198]) that the trustee's duty of disclosure extends to discretionary beneficiaries 'at least in the circumstances of a family trust'.

The right to see the trust accounts and other trust documents

4.37 Prior to that decision in *Schmidt v Rosewood Trust* (2003), which we shall examine below (**4.43**), it was generally accepted that beneficiaries, whether of a fixed or discretionary interest (*Chaine-Nickson v Bank of Ireland* (1976); *Spellson v George* (1987)), perhaps even of a contingent interest (*Armitage*, per Millett LJ, at 247),
p. 90 ie objects of a trustee's dispositive duty to distribute the trust property, were entitled to copies (made at their own expense) of the trust accounts. But they are only entitled to accounts in relation to their own interests under the trust. So capital beneficiaries with vested interests are entitled to see the trust accounts relating to the capital, but not to the way in which the trustee has dealt with the income. As Master Matthews put in *Royal National Lifeboat Association v Headley* (2016) ([14], emphasis original), what must be disclosed will:

> *depend on what is needed in the circumstances for the beneficiaries to appreciate, verify and if need be vindicate their own rights against the trustees in respect of the administration of the trust.*

4.38 However, in earlier cases the basis for these rights was not clearly established. From one perspective, the trust documents being trust property, the beneficiaries had a proprietary right to them, as they were the ultimate owners in equity of the trust property (*O'Rourke v Darbishire* (1920); *Re Londonderry's Settlement* (1965)). This is clearly misguided, because whether trust documents form part of the trust property or not, beneficiaries have no possessory rights to the trust property itself (**2.40** et seq); they merely have rights to whatever benefits of the trust property the trust terms dictate. The better view is that these rights flow from the beneficiaries' right to make the trustee account for his stewardship of the trust (*Hartigan Nominees Pty Ltd v Ridge* (1992); *Re Rabaiotti's 1989 Settlement* (2000)).

4.39 In line with this reasoning, in *Re the HHH Employee Trust* (2012) the Jersey Royal Court held that where the settlor of a pension fund trust had fiduciary powers under the trust to appoint new trustees and to appoint a protector, the court's general supervisory jurisdiction over trusts would allow it to require the disclosure of documents from this power holder to the beneficiaries.

4.40 In *Erceg v Erceg* (2017), the NZCA considered whether a bankrupt appellant had standing to seek disclosure of information relating to two discretionary trusts (he was within the class of beneficiaries of each of the trusts). The beneficiary's status as a bankrupt brought into question whether the right to seek disclosure was 'property' or a 'right in relation to property', which would have been vested in the Official Assignee pursuant to s 3 of New Zealand's Insolvency Act 2006. The Court of Appeal found that (at 333) it was unnecessary to consider whether the beneficiary's right to seek disclosure was 'property', because the appellant's standing to request disclosure of the documents derived from his 'status (or capacity) as a beneficiary of the Trusts.' Becoming a bankrupt did not alter or annul the appellant's status as a beneficiary, and it was that 'beneficiary status that entitles the appellant to have the trustees' duties to beneficiaries enforced, and to that end to request disclosure of trust documents by the trustees.'

Disclosure of the trustees' reasons for exercising dispositive discretions

4.41 Based on the case *Re Londonderry's Settlement* (1965), trustees are not required to disclose documents
p. 91 which reveal their reasons for exercising their dispositive discretions, eg giving more money to object X rather than to object Y. Danckwerts LJ provided the rationale for the rule as follows (at 935–936):

> *It seems to me that where trustees are given discretionary trusts which involve a decision upon matters between beneficiaries, viewing the merits and other rights to benefit under such a trust, the trustees are given a confidential role and they cannot properly exercise that confidential role if at any moment there is likely to be an investigation for the purpose of seeing whether they have exercised their discretion in the best possible manner.*

Salmon LJ added (at 937):

> *Another ground for this rule is that it would not be for the good of the beneficiaries as a whole, and yet another that it might make the lives of trustees intolerable should such an obligation rest upon them ...*

4.42 Along the same lines, in *Breakspear v Ackland* (2008), a case concerning the disclosure of a letter of wishes to beneficiaries, Briggs J emphasised that such wishes are normally expressed to be confidential (**4.6**), with the result that, in general, trustees had no obligation to disclose such letters to beneficiaries, nor give reasons for not doing so. But a new wrinkle has recently arisen. A beneficiary can apply for the information held by trustees under the Data Protection Act 1998, although in practice that may not result in the provision of much information; see *Dawson-Damer v Taylor Wessing LLP* (2020).

Schmidt v Rosewood Trust

4.43 *Schmidt* concerned a modern discretionary trust, and concerned a claim for rights to information, not from a beneficiary with a defined interest under the trust, but from an object of a mere power of appointment. The following two passages indicate the standing and right to information issues that can arise with these trusts.

4.44 More than 20 years ago in *Re T R Technology Investment Trust plc* (1998) Hoffmann J said (at 263–264, emphasis added):

> *It was a typical offshore trust and since a number of these trusts feature in these proceedings, it may be useful to describe their general characteristics. The named settlor is usually a stranger to the transaction who has been requested to lend his name to a document which records (in many cases truthfully) that he has provided a nominal sum as the initial trust fund ... The name of the person providing the assets subsequently added to the fund, whom I may call 'the real settlor', does not appear ... The trustees are given a wide discretion to pay income and capital to the beneficiaries, but the persons actually contemplated as beneficiaries are not necessarily named in the document. Instead, a local charity or some other person will be named and the trustee given a discretionary power to add to the list of beneficiaries ... Sometimes the*
> p. 92 *trustee will be given a 'letter of wishes' by the real settlor saying whom he wishes to benefit.*
>
> ↵ *Sometimes the real beneficiary, who may be the real settlor himself, will remain a matter of oral understanding between him and the trustee*. These trusts therefore reveal very little and depend upon trust and confidence reposed in the trustee to give effect to expectations and understandings which may not be legally enforceable. *The business of providing offshore financial services requires a reputation for probity, efficiency and discretion in executing such trusts in accordance with the confidential wishes of clients.*

4.45 One note about the 'nominal' versus the 'real' settlor issue. You might wonder why the identity of the real settlor is not on the trust instrument. The basic point is confidentiality, or secrecy. The idea is that if someone got their hands on a copy of the trust instrument, they would not be able to tell who the real settlor was. I have been told, but cannot verify, that one Guernsey fisherman has served as the nominal settlor for many, many trusts in that jurisdiction. The same confidentiality issue explains why the trust instrument will state that the sum settled is nominal, say £10. Because the real assets are later transferred to the trustees by the real settlor, such trusts are sometimes called 'pour over' trusts.

4.46 In *Schmidt* itself, Lord Walker, delivering the judgment of the PC, said:

> *[34] ... It is appropriate to reflect that ... the forms and functions of settlements have changed to a degree which would have astonished Lord Eldon. By the 1930s high rates of personal taxation led some wealthy individuals to make settlements which enabled funds to be accumulated in the hands of overseas trustees or companies. ... This practice increased enormously with the introduction of capital gains tax in 1965. But increasingly stringent anti-avoidance measures encouraged legal advisers to devise forms of settlement under which the true intended beneficiaries were not clearly identified in the settlement. Indeed their interests or expectations were often barely perceptible. Rarely did a beneficiary take an indefeasibly vested interest with an ascertainable market value. Tax avoidance is therefore one element which has strongly influenced the forms of settlements; and once the offshore tax-avoidance industry has acquired standard forms its inclination is to use them, subject perhaps to some more or less skilful adaptation, even for clients whose aim is not to avoid United Kingdom taxation.*
>
> *[35] There is another element, also linked (though less directly) to taxation, which has encouraged the inclusion in settlements of very widely defined classes of beneficiaries. After the Second World War estate duty was charged in the United Kingdom at very high rates, with much less generous reliefs for agricultural and business property than those now available. A wealthy landowner or businessman might be advised that the safest way to preserve his fortune was to give most of it away, while he was still in the prime of life, to trustees of an irrevocable settlement in discretionary form under which the settlor himself was not a beneficiary. It is not surprising that a settlor in such a position should wish to cover as comprehensively as he could all possible current and future claims on his bounty, since he was being asked to make an immediate, irrevocable disposition of much of his wealth, rather than being able to review from time to time the ambulatory dispositions in his will and codicils. But his lawyers might also advise him that the most natural expressions for defining discretionary objects of his bounty (such as 'relatives', 'old friends',*
> p. 93 *'dependants' or 'persons with moral claims') were of doubtful ↵ legal efficacy. So there was a tendency to define the class in the widest possible terms. The process can be seen in a long line of cases starting with* In re Gestetner Settlement *[1953] Ch 672. It led to* In re Manisty's Settlement *[1974] Ch 17, upholding the validity of an intermediate power comparable to that in clause 3.3 of the Everest Trust [that is, a power to add as beneficiaries anyone in the world apart from a very small class of excluded persons].*
>
> *[36] The Board have to consider what rights or claims to disclosure the appellant has, either personally or as his father's personal representative, under two badly drafted settlements whose terms have been moulded by the sort of influences mentioned above. One possible reaction would be that Mr Schmidt and his colleagues have made their bed and they must lie on it; if they have deliberately entered into a web of camouflage, it is hardly for anyone claiming through them to complain that the position is not transparent. As Lord Greene MR observed, giving the judgment of the court in* Lord Howard de Walden v Inland Revenue Comrs *[1942] 1 KB 389, 397 if a taxpayer plays with fire it scarcely lies in his mouth to complain of burnt fingers.*

4.47 Nevertheless, Lord Walker continued as follows:

> *[36] ... However, the Board consider that that inclination must be resisted. ... It is fundamental to the law of trusts that the court has jurisdiction to supervise and if appropriate intervene in the administration of a trust, including a discretionary trust. As Holland J said in the Australian case of* Randall v Lubrano *(unreported) 31 October 1975, cited by Kirby P in* Hartigan Nominees Pty Ltd v Rydge *(1992) (at 416):*
>
> > *'no matter how wide the trustee's discretion in the administration and application of a discretionary trust fund and even if in all or some respects the discretions are expressed in the deed as equivalent to those of an absolute owner of the trust fund, the trustee is still a trustee.'*

4.48 Lord Walker firmly adopted the view that the beneficiary's right to information flowed from the inherent jurisdiction of the court to ensure that trusts were properly supervised and enforced, and that, depending on the circumstances, in some cases an object of a power of appointment appropriately had such a right. In the exercise of its inherent jurisdiction, the court might refuse, in certain cases, a claim by an object for information:

> *[67] [T]he recent cases also confirm (as had been stated as long ago as* In re Cowin *33 Ch D 179 in 1886) that no beneficiary (and least of all a discretionary object) has any entitlement as of right to disclosure of anything which can plausibly be described as a trust document. Especially when there are issues as to personal or commercial confidentiality, the court may have to balance the competing interests of different beneficiaries, the trustees themselves, and third parties. Disclosure may have to be limited and safeguards put in place. Evaluation of the claims of a beneficiary (and especially of a discretionary object) may be an important part of the balancing exercise which the court has to perform on the materials placed before it. In many cases the court may have no difficulty in concluding that an applicant with no more than a theoretical possibility of benefit ought not to be granted relief.*

p. 94 **4.49** What does it mean to say that an applicant has 'no more than a theoretical possibility of benefit'? Consider yourself. As a student of this subject, you will now know that, because of intermediate powers of appointment, or intermediate powers to appoint someone to a class, as in clause 1(ii) in Example 5, you are the object of a power of appointment in countless trusts. You decide, therefore, to go on a cycling tour of the Isle of Man, Guernsey, and Jersey, stopping at each trust company office you pass on the way. You knock on the door and tell the trust officer, 'Please provide full information on all the trusts you administer which contain intermediate powers of appointment'. You will, of course, be sent away with a flea in your ear. And quite right, too. Assuming that these trusts have been settled by strangers having nothing to do with you, any appointment to you would almost certainly be regarded as 'irrational, perverse, or irrelevant to any sensible expectation of the settlor' (**3.53**). This is the sense in which, though a member of the class of objects, you have no more than a theoretical possibility of benefit.

4.50 In the New Zealand case *Foreman v Kingstone* (2004) Potter J made the point this way:

> *[87] Of course what is a reasonable request for information is likely to be viewed differently by trustees conscious of their duties to administer the trusts for the benefit of all beneficiaries, and the particular beneficiaries seeking information. There are a number of factors which will bear on the situation. To take an example: the M P Foreman Trust by definition includes within the class of discretionary beneficiaries 'any charity within New Zealand'. It could be expected that trustees and the Court in the exercise of its supervisory jurisdiction, would view differently a request of the trustees for disclosure of trust documentation made by a random charity which had not, pursuant to the exercise by the trustees of their discretion, become an object of the trust, and a similar request from persons named or included by definition within the class of discretionary beneficiaries.*

4.51 The result in *Schmidt* can be questioned (see Pollard (2003); Smith (2003a), (2016); (2017); for a survey of the issues raised by *Schmidt*, see Ho (2010)). The decision seems to create a good measure of uncertainty in this area, and it may be difficult for trustees to decide what information they ought properly to reveal to objects without applying first to the court, which will create an expense for the trust. *Schmidt* might also seem to accept the inevitability of, if not actually endorse, an unfortunate antagonistic attitude between trustee and beneficiary. On this latter point, Hayton (in conversation with the author) argues for more openness between trustees and beneficiaries. The more one tries to hide things from people the more suspicious they become: 'no one likes being treated like a mushroom, kept in the dark and fed you know what.'

4.52 Yet it is certainly not clear that *Schmidt* has led to a general departure from the previous principles. In the Australian case *McDonald v Ellis* (2007) Bryson JA held that in the case of a beneficiary with a vested entitlement, the court should have no discretion; such a beneficiary should be entitled to all relevant trust information as of right.

4.53 In *Lewis v Tamplin* (2018), HHJ Matthews held that beneficiaries, in particular beneficiaries of fixed trust
p. 95 interests, are generally entitled as of right that the trustee disclose trust documents; this is part and parcel of the trustee's duty to account; *Schmidt* should not be read to indicate otherwise, in particular *Schmidt* should not be read to say that it was at the discretion of the trustees whether to disclose information in such cases (at [30], [41]). He stated ([41], emphasis added):

> The whole direction of travel [in *Schmidt*] is in equating the position of the discretionary object to that of the fixed interest beneficiary, and not the other way around. *The implication is that the beneficiary of a fixed, transmissible interest would normally obtain the assistance of the court.*

4.54 HHJ Matthews also denied that the 'Londonderry principle' protecting the trustees' reasons for exercising their dispositive discretions applies to the exercise of administrative powers of trustees. He said (at [47]; see also [82]–[85]):

> *[That] would mean in practice that trustees were never obliged to disclose professional advice or even other information about (for example) dealings with the trust assets, because the relevant documents might well disclose reasons why the trustees had decided to sell this asset and buy that one. That cannot be right. In addition to that, I find that, in the case of* Re Londonderry's Settlement *[1965] Ch 918 itself, the members of the court made it clear that their decision was one in relation to dispositive powers of trustees.*

4.55 HHJ Matthews then went on to discuss disclosure of various documents sought by the beneficiaries. Importantly, he had this to say about documents which the trustees said were privileged by the lawyer-client relationship of confidentiality:

> *[59] [T]he claimants are not entitled to production to them of any documents protected by legal professional privilege of the trustees in any capacity other than as trustees of the Tamplin Trust. Originally, the trustees sought to claim legal professional privilege for all the communications with their lawyers … This untenable position has wisely been abandoned. There is a clear distinction to make. In general, where trustees seek legal advice for the benefit of themselves personally, eg in relation to possible breach of trust liability, or of another trust of which they are trustees, and pay for it themselves, or out of the funds of that other trust, without recourse to the funds of the Tamplin Trust, that advice may well be privileged in favour of those trustees as against these beneficiaries. But, where the advice is sought for the benefit of the Tamplin Trust as a whole, and the trustees pay for that advice out of Tamplin Trust funds, then such advice, even though it may be privileged as against third parties, is not privileged as against the beneficiaries, and is liable to be ordered to be produced.*

Issues and concerns

4.56 Many of the issues now to be discussed draw heavily upon Lionel Smith's 'Massively Discretionary Trusts' (Smith (2017)). Look again at Example 5 (**4.2**) to refresh your memory about its basic structure.

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MDTs and charities—a charitable trust must be exclusively charitable

4.57 For a charitable trust to be valid, it must be for exclusively charitable purposes. So, for example, one cannot transfer £1m to trustees for a charitable purpose, such as a trust to relieve poverty, and then give the trustees a power to appoint property to individuals from that £1m. So, whether an MDT violates this rule depends upon how it is structured.

4.58 A trust with the following structure is perfectly valid:

1. A trust of the income for individuals, whether discretionary or not.
2. Notwithstanding 1., a power to accumulate the trust income and add it to the trust funds.
3. A discretionary trust of the trust funds under the 'default clause', such as 'on trust for such UK charities as my trustees shall at their absolute discretion select.'

This structure is valid because there is a trust of the income for individuals, and a charitable trust of the capital. Such a trust is no different in principle from 'to John for life and then to the International Red Cross'. Both structures are valid because the trust of income and the trust of capital are distinct gifts, and the gift of capital is exclusively charitable.

4.59 But consider this structure:

1. A duty to accumulate the trust income and add it to the trust funds.
2. Notwithstanding 1., a power to distribute the trust funds to individuals.
3. A discretionary trust of the trust funds for distribution on the 'Vesting Day', such as 'on trust for such UK charities as my trustees shall at their absolute discretion select.'

This structure, I submit, is invalid because the entire trust of the assets is for the capital beneficiaries, the charities—a duty to accumulate is simply a duty to add the income to capital, so such a duty makes the capital beneficiaries also the income beneficiaries. The powers under 2. then give the trustees the power to appoint the trust assets away from the charitable beneficiaries. The trust is then not wholly charitable, and it fails. Nevertheless, if the text of Lewin is any guide (Lewin (2020), 21-087, quoted at **4.67** below), this sort of trust is common and commonly understood to be valid.

Determining the 'true intended beneficiaries'

4.60 As we have already seen (**4.44**, **4.46** et seq), both Lords Hoffman and Walker have pointed out that MDTs give rise to difficulties determining the legally enforceable rights under MDTs. Questions will naturally
p. 97 arise with respect to standing to enforce the trustees' obligations, rights to information, and the application of the principle in *Saunders v Vautier* (**3.62**).

4.61 We can oppose two perspectives, that of Nolan (2017) and Smith (2017). Nolan argues that courts, relying on their inherent jurisdiction to administer trusts, will allow *certain* objects to enforce MDTs. The reader will recall that in *Schmidt* the Privy Council granted restricted rights to information concerning the trust to an object, indeed relying upon its inherent jurisdiction. Smith is less sanguine. To summarise Smith's position roughly and briefly, since a trustee owes obligations regarding the trust property only to the objects of trusts and not to objects of mere powers, only the former have the corresponding rights to enforce the trust, and consequently, the right to information from the trustee concerning the latter's administration of the trust. This is, as we have seen (**4.31**), for Smith, a matter of the logic of the trust.

4.62 I shall not adjudicate this dispute here except to point out one feature of the discussion. Nolan accepts that not just any object of an MDT should have standing to enforce the trust (Nolan (2017), 167–168, emphasis added):

> *The court can limit the claims it hears to those made by an object who has a substantial possibility of seeing benefit from the trust, … one of 'the true intended beneficiaries' of the settlement … But the court need not even entertain claims brought by those who have no substantial expectation of benefit.* Who are the 'true intended beneficiaries', and who are not, simply turns on the evidence, and the court's evaluation of that evidence. And there will often be a letter of wishes which makes the distinction clear, something that the court can always demand to see.

4.63 It seems, then, that Smith and Nolan agree on the basic principle that only true beneficiaries should be entitled to enforce the trust. Where they differ is on whether, as a matter of legal principle, this should be determined on evidence entirely extrinsic to the trust instrument which sets out the trust's purported terms, evidence which will almost certainly directly contradict the plain meaning of those terms. For example, it is

commonly understood that the 'final' or 'default' capital beneficiaries are not intended to receive anything, so they are not 'true, intended beneficiaries'. Furthermore, and we shall return to this point regarding letters of wishes (**4.77** et seq), the flexibility of MDTs lies in the fact that the actual beneficial interests are determined on evidence extrinsic to the trust instrument, and there is every likelihood that the 'true intended beneficiaries' may change, often radically, over time. To take the most common example from the cases, the spouse of the settlor may well be a 'true, intended beneficiary' just until they file for divorce. Finally, *Schmidt* gives almost no practical guidance on the 'evidence' upon which such determinations are to be made.

4.64 This dispute may reveal a profound difference between Nolan's and Smith's particular 'theories' of the power to create a trust, especially concerning the 'certainty' requirements. What sort of power is it to create a legal structure whose defining legal rights, duties, and powers can vary enormously from time to time, often suddenly, and which can only be ascertained by reference to actions and events entirely extrinsic to its purported terms?

p. 98

The registration of beneficial trust interests

4.65 Following international movements to thwart money-laundering and tax evasion, trustees must now register the trusts they administer and, importantly, they must identify the beneficiaries of their trusts. Examining the details of the legislation (see https://www.gov.uk/guidance/register-a-trust-as-a-trustee *<https://www.gov.uk/guidance/register-a-trust-as-a-trustee>*) is beyond our purposes, but one feature stands out in relation to MDTs; it would seem that in registering the beneficial interests under such trusts, only the identity of the 'true' beneficiaries would have to be revealed.

Standing to enforce and rights to information

4.66 Following Nolan's approach, it would appear that despite who happens to appear (or not appear) in the class of 'Beneficiaries' in clause 1 of Example 5, standing to enforce the trust and rights to information, such as the right to see the trust accounts, will be restricted to the 'true, intended beneficiaries' whose identity will be determined on the extrinsic evidence of the settlor's intentions, in particular as expressed in the letter of wishes.

4.67 Lewin ((2020), 21-087) gives an example of where this reasoning leads (I have already cast doubt on the validity of this trust structure (**4.59**) but treat it as valid for the sake of argument):

> *Take for instance, the case of an offshore trust where the only trusts are a trust for accumulation during the trust period and a trust for a named charity, typically the Red Cross, at the end of this trust period, but those trusts take effect subject to fiduciary powers of appointment and distribution (not yet exercised) in favour of a class consisting of no-one (or no-one other than the named charity) but with power (not yet exercised) for the trustees to add any persons to the class during the trust period. If the claimant is able to prove that his late father was, or at least prima facie was, the real settlor in relation to the trust [see* **4.45** *above] and that he had a normal relationship to his father, and that the settlor had a reason (not involving illegality) for creating a trust under which the identity of the intended beneficiaries was not apparent from the trust instrument, those facts, combined with the structure of the trust instrument, may suffice to show that prima facie the substantial purpose of the settlement was to enable benefits to be provided for the claimant, or the claimant and other members of the family, as would be permitted by the trust upon exercise of the power of addition. The evidential burden would then shift to the trustees to meet the case that the claimant's expectations were real and substantial. The claimant would be assisted if he had in his possession the real settlor's letter of wishes indicating that the claimant was the intended beneficiary, but even without that the facts might be strong enough to satisfy the court.*

Saunders v Vautier issues

4.68 Since MDTs are trusts, the principle in *Saunders v Vautier* applies. Three points arise. The first is that if
p. 99 we go down the 'true, intended beneficiaries' route, then it would seem to follow that they and they alone have the *Saunders v Vautier* right to collapse the trust, irrespective of whoever else is an object under the strict terms of the trust.

4.69 Second, as we have seen (**3.73**), it is unsettled whether objects of mere powers of appointment must agree to any collapse of the trust under the principle, and it is even less settled with respect to intermediate powers to appoint members to a class of beneficiaries as under clause 1(ii) of Example 5 (Lewin (2020), 22-023). Two recent decisions are of note here. First, in *Orb ARL v Ruhan* (2015) the court stated (at [118]) that it was arguable on the current state of the law that the present objects of a discretionary trust could invoke the rule, notwithstanding the fact that the trustees had a power to add members to the class. Second, in the Guernsey case *Rusnano Capital AG (in liquidation) v Molard International (PTC) Limited* (2019); affirmed in *Molard International (PTC) Limited v Rusnano Capital* AG (2019), the same issue arose, and though the case was decided on the construction of Guernsey legislation which codified the principle in *Saunders v Vautier*, the court made it clear that it could find no principle in the *Saunders v Vautier* doctrine which would have prevented the identified beneficiaries invoking the principle despite the trustees having a power to add to their number ([22]–[23]).

4.70 One case that is cited by the proponents of the view that where there is a power to add beneficiaries the principle in *Saunders v Vautier* cannot be invoked is *Re Trafford's Settlement* (1984). (See *Orb ARL*, [117], [118]; *Rusnano*, [28],[30]; *Molard*, [29].) With respect, this case is a very frail reed on which to support that contention. In *Re Trafford* a man was the beneficiary of an income interest under a trust. The class of income beneficiaries could expand to his wife and children if he married and had children, but he never married and had no children. The question was whether he was solely entitled to the income of the trust prior to his death. Now you might say, quite sensibly, 'of course he was', as he was the only income beneficiary at the time, and

the court acknowledged the attractiveness of this position (at 40F). But the court held (at 40F–41A), relying in part (at 39B–C, 40F) upon an *obiter dictum* in another tax case (*Re Weir* (1971) at 169 per Russell LJ (quoted below (**4.72**)) that where the class of beneficiaries could expand on the happening of certain events (here marriage or the birth of children), the trustees were entitled to withhold the payment of income to the sole beneficiary for a reasonable time just in case the class might expand, so that that income could be paid to the incoming class member.

4.71 The first thing to notice about this case is that it concerned whether the sole beneficiary had an 'interest in possession' under a taxing statute in the income as it arose, and the court held that if it held otherwise than it did this would produce a number of inconvenient tax consequences given the wording of the statute, and these consequences fortified the court in its decision (at 41B–G).

4.72 But more importantly the decision is questionable in principle. A beneficiary entitled to income is entitled to all the income that arises during the period in which they are a beneficiary. On what basis would a beneficiary who became a member of the class of beneficiaries on 1 January 2022 be *entitled* to *any income* that
p. 100 arose in 2021? And note that the obiter dictum in *Re Weir* would seem to apply only in very special circumstances:

> *a sole object for the time being would not necessarily be entitled as such to insist upon payment over of every penny come to the hands of the trustees: the trustees on learning of an imminent addition to the class of objects, for example a child of an impoverished C, would be entitled to keep income in hand with a view to applying it for the benefit of C's child.*

This example obviously does not generalise to the proposition that trustees may always hang on to some income accruing to income beneficiaries just in case the class of beneficiaries may expand. With respect, then, neither *Re Weir* nor *Re Trafford* provide support for the general proposition that the members of a class of income beneficiaries are not entitled to the income as it arises, on the basis that the trustees have a power to add to the class of beneficiaries, a power which they have not in fact exercised.

4.73 Now you might ask, why wouldn't the trustees, faced with a demand by the solely entitled identified beneficiaries to collapse the trust, not just immediately exercise their power to appoint new individuals to the class of beneficiaries, assuming such beneficiaries would not agree to collapse the trust under the principle of *Saunders v Vautier*? It is submitted that this exercise of the power would be challengeable first, as one possibly undertaken in bad faith, but also for a purpose for which the power was not conferred (**3.43**). The trustees might argue that by engaging in this manoeuvre they were fulfilling the intentions of the settlor who wished the trust to continue. The answer to this is merely to reiterate the trite law point that the operation of the principle in *Saunders v Vautier* is to defeat the settlor's intentions, and so the beneficiaries' rights under this rule should not be permitted to be abrogated for the sole purpose of abrogating their rights. Finally, the rights of the beneficiaries to invoke the principal must be determined at the time the demand to collapse the trust is made. Not only can the trustees not undermine their rights by purporting to appoint new beneficiaries following that demand, the trustees cannot point to future possibilities. For example, consider the case of a discretionary beneficiary of a trust of the income. If she were to die next year, she would lose her interest. But trustees cannot point to that possibility and deny her status as a beneficiary here and now.

4.74 A different sort of case may be relevant here. It is possible for a settlor to insert a trust term which provides for the case where a dispositive provision fails (which, depending on the nature of the equitable interest created by the provision, might prevent an automatic trust from arising (**2.14**)). This happened in *Jeffreys v Scruton* (2020). There was a testamentary trust of income for the settlor's severely disabled son, and the trustee had an intermediate power to appoint others to the class of income beneficiaries. There was a further provision which provided that, if this trust failed, a second trust to distribute the capital to the settlor's nieces and nephews would operate. As it happened, the son predeceased the settlor but she did not change her will. Clearly the trust for the son failed for lack of an object. But the trustees argued that the trust of the
p. 101 income had not failed because they could, essentially, keep it alive by using their power of appointment to add new members to the class of objects. The court decided the case against the trustees following a thorough exercise of construction of the trust instrument. Although they did not rely upon the settlor's letter of wishes, it fortified their conclusion because it basically advised the trustees to use their powers to appoint additional members to the class of income beneficiaries to appoint those persons, including institutions and charities, which were assisting her son during his lifetime. The important point for our purposes is that an intermediate power to appoint members to a class of objects may be 'dependent' upon their remaining at least one of the original objects of the class.

4.75 Applying this reasoning to Example 5, if all the beneficiaries identified in clause 1(i) were tragically wiped out, then the power in clause 1(ii) might fall as well. In that case there would be a resulting trust of the income interest to the settlor. Besides the power to appoint new beneficiaries to the class of income beneficiaries, the other powers relating to the original class of beneficiaries, set out in clauses 2, 3, 4, and 5. might also operate on the same basis, ie they were only intended to operate on the basis that the original class of beneficiaries could benefit from them. If that is right then there would remain only a trust of the income for the settlor, and the trust of the capital for charities. In such a case it would seem clear that the father and the Attorney-General representing the charities could invoke the principle in *Saunders v Vautier.*

4.76 Third, there is one final wrinkle that we have to consider. It appears to be not uncommon for an MDT to be created without the trust instrument identifying *any* income beneficiaries. The idea seems to be that this can be done later, by exercising the power to appoint members to the class of beneficiaries. That is the supposition in the hypothetical example from Lewin discussed earlier (**4.67**). Again, I have submitted that that structure is not valid (**4.59**), but again assuming for the sake of argument that it is, the court in *Rusnano* said this ([34]):

> *If the trust were what has been called a Red Cross Trust, it is quite possible that the default charitable beneficiary, if the only named beneficiary, will not know about the settlor's possible bounty and so be unable to invoke [the legislation codifying the principle in* Saunders v Vautier*]. However, even if a charity knew that this option existed, the charity may choose not to terminate the trust on the basis that I suspect that such a charity would quickly discover that it will no longer be the preferred charity in such cases going forwards. In other words, an immediate windfall may not be a sound longer-term strategy.*

Whether the Attorney-General or a named charity would subscribe to the strategy set out in the last sentence is, to your author's mind, an open question (recall *Re Barton* (**3.71**)).

The problematic status of letters of wishes

4.77 On its face the trust instrument of an MDT allows the trustees to apply the trust assets to anyone they
p. 102 choose by appointing them to the class of 'beneficiaries'. As we have seen (**4.6**), this led to the practice of the settlor's providing a letter of wishes to provide some guidance to the trustees in exercising their discretions. Regarding this practice Smith says (2017, 45): 'Paradoxically, the settlor's wishes, which are not binding and are not terms of the trust, are controlling.' The paradox is obvious—how can the settlor's power to determine ('control') the distribution of the trust assets not displace the actual terms of the trust, or rather, be part of the terms themselves? As we shall see, (**5.69**), sometimes the court will find that the wishes expressed in the letter are in such an imperative form (the trustees 'shall' do x or y) that the letter does actually displace the written trust terms, negating the trustees' discretions. This again raises the point about 'true, intended beneficiaries'. Note again the last line from the quotation from Nolan (**4.62**): '*And there will often be a letter of wishes which makes the distinction clear, something that the court can always demand to see.*' So, the letter of wishes does figure centrally in determining the 'true, intended beneficiaries'. But on what theory of the trust are the 'real' trust terms, which identify the 'true intended beneficiaries', held not to be terms of the trust?

The 'updating' of letters of wishes

4.78 It appears that it is commonly understood that letters of wishes can be 'updated' by the settlor from time to time, or one letter substituted by a new one at the settlor's choosing. But this would seem to violate a basic principle of trust law, which might be stated as the principle that 'a settlor can only settle the trust once.'

4.79 A trust is a disposition of property. Once it occurs, unless the terms of the trust grant powers to the settlor, they have no right, qua settlor, to enforce the trust or dictate to the trustees how they exercise their discretions, for the simple reason that the property is no longer theirs, it belongs to the beneficiaries. After you have settled the property, you are not entitled to add or delete terms. And the traditional understanding of the 'proper purposes' doctrine (**3.43**) regarding the exercise of a trustee's powers is that these purposes are determined at the time the trust is created. Those purposes cannot be 'updated' by the settlor from time to time because like the trusts terms themselves they are, unless provision is made to the contrary, fixed at the time the trust is created.

4.80 But, of course, the settlor's actual intentions are determinative of the terms of the trust whether or not they appear in the written trust instrument. If, because of the advice they have been given, it is the settlor's true understanding that they can, via a letter of wishes, dictate from time to time what the trustees must do, this is just to say that the trust assets are held to the settlor's order. What this would in fact amount to is not only a general power to amend the trust terms but also a power of revocation (**2.11**), because the settlor could tell the trustees to hold the trust assets for her own benefit absolutely. This is not a fiduciary power (**3.28**). The settlor can exercise it just as she likes without being concerned in the least with the interests of others.

4.81 Consider the following, which your author captured in a perfunctory internet search:

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> *If you have incorporated a trust into your will, or have created a lifetime trust, then it is important to let your trustees know what your wishes are with regards to how you ↵ would like the assets of your trust to be managed and distributed. The best way to do this is to set out your wishes in writing or, more specifically, in a letter of wishes to your trustees. Letters of wishes are not legally binding but they do hold strong moral weight and your trustees should have good reason to depart from their guidance. You can include guidance such as ages at which you envisage your beneficiaries receiving capital from the trust fund, what you envisage the trust fund being used for—i.e to fund educational costs or to help with the purchase of a property etc. A great benefit of letters of wishes is that they can be updated as often as you like—if your circumstances change or you simply change your mind—without the need to update your will itself. Letters of wishes should be signed and dated by you and then stored with your will or trust document.*

From 'Letters of Wishes' (http://www.birketts.co.uk/insights/legal-updates/letters-of-wishes *<https://www.birketts.co.uk/insights/legal-updates/letters-of-wishes>*, last visited 3 June 2020); see also *Breakspear v Ackland* (2008), [3]–[4] where Briggs J appears to treat written letters of wishes and oral expressions of wishes as standing on the same footing, and [6], where he refers to the 'flexibility' of '[t]he combination of a broad discretionary trust accompanied by a wish letter.'

4.82 If therefore, the ability to alter her wishes at will does reflect the settlor's true intention, this has consequences. If, for example, the settlor becomes insolvent or is subject to marital property proceedings, it is a beneficial asset of hers available to their creditors or spouse as the case may be.

4.83 One concluding point, which relates to everything we have discussed in this chapter. Defenders of MDTs will typically claim that whatever the guidance from the settlor in his letter of wishes, and whatever the court may determine about his wishes from that and any other evidence external to the trust terms, the discretions remain the trustees', and whilst as a matter of good practice they might consult with the settlor (whilst she is still alive) and with the protector and 'true, intended beneficiaries' prior to exercising their dispositive discretions, they will do so having formed their own independent judgement.

4.84 This is the theory, though there may be doubts that this is always or even typically the practice. In *Pitt v Holt* (2013) Lord Walker said (emphasis added):

> *[67] It is interesting, in this context, to compare the facts of some of the offshore cases with those of* Turner v Turner *[1984] Ch 100 [**3.46**]. That was a case in which a farmer made a discretionary settlement which he did not understand, and appointed as trustees family friends who never realised that they had any responsibility at all except to do as the settlor asked. They thought that it would be intruding into the settlor's affairs if they were to read the documents that they were asked to sign (see at pp 106–108). Anyone familiar with the duties of trustees may find this hard to contemplate (as Mervyn Davies J did, at p 109).* But it may be that some offshore trustees come close to seeing their essential duty as unquestioning obedience to the settlor's wishes.

4.85 Last word to Christopher McCall (2013, 339):

p. 104 ↵ *[Y]ou can have trustees bound to consult with their beneficiaries and a protector and then required to form their own views how to act in the light of that consultation … But not many trusts work like that. Most trustees are if not muppets then at least puppets who charge a high fee for being told what to do and meanwhile safeguarding the funds. That is not what trusteeship was meant to be.*

MDTs as 'chameleon trusts'

4.86 There is one final issue to be discussed, which I shall dub the 'chameleon trust' issue (aka the 'Angora cat' problem; see *JSC Mezhdunarodniy Promyshlenniy Bank v Pugachev* (2017), [438]–[440] per Birss J). A chameleon changes its colour depending on the colours of its immediate environment. As applied to MDTs, the issue is whether the trust can be presented in one way for the purpose of one kind of litigation, and another way in another kind of litigation. An example will illustrate.

4.87 Let us use our Example 5, where there is a discretionary trust of capital for charities. Let's say the 'true, intended beneficiaries' wish to collapse the trust and the trustees have no objections. As we have seen (**3.62**), all the beneficiaries of a trust must participate in order to collapse the trust. (The same is true where the beneficiaries want to alter, or 'vary' the terms of the trust (**3.64**)—we will look at the variation of trusts later (**8.69** et seq).) Normally, this would require getting the Attorney-General, who enforces charitable trusts to agree, as he would represent the gift to charity. But if the trustees establish to the satisfaction of the court that the charities were not really intended to receive anything, a complacent court might not require the Attorney-General to be represented. This was what the court held in the Jersey case of *Re GEA Settlement* (1992).

4.88 Now let us assume a different sort of litigation: the settlor has become bankrupt, and his creditors claim that the 'dummy' capital beneficiaries were never intended to receive anything, and so the capital interest of the trust goes back to the settlor by way of resulting trust. They might even be able to make a claim that the entire beneficial interest under the trust results to the settlor if no other beneficiaries have at that point been appointed. Here's where the trust, as a chameleon, changes its colours. Now the trustees vigorously defend the validity of the trust, claiming that the 'default' clause is a perfectly valid trust of the capital. The point here, obviously, is that a trust cannot be 'this' in one case and 'that' in another, but the rules (if one can call them 'rules') about determining who are the 'true, intended beneficiaries' seem to present just that danger.

Further reading

Bennett & Hofri-Winogradow (2021)

Hudson (2021)

McCall (2013)

Miller (2018)

p. 105 ↵ Nolan (2017)

Penner (2021a)

Smith (2003a, 2017)

Turner (2018)

Must-read cases: *IRC v Broadway Cottages Trust* (1955): *McPhail v Doulton* (1971); *Schmidt v Rosewood Trust* (2003); *Breakspear v Ackland* (2008); *Re Trafford's Settlement* (1984).

Self-test questions

1. What are the arguments both for and against the 'complete list' and 'is and is not' tests?
2. Explain the court's reasoning in *McPhail v Doulton* (1971).
3. Explain the court's reasoning in *Schmidt v Rosewood Trust* (2003).
4. What does it mean when a claimant seeking information from a trustee has 'no more than a theoretical possibility of benefit'?
5. How should the court determine who the 'true intended beneficiaries' are?
6. What are the advantages and disadvantages of letters of wishes?
7. As a matter of principle, should any object of an intermediate power of appointment be able to block the operation of the principle in *Saunders v Vautier*?
8. What does it mean to call a trust a chameleon trust?