

TAX

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TOOL FOR REVERSING TRUSTEE DECISIONS



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There is a little known rule that can help trust advisers when a disposition made by trustees turns out to have unexpected and adverse consequences.

They may have made a disposition that gave rise to an unintended and unexpected tax liability but if it can be shown that they had misunderstood the effect of what they were doing, they may be eligible to have that disposition set aside.

The rule explained

The rule is commonly referred to as the rule in *Hastings-Bass*. The rule has its origins in *In re Hastings-Bass deceased [1975] Ch 25*, a decision of the English Court of Appeal. In that case the Court of Appeal made a negative statement that a disposition would not be set aside on the basis that the trustees had misunderstood the effect of what they were doing but it allowed for certain exceptions to this rule.

It was held that a disposition could be set aside if it was clear that the trustees would not have acted as they did if:

- they had not taken into account things they should not have; or
- they had not failed to take into account things they should have.

Over time, the “negative” expression of the rule by the English Court of Appeal has

morphed into a “positive” rule such that it is now commonly expressed in the UK that a court will interfere with a discretion made by a trustee if it is clear that the trustee would not have acted as they did had they taken into account everything they should have or had not taken into account things they should not have.

Why is it useful?

The rule in *Hastings-Bass* is a useful one as it has been applied more broadly and generously by the English courts in setting aside dispositions made by trustees than other equitable remedies.

Courts can set aside dispositions on the grounds of mistake or could rectify a deed which does not reflect the true intentions of the parties, but they are usually reluctant to do so. The principle behind their reluctance seems to be that formal documents executed by persons of full capacity ought to be upheld.

In contrast, the rule in *Hastings-Bass* seems to require that the trustees only need to show that, on the balance of probabilities, they would have acted differently if they had known the true effect of the disposition they were making. This seems to be the case even if the only misconception is around the fiscal or tax consequences of the action taken by the trustees.

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Cases when the rule has been applied in the UK

- Retirement of a professional trustee meant there was no longer a majority of overseas trustees for a will trust which subjected the trustees to capital gains tax. The trustees' failure to predict the fiscal effect of the future retirement of the professional trustee meant the appointment was set aside (*Green v Cobham* [2000] WTLR 1101).
- Trustees exercised a power of appointment to appoint assets to the principal beneficiary of a trust who then assigned his interest to another trust. The timing meant an exemption from capital gains tax was not available and a liability of £1 million pounds was triggered. The appointment was set aside on the grounds that the fiscal consequences of the disposition were part of the effect which the trustees ought to have taken into account (*Sieff v Fox* [2005] 1 WLR 3811).

How has it been applied in New Zealand?

There are no recent New Zealand cases that have relied upon the rule to set aside trustee dispositions but the rule has been referred to in a number of decisions.

In *Kain v Hutton* [2007] 3 NZLR 349, the Court of Appeal and the High Court noted the English Court of Appeal's decision that, before a review of trustees' decisions was justified on the grounds of inadequate consideration of the subject-matter, it needed to be clear that, had the trustees approached their task more diligently, there were relevant considerations which would have affected the ultimate decision or that there were irrelevant considerations which ought not have been taken into account. In other words, it needed to be clear that any

failure to inquire must have affected the outcome.

Justice Fisher in *Wrightson Limited v Fletcher Challenge Nominees Ltd* (1998) 1 NZSC 40,388 at 40,413 referred to the rule in *Hastings-Bass* when setting out a list of the situations in which a court will set aside trustees' decisions. The list included where the trustees had considered irrelevant considerations and where they had failed to consider relevant considerations.

Because the facts of the cases brought before the New Zealand courts have not supported the application of the rule in *Hastings-Bass*, it is difficult to determine whether the New Zealand courts would apply the rule as generously as their English counterparts.

The future of the rule

To date, the English Court of Appeal has not had the opportunity to consider the rule fully and, when it does, some commentators believe that its application may be restricted or narrowed. However, the rule seems to be fairly entrenched in the UK common law and any change may be slow to occur. It is a useful rule to bear in mind when dispositions made by trustees go wrong.