



# WEEKLY TAX BULLETIN

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## Trustee powers under discretionary trusts - we have all been warned

*by Matthew Burgess, Director, View Legal*

The ability of a court to review, and potentially unwind, a decision of a trustee is in many respects predicated on the trust adviser's mantra profiled often in this Bulletin, namely: 'read the deed'.

The issues in this regard can be particularly critical in relation to discretionary trusts where, at least in theory, there are few limitations placed on a trustee concerning most key aspects of the administration of the trust.

In a sentence the heuristic the courts appear to apply is that a trustee's decision cannot be reviewed unless on the material before the trustee it is one that no reasonable trustee could have made.

What this rule means in any particular factual matrix can however be somewhat nuanced.

### *Recent decision*

For example, in the recent case of *Owies and Owies v JJE Nominees Pty Ltd* (ACN 004 856 366) (in its capacity as trustee for the Owies Family Trust) [2022] VSCA 142 (“Owies”), the appeal court reached an opposite conclusion to the trial judge in relation to the appropriateness of various distributions made by the trustee.

The key error of the initial judge was said to be due to the adoption of 'an unduly narrow view of the evidence and the structure of the trust deed as a whole'.

### *Key principles from Owies*

Relevantly the court confirmed the following key principles in relation to any review of the exercise of a trustee of discretionary powers.

In considering the nature of the power to distribute annual income, the starting point must be the nature and purpose of the trust having regard to the terms of the trust deed. Here the settlor confirmed in the trust deed their desire to make 'provision for the Primary Beneficiaries and the General Beneficiaries'.



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An obvious, but unstated, premise on which the trustee would be expected to discharge its duties is that it would generally be informed about the differing circumstances, needs and desires of each beneficiary as an incident of the familial bonds that underpin the trust and explain its purpose.

If those familial bonds become strained or broken (as they did here), neither the purpose of the trust to provide for the family as a whole nor the requirement that the trustee properly inform itself change.

While the trust deed did contemplate unequal distributions across the beneficiaries (due to the width of the discretionary powers given to the trustee), the exercise of all of the powers had to take into account the purpose of the trust and the default distribution clause that provided that the three children would be entitled in equal shares.

Distributions that did not provide anything to any of the children were considered by the court as being 'remarkable'.

As explained in *Pitt v Holt* [2013] 2 AC 108 (“Holt”) there is a distinction between distributions that are plainly beyond power (for example to a person who is not in fact a potential beneficiary) and those dispositions that are within power, but in respect of which there has been some breach of duty (that is a distribution to a potential beneficiary where the trustee has failed in its duty to give proper consideration to relevant matters or its duty to give real and genuine consideration to the power).

Using the principles in *Holt* therefore, a breach of trustee duty, for example due to a failure to give due consideration to the interests of a beneficiary or object of a power does not automatically lead to the decision being set aside and its consequences reversed. Rather, it is necessary for those aggrieved with the breach to establish that the decision should be set aside; it would then be necessary for the court to determine any defence that might be raised in answer.

That is the distributions are not void, only voidable - a key factor in *Owies* given that the aggrieved beneficiaries had not applied for the distributions to be set aside. Thus, despite the court concluding the distributions were inappropriate, they remained undisturbed.

## *A warning for trustees - and advisers*

The outcome in *Owies*, whereby a court unwinding of historical distributions was essentially only avoided due to a technicality in relation to the way the proceedings by the aggrieved beneficiaries were crafted, is a stark reminder for trustees, and trust advisers.



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In particular, there are onerous obligations that must be discharged before a trust resolution is valid at law - aside from any questions as to the validity or appropriateness of the proposed distribution from a tax planning perspective.

Furthermore, another recent decision - involving a well-known Australian business family, namely, *Smorgon v ES Group Operations Pty Ltd & Ors* [2021] VSC 608 (“Smorgon”) provides additional reason for vigilance in this area.

In *Smorgon*, a disgruntled potential beneficiary of a number of discretionary trusts - despite not being a primary beneficiary of most trusts in the group - applied to court seeking access to a vast array of information concerning the trusts.

While access was denied in relation to many of the trusts, in relation to 2 trusts where the relevant beneficiary was in fact essentially a 'primary beneficiary' - and there were no clauses in the trust deed restricting disclosure - access to the trust deeds, profit and loss statements and balance sheets was given by the court, despite the trustee's attempts to deny the beneficiary.

