In depth

Massively discretionary trusts***

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Abstract

Trust drafting practices have changed dramatically in recent decades. A range of considerations has led to an increase in the dispositive discretions held by trustees. In some cases, the trustees' dispositive discretions effectively govern the whole trust structure, leading to what the author calls a 'massively discretionary trust'. These trusts create a series of legal risks. These include the possibility that the trust property is held on resulting trust from the moment of the trust's constitution and the possibility that the beneficiaries can collapse the trust and take the trust property. Some drafting techniques may be based on a misunderstanding of the law; some may invite litigation; and the governing legal principles, as understood by some drafters, may be subject to revision and refinement by the courts. This article will examine some of these possibilities using concrete examples.

Introduction

Trust drafting practices have changed dramatically in recent decades. A range of considerations has led to an increase in the dispositive discretions held by trustees. In some cases, the trustees' dispositive discretions effectively govern the whole trust structure, leading to what could fairly be called a 'massively discretionary trust'. These trusts first became popular in offshore jurisdictions, but have now moved onshore.[1] The goal of this article is to identify a range of legal risks that may arise from this style of trust drafting. I use this term, 'legal risk', in a broad way to cover risks arising from uncertainties about the law, as well as risks of litigation.

Onshore courts may not be as accepting of massively discretionary trusts as some drafters may wish. The relevant legal risks include the possibility that the trust property is held on resulting trust from the moment of the trust's constitution, and the possibility that the beneficiaries can collapse the trust and take the trust property. These and other risks can arise in several ways. Some drafting techniques may be based on a misunderstanding of the law; some techniques may invite litigation; and the governing legal principles, as understood by some drafters, may be subject to revision and restatement by onshore courts. This article will examine some of these possibilities using concrete examples.

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1. For examples, see *Chief Commissioner of Stamp Duties (NSW) v Buckle* [1998] HCA 4, 192 CLR 226 [9]–[25]; *Clayton v Clayton* [2016] NZSC 29, in which the terms of the trust are set out in the Appendix to the judgment; *JSC Mezhdunarodniy Promyshlenniy Bank v Pugachev* [2017] EWHC 2426 (Ch) [106]–[142].

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Terminology

In 2011, the Judicial Committee of the Privy Council gave its advice in *Tasarruf Mevduati Sigorta Fonu v Merrill Lynch Bank and Trust Company (Cayman) Ltd*.[2] Lord Collins, giving the advice of the Board, described the trusts in issue in the following terms:

> Mr Demirel [the settlor] had established two discretionary trusts in the Cayman Islands, with assets of some US$24m. For practical purposes the beneficiaries are Mr Demirel and his wife. ... On 28 June 1999 Mr Demirel executed two deeds of trust, establishing two trusts, the Mana Trust and the Dolphin Trust ('the Trusts'). ... The Trusts are Cayman Islands discretionary trusts, and it is common ground that the Trusts are valid and duly constituted as a matter of Cayman Islands law. The discretionary objects of both Trusts are Mr Demirel, Ayse Nur Esenler, who is now the wife of Mr Demirel, and Mr Demirel's children and remoter issue now living or born afterwards. At present, Mr Demirel has no living children or remoter issue. The residuary beneficiary is charity [*sic*].[3]

There is no rule book for the terminology of trusts, and indeed some of it is surprisingly unstable. Some of the most basic words and phrases—'trust', 'beneficiary', 'discretionary trust'—are ambiguous. This ambiguity can lead to serious misunderstandings about fundamental principles.

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'Trust'

Even the word 'trust' is used in two different senses. The wider sense of 'trust' is that of 'a legal structure in which property is held in trust'. This is the sense that Lord Collins used when he said that the two 'trusts' were called the Mana Trust and the Dolphin Trust. Such a structure can have a whole range of terms, dealing with interests in income and capital; it may give the trustee, or others, or both, dispositive discretions in relation to the trust property; and it likely has any number of provisions on administrative powers, including investment powers. Sometimes, the trust is given a name.

The narrower sense is that of 'an obligation with respect to the benefit of property'. This sense is found in the first sentence of *Underhill and Hayton*.[4] This is the sense that is used when someone examines a particular provision within a trust structure, and asks, 'does it create a trust or a power?'[5] Even if the answer is 'a power', this does not mean that there is no trust structure; there is probably still a trust in the wide sense, since there are other provisions and since property is held in trust by trustees.[6] The conclusion means only that the particular provision does not create a trust in the narrower sense, but rather gives the trustees (or someone) a discretionary power; this

2. *Tasarruf Mevduati Sigorta Fonu v Merrill Lynch Bank and Trust Company (Cayman) Ltd* [2011] UKPC 17, [2012] 1 WLR 1721. The case is noted by L Smith (2013) 129 LQR 332. Although Cayman Islands trust law is different from English law, particularly in relation to the statutory STAR trust, there was no suggestion that the trusts in question were STAR trusts, and there was no reference in the judgment to any differences between English law and Cayman law. In any event, nothing turns on this for the points I wish to make.

3. ibid [4], [9]–[10]. The final sentence appears this way in two law reports, including the Weekly Law Reports. Lord Collins might have meant 'a charity', perhaps a particular charity named in the trust deed; we will return to this issue later on.

4. D Hayton, P Matthews and C Mitchell, *Underhill and Hayton: Law Relating to Trusts and Trustees* (19th edn, LexisNexis 2016) [1.1] (1): 'A trust is an equitable fiduciary obligation, binding a person (called a trustee) to deal with property (called trust property) owned and controlled by him ... for the benefit of persons (called beneficiaries ...) ... any one of whom may enforce the obligation.'

5. This is also the sense that one author had in mind when he recently said that 'discretionary trust' is an oxymoron: J Nitikman, 'Sham, Illusion and All That Jazz: A Case Comment on *Clayton v Clayton*' (2016) 22 *Trusts & Trustees* 180, 180. What the author means is that an obligation cannot be non-obligatory. As I explain below, however, in the subsection 'Discretionary trust', there can be a discretionary trust even when 'trust' is used in the narrow sense.

6. Hence, in *Re Baden's Deed Trusts* [1969] 2 Ch 388 (CA), the Court of Appeal held that cl 9(a) of the settlement created only a power, not a duty or a trust in the narrow sense. But it did not follow that there was no trust anywhere in the story: the settlement still created a trust. The conclusion on cl 9(a) was overruled by the House of Lords (*McPhail v Doulton* [1971] AC 424 (HL)).

implies no conclusion about whether there is a trust in the wider sense.[7]

The overlap between the two senses is that every trust structure—every trust in the wider sense—must include at least one trust in the narrow sense—an obligation with respect to the benefit of the property held in trust. It is because of that obligation that we can say that the property is held in trust; and then we may use the wider sense to refer to the whole structure, discretions and all. Conversely, if there is no trust in the narrow sense, there can be no trust in the wider sense either. This is because if there were no trust in the narrow sense, the 'trustees' would not owe any obligation relating to the benefit of the property; but then, they would not be trustees. And this is why, outside of trusts for charitable purposes, there is no trust unless there is a beneficiary: to say that the trustee owes an obligation with respect to the benefit of the property is to say that someone is owed that obligation.[8] The person who is owed the obligation is a beneficiary. The principle that there must be a beneficiary in order for there to be a trust is usually called the beneficiary principle. A beneficiary is always needed for there to be a trust in the narrow sense; and a trust in the narrow sense is always needed for there to be a trust in the wider sense.[9]

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'Beneficiary'

Even 'beneficiary' is ambiguous. When there is a trust in the narrow sense, not being a charitable trust, the trustee is obliged to hold the trust property for the benefit of one or more persons. They are called beneficiaries: the persons who are entitled to the trust property, even though their entitlements may be vested or contingent, defeasible or indefeasible. That is the strict or narrow sense of the word 'beneficiary'.

But the word has wider senses. We may talk of the beneficiary under a policy of life insurance, or under a will; these persons are not trust beneficiaries. In the trust context, various people may benefit from a charitable trust, and may in a wide sense be called beneficiaries; but they are not beneficiaries of the trust in the strict sense. More importantly, the same is true for objects of a discretionary power, even if it is a power held by trustees, and even if the property in question is held in trust. Assume that the trustees have a discretionary power that allows them, but does not require them, to transfer some or all of the trust property to one or more of the settlor's children. It may be that the children get all of the property, bringing the trust to an end. They benefit. But in their capacity as objects of a power, they are not trust beneficiaries, and they cannot satisfy the beneficiary principle. The reason is that the trustee does not owe

7. Hence, some authors have expressed this question of construction as whether the provision in question creates a power or a *duty:* AH Oosterhoff, R Chambers and M McInnes, *Oosterhoff on Trusts: Text, Commentary and Materials* (8th edn, Carswell 2014) ch 3. This avoids confusion with the wide sense of 'trust' that refers not to a particular provision but to the whole structure.

8. *Underhill and Hayton*, (n 4) [8.146–8.156] argue that non-charitable purpose trusts should be possible in English law, even though this would be inconsistent with their own definition of 'trust' (the inconsistency is acknowledged at 8, fn2). This remains very much a minority view for the common law, and even in jurisdictions where non-charitable purpose trusts are permitted by legislation, they create theoretical problems since they involve assets that beneficially belong to no one: P Matthews, 'From Obligation to Property, and Back Again? The Future of the Non-Charitable Purpose Trust' in D Hayton (ed), *Extending the Boundaries of Trusts and Similar Ring-Fenced Funds* (Kluwer Law International 2002) 203; L Smith, 'Give the People What They Want? The Onshoring of the Offshore' (2018) 103 Iowa L Rev 2155. Why should a person be able to affect assets to some private purpose of his choice, while at the same time insulating those assets from his creditors? The generally accepted onshore common law position is that non-charitable purpose trusts cannot be created, at least outside of the so-called 'anomalous exceptions' (*Underhill and Hayton* (n 4) [8.163–8.174]), which are probably best regarded as powers. But even if this minority view were accepted, it would be based on the argument that there is a trust in the narrow sense: the trustee is obliged to apply the property to the purpose, with the enforcement of that obligation falling to a named 'enforcer'. The traditional view is simply that such an arrangement does not include a genuine obligation, since neither the enforcer nor any other person has a direct interest in the performance of the obligation; see also K Low, 'Non-Charitable Purpose Trusts: The Missing Right to Forego Enforcement' in RC Nolan, KFK Low and TH Wu (eds), *Trusts and Modern Wealth Management* (CUP 2018) 486. A trustee's obligation relating to the benefit of trust property has the effect that his own creditors have no access to that property; outside of the (public) case of charity, someone should (and so should his or her creditors).

9. With respect, this is why it was questionable for French CJ to suggest that it is possible to create a trust in which 'there was no equitable interest in its assets held by anyone': *Kennon v Spry* [2008] HCA 56, 238 CLR 366 [49]; although much depends on what he meant by an 'equitable interest'. If an equitable interest is that which is held by a person who has a right (albeit possibly defeasible, and possibly only as a member of a group) to some of the trust property, then it is not possible. An attempt to do that leads (unless it creates a charitable trust) to an immediate resulting trust, so that the settlor holds an equitable interest. The only alternative is that the property is not held in trust: if you transfer property to someone and *empower* that person to dispose of it in certain ways, but do not *oblige* her to dispose of it in any particular way, you may find that it is hers beneficially (*Re Harbison* [1902] 1 Ir R 103 (MR)). French CJ referred to *Commissioner of Stamp Duties (Queensland) v Livingston* [1965] AC 694 (PC), but the crucial feature and central holding of that decision is that the estate of a deceased person is *not* a common law trust. See L Smith, 'Scottish Trusts in the Common Law' (2013) 17 Edinburgh L Rev 283. The analysis of Heydon J in *Kennon* [170]–[172] is preferable.

them any obligation relating to the benefit of the property. They are not beneficiaries in the strict sense.[10] The beneficiary principle requires the presence of one or more beneficiaries in the strict sense.[11]

The ambiguity of the term 'beneficiary' is illustrated by the passage set out above from the *TMSF* case.[12] Mr Demirel and his wife are said to be beneficiaries '[f]or practical purposes'; then they are described as 'discretionary objects', and 'charity' is said to be the 'residuary beneficiary'. The reason this is important is that objects of discretionary powers are not beneficiaries in the strict sense and cannot satisfy the beneficiary principle. This cannot be changed by calling them 'beneficiaries' in the trust instrument.[13] The beneficiaries, in the strict or correct sense and as a matter of trust law, are the people who will get the trust property if the discretions held by trustees or others are *not* exercised. This is another way of saying that they have a right, albeit defeasible by the exercise of the discretions, to the trust property.

The beneficiary principle requires the presence of one or more beneficiaries in the strict sense

Objects of powers do not have any right to any property. Perhaps less obviously, they do not have a right to enforce the trust, certainly when 'trust' is used in the narrow sense. This is just saying the same thing in a different way, because the trust in the narrow sense is the obligation relating to the benefit of the trust property, and by definition, that obligation is owed to the beneficiaries in the strict sense 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. But it appears that the rights of objects of powers are even more limited than this: they do not have standing to sue for breach of trust. In *Re Manisty's Settlement*,[14] Templeman J said:

> The court cannot insist on any particular consideration being given by the trustees to the exercise of the power. ... If a person within the ambit of the power is aware of its existence he can require the trustees to consider exercising the power and in particular to consider a request on his part for the power to be exercised in his favour. The trustees must consider this request, and if they decline to do so or can be proved to have omitted to do so, then the aggrieved person may apply to the court which may remove the trustees and appoint others in their place. This, as I understand it, is the only right and only remedy of any object of the power...

It may also be that in an appropriate case, albeit an unusual one, the court might exercise the discretion itself.[15] But the point is that the object's rights are limited to ensuring the proper exercise of the power.

This might seem surprising. If a trustee had misappropriated property, or had made negligent investments, or was about to enter into a transaction in a conflict of interest, or had secured an unauthorized profit, should not the object of a power have standing to complain? There seems to be no onshore authority that affirms such a proposition, and a moment's reflection shows why this is the case. The object, by definition, has no right to any of the trust property. All of the actions that a beneficiary may take that are related to the proper administration of the trust are different ways of ensuring that the trust property is preserved, protected, and properly applied; but only a

10. To be clear, in this section I am addressing the case of a power which the trustees (or others) can choose to exercise or not to exercise. I am *not* addressing the less common case in which the trustees are *obliged* to distribute some property among a class of beneficiaries, but have a choice as to which of them shall receive it. That situation is discussed in the next section.

11. The word 'object' also has wide and narrow senses. In a wide sense, it includes both beneficiaries in the strict sense, and those who are merely objects of powers. It might even include charitable purposes. This is the sense used when we say that every trust (and every power) must satisfy the relevant test of certainty of objects. The narrow sense contrasts objects (of non-obligatory powers) with beneficiaries in the strict sense. Generally in this article, I use the word 'object' in the narrow sense.

12. See n 3.

13. *Kennon* (n 9) [125] (Gummow and Hayne JJ).

14. *Re Manisty's Settlement* [1974] Ch 17, 25. This summary of the law was based on leading cases such as *Re Gulbenkian's Settlement* [1970] 1 AC 508 (HL) and *McPhail* (n 6).

15. *Mettoy Pension Trustees Ltd v Evans* [1990] 1 WLR 1587, 1617–18.

beneficiary has any right to any of that property. In other words, trustees' duties relating to the proper administration of a trust are essential to the performance of the trust in the narrow sense, and those duties are owed to the beneficiaries.

Objects of powers do not have any right to any property

If the object of a discretionary power were allowed to enforce the proper administration of the trust, it seems that she would effectively be enforcing the rights of someone else: namely, the beneficiary. But by what authority? Against that, one might say that since the trust property is the property which the object has a possibility of acquiring, therefore the object of a power has a right that the trust be properly administered. But this does not follow; indeed it begs the question. Just because one has a hope of acquiring something, it does not follow that one has a right to its preservation. If Albert's current will leaves his house to Brenda, she has a possibility of acquiring the house, but it does not follow that she has any right to secure its preservation.

Moreover, such a proposition would lead to strange results. First, if objects of powers had rights of enforcement, there should be no problem about creating non-charitable purpose trusts; one would only have to add a power, and there would be a person (or more than one) with a right to supervise and enforce the proper administration of the trust. In other words, the proposition that objects of powers can enforce the proper administration of a trust is straightforwardly inconsistent with the beneficiary principle.[16] Moreover, many trusts of the kind with which this article is concerned have powers with a very wide range of objects: the objects of such a power might well be anyone in the world, perhaps excluding the trustees. Are we to think that in such a case, anyone in the world has the right to enforce the proper administration of the trust? Is everyone in the world owed the fiduciary obligations of trusteeship? That is not English law.[17] It is certainly not what the drafters of such trusts must think.[18]

Are we to think that in such a case, anyone in the world has the right to enforce the proper administration of the trust?

'Discretionary trust'

The term 'discretionary trust' is also ambiguous, its ambiguity corresponding to the different senses of 'trust'. When the phrase 'discretionary trust' uses 'trust' in the wide sense, then the phrase means 'a trust structure in which the trustee, or someone, holds (some or many) dispositive discretions'. It is not a term of art.[19]

When I was small, I was taught that 'discretionary trust' *is* a term of art, and has a very precise meaning.

16. Richard Nolan has argued that objects of powers have standing to enforce trust administration: R Nolan, 'Invoking the Administrative Jurisdiction: The Enforcement of Modern Trust Structures' in PS Davies and J Penner (eds), *Equity, Trusts and Commerce* (Hart 2017) 151,160–68. The only case that he cites directly on point, however, is from Jersey. That decision relied on *Schmidt v Rosewood Trust Ltd* [2003] 2 AC 709 (PC) 714; I will argue below (in the section 'Rights to information') that the reasoning in *Schmidt* is doubtful, as is its authority in English law. Moreover, Jersey allows non-charitable purpose trusts, and so has abandoned the beneficiary principle; it systematically allows trusts to be enforced by non-beneficiaries. On the substance, Nolan argues (168) that because objects of powers have some rights 'in relation' to a trust fund (such as those identified in the extract above from *Re Manisty's Settlement* (n 14)), therefore they have standing to enforce the trust. But this simply does not follow; having some rights does not give you more rights, nor a right to assert the rights of another (the beneficiary). *Re Manisty's Settlement* says that the rights it identifies are the only rights of an object, and this seems to be inherent in the difference between being an object and being a trust beneficiary.

17. In *McPhail* (n 6), the House of Lords held that while a class of objects of a power can be extremely wide, a class of trust beneficiaries cannot be; it must not be 'administratively unworkable' (457). It would be impossible to make sense of this holding, which referred explicitly to the beneficiary principle, if objects of powers had the same enforcement rights as trust beneficiaries.

18. In the section 'Rights to information' we will examine the holding in *Schmidt* (n 16) that the court has a discretion as to whether objects of powers can demand information about the trust, and the suggestion in the same case that even trust beneficiaries do not have a right to such information. So far as I know, the courts have not suggested that they have a discretion as to who can enforce the proper administration of the trust property, although Nolan (n 16, 166–67) argues that this is the law, going so far as to suggest that trust beneficiaries may not always have rights of enforcement. It is unclear what theory of the trust underlies this approach; it seems to suppose that a trust is an institution of public law rather than one constituted of private, bilateral rights and obligations. In the Section 'Rights to information', I side with what I assume to be the traditional position, as stated by Millet LJ in *Armitage v Nurse* [1998] Ch 241 (CA) 253: 'If the beneficiaries have no rights enforceable against the trustees there are no trusts.'

19. The High Court of Australia has said of this sense of the term 'discretionary trust' that it 'has no fixed meaning and is used to describe particular features of certain express trusts': *Chief Commissioner of Stamp Duties* (n 1) [8].

Using 'trust' in the narrow sense, it means a trust—an obligation with respect to property—that is discretionary even while it is obligatory. Thus, it refers to the particular situation in which the trustees are obliged to distribute property—all of it—but at the same time have a discretion as to which members of a group or class shall receive the property in question. This sense of the phrase is now much less common than the wide sense, probably because such structures are rarely created; but it was used in the leading case of *McPhail v Doulton*,[20] and it is still encountered.[21] Since the trustees are obliged to distribute the property, it is sometimes described by saying that the trustees have only a power of selection. A discretionary trust in this narrow sense creates a situation in which all the members of the class are trust beneficiaries in the strict sense, even though none of them individually has a right to any of the property. This is because, collectively, they are entitled to the property.[22] In this respect, they are very different from the members of the class of objects of a dispositive discretion, who are not entitled to anything, even collectively.

The ambiguity of the phrase 'discretionary trust' can cause confusion. Lord Collins was almost certainly using the wider sense in *TMSF*.[23] If there were a discretionary trust in the narrow sense, whose beneficiaries were Mr Demirel and his family, then there could be no 'residuary beneficiary', because there would be an obligation to dispose of all the property among the beneficiaries of the discretionary trust.[24] Alternatively, if (as seems to have been the case) Mr Demirel and his family were only objects of powers, and there was a single residuary beneficiary, then there was not a discretionary trust in the narrow sense. There was a fixed trust, for the residuary beneficiary, but the interest of that beneficiary was defeasible by the exercise of the powers.

In the title of this article, I adopt the wider sense of the phrase 'discretionary trust'. I am not (or not usually) discussing discretionary trusts in the narrow *McPhail v Doulton* sense, but rather the kind of trusts in which the trustees (or others) hold very wide discretionary dispositive powers.[25]

'Default beneficiary' or 'residuary beneficiary'

Finally, we turn to what Lord Collins meant when he said that the trusts had a 'residuary beneficiary'. What did he mean? In a will, it is normal to have a residuary legatee, or a residuary beneficiary. This is the beneficiary who takes the residue of the estate, after creditors have been paid and particular legacies have been fulfilled. In an estate, of course, the residue is uncertain until it is ascertained by estate administration. There might be nothing at all if the deceased's debts are large.

In a trust, traditionally, there is no residuary beneficiary. Why not? Traditionally, trust instruments dispose of income interests and capital interests. If you have disposed of all of the income and all of the capital, you have disposed of everything and there can be no residue. Moreover, the capital interests do not have the aleatory or uncertain character that goes with the residue of an estate. This is because in a traditional trust, there is nothing corresponding to

20. In *McPhail* (n 6), the House of Lords held that cl 9(a) of the deed created a discretionary trust in this narrow sense. The terminology of 'discretionary trust' was used in argument, along with the alternative label 'trust power' (which is another way of capturing the combination of obligation and discretion). Lord Wilberforce in his leading speech called it both a 'trust power' (eg 448–49, 452, 455–56) and a 'discretionary trust' (eg 451–54, 457). As is well known, the holding (by a majority of three to two) was that, for a discretionary trust in this narrow sense, the applicable test for certainty of objects is 'individual ascertainability', so that it is not necessary to be able to compile a complete list of the beneficiaries of such a trust in order for it to be valid. The dissenters may well have had the better of the argument: is it possible to owe a legal obligation, relating to the benefit of property, to all the members of an unascertained class of persons?

21. It was called a 'true discretionary trust' in argument in *Schmidt* (n 16): '. . . it imposes an obligation to distribute and one or more of the beneficiaries must therefore receive the entirety of the fund'. See also *Mettoy Pension Trustees Ltd* (n 15) 1614. The terminology is also adopted in Oosterhoff, Chambers and McInnes (n 7) 21.

22. For this reason, it is not easy to describe what interest each of them has individually. It is possible that this is the structure that French CJ had in mind in *Kennon* (n 9).

23. See n 3.

24. In the same way, if 'discretionary trust' is given this meaning using 'trust' in the narrow sense, the idea of a 'non-exhaustive discretionary trust' is a contradiction in terms. If distribution of the relevant property is not obligatory, the relevant provision does not create a trust but a power.

25. For this reason, when I refer to the 'object of a power', I mean an object of a power who is *not* a beneficiary in the strict sense. In other words, I do not mean to include the beneficiary of a discretionary trust in the *McPhail* sense. Such a person is a trust beneficiary, and is also in a sense the object of a power (of selection).

particular legacies, nor anything corresponding to the debts of a deceased person: that is, pre-existing claims that have priority over the rights of the estate beneficiaries.[26]

It is the evolution of trust drafting that has led to the creation of a 'residuary' or 'default' beneficiary. Dispositive discretions have moved from the margins of trust drafting to the centre. Dispositive discretions are not by any means a new phenomenon. During much of the 20th century, they frequently qualified or limited the traditional interests that carved up the income and the capital. For example, someone holding a capital interest might find that the capital could be reduced if the trustee exercised a power over that capital. In this sense, the capital interest was defeasible. In a traditional family trust structure, the objects of dispositive discretions would typically be the same people who held the income or capital interests. So when the capital was reduced through the exercise of a dispositive discretion, it might well be the case that the discretion was exercised in favour of one of the persons who held the capital interest.[27]

It is the evolution of trust drafting that has led to the creation of a 'residuary' or 'default' beneficiary

More recent drafting styles may take dispositive discretions to an extreme: the objects of the trust, the people who are intended to benefit, may have *nothing but* the hope of receiving property via the exercise of dispositive discretions. In one version, illustrated by Tasarruf Mevduati Sigorta Fonu, they do not hold any defined interests in the income or capital, not even defeasible ones; they are only the objects of powers, which are dispositive discretions. This means that they have no right to the trust property or to any part of it; they only have the hope that these discretions will be exercised in their favour. The residuary beneficiary might be one or more named charities, or 'charity' in general, which is why the term 'Red Cross trust' is sometimes used to describe this kind of trust.[28]

In another version, which for the time being at least is more commonly found in onshore trusts, there is some commonality between the objects of the very wide dispositive discretions held by the trustees, and the residuary beneficiaries. That is, the intended objects are residuary beneficiaries as well as being the objects of the trustees' dispositive discretions.[29] But as in the Red Cross trust, it is likely that the trustees have the power to add or remove people from the class of objects of their wide dispositive discretions, and possibly to modify the class of residuary beneficiaries. The trustees also have the power to bring the trust to an end at the time of their choosing, since their dispositive discretions extend to all of the trust property; again, therefore, the interests of the beneficiaries in that capacity—in the capacity of beneficiaries—are entirely defeasible.[30] As in the Red Cross trust, the expectation in this 'family' version is that the trust property will be distributed by the trustees pursuant to their wide dispositive discretions, rather than via

26. The costs of trust management do have priority, but unlike the debts of a deceased person, these costs would rarely amount to more than a small percentage of the trust fund.

27. This is the structure of the statutory power of advancement that appears in s 32 of the Trustee Act 1925, which is inserted by legislation into English trusts unless it is expressly excluded (s 69(2)).

28. In argument in *Schmidt* (n 16, 711) it was said that in most offshore trusts '. . .(iii) the persons intended to benefit are not true beneficiaries but mere objects of those discretionary powers; while (iv) the only beneficiary properly so called is a charitable institution (hence the generic designation ''Red Cross trust'') having no connection with the settlor and never intended to benefit, except by default . . .'.

29. See, for example, the trust deed in *Clayton* (n 1), where the 'final beneficiaries' were the children of the settlor (cl 2.1). That trust also provided for other relations to be beneficiaries, should one or more of the children die before the trust came to an end (cls 10.1 (b), (c)). See also *Pugachev* (n 1) [124].

30. The details depend on the drafting. If the trustees have a power of appointment, as that term is traditionally (but no longer always) used, it is a power to 'appoint' fixed interests which remain trust interests. This may create a bare trust, which may be ended when and if the beneficiary chooses. If the trustees have a power of advancement, they hold a power to transfer property out of the trust to the objects of the power (and the term 'power of appointment' is sometimes used to describe such a power). If such a power extends to all of the trust property, its exercise can lead to the end of the trust at any time, and such a power is typical in massively discretionary trusts. The label 'advancement' itself has multiple meanings: sometimes it refers to a power to give capital to a person who already has a capital interest, vested in interest but not in possession (see n 27). Sometimes it only means that the power allows the object to be 'advanced' and benefitted, regardless of whether he or she has a capital interest. See DWM Waters, M Gillen, and L Smith, *Waters' Law of Trusts in Canada* (4th edn, Carswell 2012) 1190–93, 1199–200, and *Kain v Hutton* [2008] NZSC 61, [2008] 3 NZLR 589. Whether the use of the word 'advancement' restricts the reasons for which such a power can be used is largely a question of drafting.

the 'default clause' that identifies the residuary or default beneficiaries.

These are what I mean by 'massively discretionary trusts': trust structures in which the trustees' dispositive discretions do not merely qualify the beneficial interests, but effectively displace them, one might even say overwhelm them.[31] Contrary to what Lord Collins said about Mr Demirel and his wife, people in their position are not, at least in the Red Cross version, beneficiaries in the strict sense of that word, since they do not hold any definable beneficial interest. They are only objects of powers. But according to the beneficiary principle, *someone* has to be the beneficiary; someone has to have a right to the trust property, even if it is a defeasible right, or we will not have a trust. Or, to state the same issue from the other end, if we *do* have a trust, and we cannot identify any beneficiary in the trust instrument, then the beneficiary will be the settlor under a resulting trust. That is the lesson that Mr Vandervell learned the hard way.[32]

These are what I mean by 'massively discretionary trusts': trust structures in which the trustees' dispositive discretions do not merely qualify the beneficial interests, but effectively displace them, one might even say overwhelm them

In my view, it is a mistake to think that the residuary or default beneficiary is only there to deal with the very unlikely case in which all of the intended objects were to die.[33] If the intended objects are not beneficiaries in the strict sense, but are only objects of discretions, then the default clause is needed from the moment of constitution in order to ensure the validity of the trust. It is needed to satisfy the beneficiary principle. It names one or more beneficiaries, which the objects of the discretions are not.[34]

If the intended objects are not beneficiaries in the strict sense, but are only objects of discretions, then the default clause is needed from the moment of constitution in order to ensure the validity of the trust

The label 'residuary beneficiary' is doubly curious. 'Residuary' is misleading because, unlike in the case of a will, there is no intention that there shall be any residue at all. 'Beneficiary' is misleading because, at least in the Red Cross version, there is no intention that this entity shall receive any benefit from the trust, even though it may be the only beneficiary in the proper usage of that term.[35] That beneficiary is there for a very specific purpose, which does not

31. Particularly in the offshore, such trusts may well have a 'protector', a person who holds (whether or not in a fiduciary capacity) some rights or powers of supervision or oversight. The presence of such a person does not address any of the concerns that I raise in this article, although it may exacerbate some of them. For an onshore example see *Pugachev* (n 1), in which it was held ([178]–[179], [182], [267], [278]) that the settlor's non-fiduciary powers as a protector had the effect that he was the beneficial owner of all of the trust assets.

32. *Vandervell v IRC* [1967] 2 AC 291 (HL).

33. This seems to be implied by JK Kessler, *Drafting Trusts and Will Trusts* (12th edn, Thomson/Sweet & Maxwell 2014) [5.44]. Kessler recommends drafting trusts that are massively discretionary. His book now has a number of spin-off versions in other jurisdictions: see JK Kessler and F Hunter, *Drafting Trusts and Will Trusts in Canada* (3rd edn, LexisNexis 2011); JK Kessler and M Flynn, *Drafting Trusts and Will Trusts in Australia* (Thomson Lawbook Co 2008); JK Kessler and C Lee, *Drafting Trusts and Will Trusts in Singapore* (Sweet & Maxwell Asia 2007); JK Kessler and S Grattan, *Drafting Trusts and Will Trusts in Northern Ireland* (3rd edn, Bloomsbury Professional 2012); JK Kessler and T Pursall, *Drafting Cayman Islands Trusts* (Kluwer Law International 2006); JK Kessler, N Chand and T Pursall, *Drafting British Virgin Islands Trusts* (Sweet & Maxwell 2014).

34. One of Kessler's proposed techniques for dealing with uncertain future events is to expand greatly the class of defined 'beneficiaries' (Kessler ibid [5.48]). But what his clause calls 'beneficiaries' are only objects of powers; it is only those named in what he calls the 'default clause' who are beneficiaries in the strict or technical sense. Even with a massive class of objects of powers, a genuine beneficiary—a beneficiary in the strict sense—is needed to satisfy the beneficiary principle. A genuine beneficiary is someone who is *entitled* (even if defeasibly) to the trust property or some of it. At [29.4] Kessler mentions the possibility of a trust that names no beneficiaries, and suggests that there is a risk that it would be declared a sham; but in fact such a trust cannot be created in the common law, unless it be valid as a purpose trust, which means that it must be exclusively charitable (n 8).

The reverse point is illustrated by *Clayton* (n 1), where the 'final beneficiaries' were defined (by cl 2.1) to be the children of the settlor. The judges of the Supreme Court seemed to assume that this meant that the only ('final') beneficiaries were his two daughters: [10], [46], [93]. But any future child born to the settlor would also be a ('final') beneficiary (cl 2.1, 'final beneficiaries'). More importantly, the question who is a beneficiary is not settled by the definition clause of the trust deed, but rather by the interests created; again, the beneficiaries in the strict sense are the people who will get the trust property if the discretions held by trustees or others are not exercised. This is why, in massively discretionary trusts, it is typically the default clause that identifies the beneficiaries. In *Clayton* (n 1), if one or more of the children had died when that clause came into operation, other persons (their issue, or ultimately the next of kin of the settlor) would take the property (cls 10.1 (b), (c)). Thus, there was a class of potential future beneficiaries in addition to the daughters, even though none of those potential beneficiaries were called 'beneficiaries' or 'final beneficiaries' in the trust deed.

35. In the 'family' version, the default beneficiaries may be or include the persons who are intended to benefit. Even here, however, like in the Red Cross version, it is probably intended that they will benefit only as objects of powers, via the trustees' use of their dispositive discretions.

include receiving any benefit from the trust. It is there to satisfy the beneficiary principle.

Charitable and non-charitable trusts

As mentioned, the term 'Red Cross trust' is sometimes used to describe the kind of trust in which the role of default beneficiary is played by one or more charities. The settlor who creates such a trust, however, does not intend to create a charitable trust. It is said to be a fundamental principle of the common law that in order to be valid, a charitable trust must be exclusively charitable.[36] That is not the nature of a Red Cross trust. The intention is that the objects of discretionary powers will receive all of the benefit, even though they are not beneficiaries in the strict sense. And still less, is it desired to bring such a trust under the authority of the Attorney-General, or the supervision of the Charity Commission? It is intended to be a private, or non-charitable, trust.

But here is a question worth considering: is there anything problematic about a non-charitable trust that has no beneficiaries, in the strict sense, except one or more charities? I am assuming all along that the trustees have wide dispositive discretions. The question is, for whom do they hold the trust property in trust, subject to the exercise of those discretions? In the terms we have been using, who is the residuary or default beneficiary? Let me present three different possibilities for the drafting of such a trust. The first is that no particular charity is named as the default beneficiary. It is conceivable that this is what Lord Collins meant when he said that '[t]he residuary beneficiary is charity.'

Such a clause might be as follows: that subject to the trustees' dispositive discretions, typically in favour of family members, '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'.[37] I suggest that this clause is invalid, when combined with powers in favour of named individuals. Why? It does not satisfy the beneficiary principle. It does not name a beneficiary. Charitable trusts, or, what is the same thing, trusts for charitable purposes, do not have to satisfy the beneficiary principle; they are valid as purpose trusts. But on the other hand, such trusts are valid only if they are exclusively charitable.[38] You cannot take the benefit of some features of the law of charity while opting out of the ones you do not like.

You cannot take the benefit of some features of the law of charity while opting out of the ones you do not like

It might seem controversial for me to suggest that it is not valid. Someone might say that it is perfectly possible to have a trust structure in which the trustees are empowered to make gifts to charity. This, however, would be a trust for persons, with charity (or one more named charities) named as the object of dispositive discretions. In such a trust, the beneficiaries are persons, albeit with defeasible interests. The charities are only objects of powers. Such a structure does not include a charitable trust. Another trust structure might have both non-charitable beneficiaries and an obligatory charitable disposition. For example, I might create a trust in which the income is to go to a particular person, Mary, during her life, and then on Mary's death, the capital is to go to charitable purposes.[39] That could be perfectly valid. But the two dispositions are of different property. The income, as

36. *Morice v Bishop of Durham* (1805) 10 Ves Jun 522, 32 ER 947 (LC) 541–42, 954–55; *Chichester Diocesan Fund & Board of Finance Inc v Simpson* [1944] AC 341; H Picarda, *The Law and Practice Relating to Charities* (4th edn, Bloomsbury Professional 2010) 326–27; W Henderson, J Fowles and J Smith, *Tudor on Charities* (10th edn, Sweet & Maxwell 2015) 300–03; Kessler (n 33) [25.6].

37. Taken from an example in J Penner, *The Law of Trusts* (8th edn, OUP 2012) 53; cf Kessler (n 33) [29.4], who mentions the possibility of naming as default beneficiary 'such charities as the trustees shall determine.' In *Chief Commissioner of Stamp Duties* (n 1) [20], the trust deed before being amended provided that the ultimate beneficiaries were charities to be selected by the trustees, but only if the named default beneficiaries died without issue. This is a different case because the property is not held on charitable trusts from the moment of constitution; the obligation to so apply it would arise only if prior beneficial interests (some vested and some contingent) were extinguished. An object of a power does not have a beneficial interest.

38. Here I am using the term 'trust' in the narrow sense, of an obligation relating to the benefit of property.

39. Compare *Re Barton* [2002] EWHC 264, but note that the charity designated to take the capital was in the form of a legal person. On the other hand, the testator named particular charitable purposes. The case will be further discussed below.

it arises, is held in trust for Mary; the capital, for the charity. Moreover, the capital gift is vested (to the extent that this concept can apply to charitable purposes), but vested only in interest, not in possession. During Mary's life, the trustees are not obliged to apply the capital to charitable purposes; indeed, that would be inconsistent with investing it so as to generate income for Mary.

In the type of trust that I described earlier, however, that is not the structure at all.[40] Rather, all of the property (capital and income) is held in trust for charity, while at the same time all of the property (capital and income) is available to the trustees for the exercise of their dispositive discretions in favour of non-charitable objects. That, I suggest, is not possible. It would mean that from the moment that such a trust were constituted, the trustees would be holding the property on charitable trusts and would be obliged to use the property for the charitable ends—except such property as they distributed to non-charitable objects. One might say, in line with the discussion in the preceding paragraph, that so long as the trustees hold their dispositive discretions, they are not obliged to apply the property to charitable objects. But that does not solve the problem. From the moment of its creation, this structure has mixed objects, non-charitable objects and charitable objects; but the non-charitable objects are not trust beneficiaries. They cannot satisfy the beneficiary principle; objects of a power do not have standing to enforce the trust.

The result is that the only trust in the narrow sense—the only obligation with respect to the property—is the charitable trust; but a charitable trust must be exclusively for charitable objects, or else it fails.[41]

This problem seems obvious if you think of it the other way around. Imagine that I told my solicitor I wished to create a charitable trust. I name a perfectly valid charitable object, in such a way that there is a clear public benefit. Then I tell the solicitor, 'I would also like the trustees to have the power to give any or all of the property to a named class of persons, for their benefit, namely me and my immediate family.' Surely the solicitor will say that this is not possible. And it is no more possible when the charitable purpose comes at the end, as a so-called default clause, than when the charitable purpose comes first and is later qualified by powers for non-charitable objects. Validity does not depend on the order in which provisions are drafted.

Validity does not depend on the order in which provisions are drafted

If the default clause is invalid, then there is probably a resulting trust. The discretionary powers may stand, if they are severable, but the role of the default beneficiary will be taken by the settlor or her estate.[42] It goes without saying that this may have unintended consequences, in relation to taxation, division of family property, access by the settlors' creditors, or other matters. The only other possibility would appear to be that the discretionary powers could be held invalid as repugnant to the charitable trust; this outcome would mean that the trust was a charitable trust from the moment of its constitution. In most cases, that would be an even worse outcome from the settlor's point of view, because it would mean that the trust would be subject to public regulation and all of the property would have to be applied to charitable purposes.

A second drafting solution is to use one or more named charities. I would suggest that even here there could be a validity problem, if the named charity is itself in the form of a trust. A disposition in favour of a named charitable *trust* is not a trust for persons; it is a settlement of property on charitable trusts.[43] It must

40. See text at n 37.

41. Picarda (n 36) 326–27: '. . . if a gift or trust is to be upheld as charitable, the application of the funds to charitable purposes must be obligatory'. The power in favour of non-charitable objects obviously means that the application of the funds to charitable purposes is not obligatory.

42. See *Re Sayer* [1957] Ch 423, in which a discretionary trust (in the narrow sense) was held void (the result would be different after *McPhail* (n 6)), leading to a resulting trust, but the dispositive powers were valid.

43. Even if it obliges the original trustees to transfer the property to other trustees to pursue those purposes; compare *T Choithram International SA v Lalibai Thakurdas Pagarani* [2001] 1 WLR 1, [2001] All ER 492 (PC).

be exclusively charitable or it will not be valid. It would seem, then, that the same validity problem will arise if the default beneficiary is a named charitable trust. The disposition purports to be charitable, but is not exclusively charitable.

Most charities, however, are now legal persons. This is a third drafting solution. If one or more *persons* are named as default beneficiaries, then the beneficiary principle will be satisfied; the fact that they happen to be charities is not relevant to this question.[44] We will see below, however, that this structure creates other potential problems.

To conclude this section: the first legal risk in some massively discretionary trusts is a serious one: invalidity of the default clause, leading to a resulting trust of the only beneficial interest, in the strict sense. This may arise if the purported structure is that the trustees hold the property on trust for charitable purposes from the moment of constitution, while also having dispositive discretions in favour of non-charitable purposes. To avoid it, I would suggest, drafters who wish to use charities as the only default beneficiaries must select one or more named charities that are in corporate form. Let us see, however, where that leads.

Rights to information

Why do drafters create massively discretionary trusts? One reason is to give the trustees flexibility to react to unforeseen circumstances. This surely lies at the origin of the addition of dispositive discretions to family trusts, many decades ago. Another reason is that such a structure may make it difficult or impossible to place a value on the interest of a beneficiary, or an object of a power; this may have significant taxation consequences.[45] This may also make it practically impossible for that person to alienate his or her interest for a capital sum, which might be an important drafting objective. Some drafters may hope that this difficulty of valuation may mean that an object's interest will not be considered divisible property in the case of the breakdown of a cohabitational relationship.[46] Some may also intend that the presence of very wide discretions will make it impossible for the objects or beneficiaries of the trust to invoke the rule in *Saunders v Vautier*[47] and collapse the trust; we will return to this in a later section.

At this point there is a narrower question: assuming that a drafter is going to create a massively discretionary trust, why would he or she use charity, or one or more named charities, as default beneficiaries, when there is no intention to benefit the charity in question? Why not simply name, as default beneficiaries, one or more of the people who are objects of the dispositive discretions, as in the 'family' version of the massively discretionary trust?[48]

When charity or charities are named as a backstop to family members who are themselves genuine beneficiaries (and not merely objects of powers),

44. In charitable trusts, the validity of the trust turns on its being exclusively charitable. A charity in the form of a legal person is constituted as a legal person under statutory authority (or possibly by a royal charter), so its existence is not in question. Its obligation to use property it acquires for charitable purposes arises separately, from its constitution and (in English law) from the Charities Act 2011.

45. Following the death of the Duke of Westminster in 2016, *The Guardian* published a story entitled 'Inheritance Tax: Why the New Duke of Westminster Will Not Pay Billions' (11 August 2016, <www.theguardian.com> accessed 28 March 2019) , in which a financial advisor explained this effect in simple terms: 'The benefits of trusts are that they don't form part of somebody's estate . . . In a discretionary trust, you have a whole pick list of potential beneficiaries which the trustees can choose to appoint benefits to. Because of that, you can't point a finger to any potential beneficiary and say that's your money. Money can stay in the trust and cascade down from generation to generation and nobody pays inheritance tax on it.' The last assertion is not correct; as the story notes, '. . . trusts are subject to charges every 10 years from the anniversary of their creation. Known as the inheritance tax periodic charge, it can amount to 6% of the funds held.'

46. For an example, see *Clayton* (n 1). The settlor was the former husband, who was also the sole trustee and one of the objects of the trustee's discretions; he held, in his personal capacity, a power to add and delete persons as objects of the trustee's powers; as trustee, he could dispose of all of the property to any of the objects, and he was authorized by the trust deed to exercise the powers that he held as trustee for his own benefit (cl 14.1) and to treat the objects (of which he was one) unequally (cl 11.1). Even so, he had no defined interest in the trust, and it was argued that as a result, it was not part of the 'relationship property' that had to be divided with his former wife. The holding was, however, that the range of powers and discretions that he held were themselves 'relationship property', whose value was assessed as the value of the trust fund. This was the inevitable result of a purposive interpretation of the governing family property legislation; cf *Kennon* (n 9); *Grosse v Grosse* 2015 SKCA 68, leave to appeal to SCC refused 2016 CanLII 7608. But even in the absence of such legislation, a power that one can use for one's own benefit may itself be an asset available to one's creditors, as shown in *TMSF* (n 2) and in *Pugachev* (n 1) [178]–[179], [182], [267], [278].

47. (1841) Cr & Ph 240, 41 ER 482 (LC).

48. This variation was mentioned above, see text at n 29.

the trust is probably a settlement (a trust created by a living settlor), and the explanation may lie in taxation law.[49] Under modern taxation statutes, a settlement may attract adverse taxation consequences if there is any chance that the settlor will derive a benefit from it. If, for example, the beneficiaries are the settlor's children and remoter issue, it is conceivable (regardless of the actual facts) that all of those children and issue will die before the settlor. Thus, whether or not that happens or is likely to happen, the mere possibility may mean that the settlor has some chance, however remote, of benefitting from the settlement, because if all the named beneficiaries were to predecease the settlor, there would be a resulting trust for him or her. And this may attract a taxation rule whose effect may be that the trust is ignored for taxation purposes.

Some reported cases, arising in offshore jurisdictions, reveal a different approach, in which the real objects of the trust—those who are intended to benefit—do not have a beneficial interest, but are *only* objects of dispositive discretions. Some settlors wish to conceal their trusts, so far as they can, even from the persons whom they expect might or will benefit.[50] Some settlors may have created trusts of this kind on the view that the difference between being a trust beneficiary and being the object of a dispositive discretion made a big difference in relation to rights to information. Thus, making persons only objects of powers, and not beneficiaries, might reduce their ability to find out about the trust (its existence and terms, the property held in trust, and so on). It is important to remember that in this kind of structure, at least in jurisdictions where the beneficiary principle applies, the default or residuary beneficiary plays a very important role, because it is the only beneficiary in the strict sense and it is therefore necessary for the validity of the structure (at least, if a resulting trust is to be avoided).

Some settlors wish to conceal their trusts, so far as they can, even from the persons whom they expect might or will benefit

The view that objects of powers have no rights to information was called into question in 2003 by another Privy Council case, namely *Schmidt v Rosewood Trust Ltd (Isle of Man)*.[51] Here Lord Walker of Gestingthorpe described a sub-species of massively discretionary trust in these words:

> The trusts and powers contained in a settlement established in such circumstances may give no reliable indication of who will in the event benefit from the settlement. Typically it will contain very wide discretions exercisable by the trustees (sometimes only with the consent of a so-called protector) in favour of a widely-defined class of beneficiaries. The exercise of those discretions may depend on the settlor's wishes as confidentially imparted to the trustees and the protector. As a further cloak against transparency, the identity of the true settlor or settlors may be concealed behind some corporate figurehead.[52]

A trust that aims to create a cloak against transparency is what some people call a black hole trust.[53] It is certainly not the case that every massively discretionary trust aims to create such a cloak, but some

49. See the summary of part of *Chief Commissioner of Stamp Duties* (n 37). This structure does not attract the invalidity risk described in the previous section, even if the charities are not named corporate charities, because the property is not held on charitable trusts at the moment of constitution. The charitable trusts arise only upon the satisfaction of conditions precedent.

50. This is a desire which is expressly catered for in some offshore jurisdictions, most notably via the Cayman STAR trust: '[o]nly the enforcer can enforce the trust and beneficiaries, as such, have no standing to enforce the trust or obtain information in relation to the trust. . .': GJR Stein, 'Cayman STAR Trusts: Three Years On' (2000) 7 *Trusts & Trustees* 28, 28.

51. See n 16.

52. ibid [1]. Note that Lord Walker here uses the word 'beneficiaries' to refer to objects of powers who are probably not beneficiaries in the strict sense (section 'Terminology', subsection 'Beneficiaries').

53. P Matthews, 'The Black Hole Trust: Uses, Abuses and Possible Reforms' [2002] Private Client Business 42, 110. Paul Matthews has also used the term 'blind trust': P Matthews, 'In the Land of the Blind, the One-eyed Salesman is King' (1998) 2 Jersey L Rev 143. In North America, at least, a 'blind trust' refers to a trust in which the beneficiary (often a politician) voluntarily gives up her right to know how the trust property is invested; this is a tool commonly used to deal with possible conflicts of interest.

clearly do.[54] To some extent, *Schmidt* defeats such goals, because it rejected the view that an object of a dispositive discretion has no standing to obtain information about a trust. The decision restated the conceptual basis for trustees' obligations to disclose information to trust objects. According to *Schmidt*, those obligations are not based on beneficiaries' equitable ownership of the trust property; rather, it was said, they are based on the court's inherent jurisdiction to supervise the administration of trusts. A leading textbook suggests, rightly in my view, that it is the accountability of trustees that is the foundation of their obligation to produce information.[55]

Although Schmidt *could be said to have improved the position of objects of powers regarding access to information, it might also be said to have worsened the position of beneficiaries*

Although *Schmidt* could be said to have improved the position of objects of powers regarding access to information, it might also be said to have worsened the position of beneficiaries. According to the advice of the Board in *Schmidt*, even beneficiaries no longer have a right, in the strict sense, to information about the trust. Lord Walker made one comment that seems to address massively discretionary trusts: he said it would be in the discretion of the court whether any information should be available to a 'beneficiary with only a remote or wholly defeasible interest'.[56] That would seem intended to speak to the 'Red Cross' kind of residuary beneficiary.

I can understand this position, but I agree with Lusina Ho that it needs more analysis.[57] In 1998, Millett LJ said in *Armitage v Nurse:* 'Every beneficiary is entitled to see the trust accounts, whether his interest is in possession or not.'[58] The suggestion in *Schmidt*, which made no reference to *Armitage*, would qualify that statement severely. Indeed, *Schmidt* effectively contradicts it, unless the later case intended to suggest only that some kinds of information might be properly withheld from beneficiaries. As a matter of English law, *Schmidt*, being an Isle of Man decision, is not capable of overruling *Armitage*.[59] *Schmidt* is binding only in the Isle of Man.

Moreover, even in jurisdictions where neither decision is binding, the suggestion in *Schmidt* regarding beneficiaries is questionable. Let us assume that we have a trust in which the default beneficiary is a named charity. Because it is only a default beneficiary, or in the words of *Lewin on Trusts*, a 'long stop' beneficiary,[60] the suggestion is that it does not hold this fundamental right to be told about the trust and to see the accounts.

But we need to remember that in the structure we are concerned with, this beneficiary may be the only beneficiary of the trust in the strict sense. If it is, then the trust depends for its validity on the presence of this beneficiary, since every trust that is not exclusively charitable must have a beneficiary. Objects of powers cannot satisfy the beneficiary principle, and turn what is not a trust into a trust.[61] So can we really say, of the only beneficiary, who is making the whole structure stand up, that it is not really a beneficiary because its interest is defeasible? A defeasible interest is nothing unusual: it is found in almost every trust, because almost every trust has some dispositive discretions.

54. These are the trusts against which *The Economist* spoke when it said ('Mistrust the Trusts', 9 November 2013): 'A structure that was set up to protect the wives of medieval crusaders has ended up being used by the sort of business people who greet the Russian leader as ''Vladimir''.' For an object example, see *Pugachev* (n 1), where the description might have been applicable to both sides; it appears that no objection was taken, at least in this phase of the proceedings, to the ability of the successful plaintiff to have access to the British court system. *The Economist* called for the public registration of trusts and their beneficiaries (both actual and potential).

55. *Underhill and Hayton* (n 4) [56.24].

56. See n 16 [54].

57. L Ho, 'Trustees' Duties to Provide Information' in E Bant and M Harding (eds), *Exploring Private Law* (CUP 2010) 343.

58. *Armitage* (n 18) 261.

59. *Willers v Joyce* [2016] UKSC 44 [12]: '. . . given that the JCPC is not a UK court at all, decisions of the JCPC cannot be binding on any judge of England and Wales, and, in particular, cannot override any decision of a court of England and Wales . . . which would otherwise represent a precedent which was binding on that judge'. This was a unanimous decision of a nine-judge panel.

60. J Mowbray and others, *Lewin on Trusts* (18th edn, Sweet & Maxwell 2008) [23–74].

61. And this, whether or not the trust deed calls them 'beneficiaries': see n 34.

Can we really say, of the only beneficiary, who is making the whole structure stand up, that it is not really a beneficiary because its interest is defeasible?

The interest of the default beneficiary is defeasible, but if that beneficiary is named or identified and exists, this interest is almost certainly vested, not contingent. Here I disagree with Sir Anthony Mason, who has said: 'A person entitled in default of distribution in a discretionary trust has no more than a contingent remainder, if that.'[62] If there is a discretionary trust in the narrow sense,[63] then the property must be distributed and no one is entitled in default. Sir Anthony is here discussing discretionary trusts in the wider sense, since he also says that the '[t]he members of the class eligible to be appointed are objects of the power, not beneficiaries in the strict sense.'[64] But *someone* must be a beneficiary in the strict sense, throughout the life of the trust, and in a massively discretionary trust, this someone is the default or residuary beneficiary.[65] Whether an interest is vested or contingent is determined by the structure of the trust and the interests it creates, not by the practical likelihood that its holder will receive property. The interest of the default beneficiary is defeasible because of the dispositive discretions, but this does not make it contingent, at least if we are to adopt the conceptual framework that was developed in land law and that has always been applied to trusts in relation to perpetuities. A contingent interest is one that does not vest until the satisfaction of a condition precedent; a contingent interest is always a future interest.[66] Whether an interest is vested or contingent is a question of construction, but the presumption is in favour of vesting.[67] The need for the passage of time, or of a life, certainly does not make a remainder interest contingent; it goes to whether it is vested in possession or only vested in interest. The fact that a present interest may be defeated by the later occurrence of an uncertain event does not make it contingent, but rather defeasible. This is borne out, for example, by *Pearson v IRC*,[68] which was decided at an early stage of the evolution of the modern discretionary trust. A majority held that the interests of the default beneficiaries, which interests were subject to overriding discretionary powers held by the trustees, were not 'in possession'; but they were vested, not contingent, despite those wide powers. Lord Keith of Kinkel said of the beneficiaries:

> Each of them having attained 21 years of age had a vested interest in the fee [*sic*; fund?] of one third subject to the possibility of divestiture through the exercise of the trustees' overriding power of appointment and also, during the lifetime of the settlor, to the possibility of defeasance pro tanto through the birth to him of any further child who attained the age of 21.[69]

To repeat: the beneficiary principle requires that there be a beneficiary from the moment of the trust's constitution.[70] Thus, the interest of a named default beneficiary, even if defeasible by the exercise of a power, must be vested, not contingent.[71] The interest of a default beneficiary can be contingent only if there

62. Sir Anthony Mason, 'Discretionary Trusts and their Infirmities' (2014) 20 *Trusts & Trustees* 1039, 1045.
63. See above, section 'Terminology', subsection 'Discretionary trust'.
64. Mason (n 62) 1045.
65. *Kennon* (n 9) [170]–[172] (Heydon J).
66. eg EH Burn and J Cartwright, *Cheshire and Burn's Modern Law of Real Property* (18th edn, OUP 2011) 527.
67. *Re Mallinson Consolidated Trusts* [1974] 1 WLR 1120, [1974] 2 All ER 530 (ChD).
68. [1981] AC 753.
69. ibid 780.
70. One reviewer noted that a person could create a trust for the children of X, even if X has no children at the moment of constitution. This is true, but it will (in the absence of other provisions) create a resulting trust at the moment of constitution, with the interest of the resulting beneficiary probably defeasible by the condition subsequent of the birth of a child of X.
71. If there are *unnamed* potential future beneficiaries, they do not have vested interests (see n 34 for examples). But such persons could not, on their own, satisfy the beneficiary principle; if there were *only* potential future beneficiaries, there would be an immediate resulting trust (see the previous note).

I therefore disagree with the characterization of the interests of named default beneficiaries as 'contingent' in *Chief Commissioner of Stamp Duties* (n 1) [21]. As in *Pearson* (n 68), they were vested but defeasible. If this were not the case, the trust property would have been held on charitable trusts ([20]). The High Court characterized them as vested subject to defeasance only after the trust deed was amended to remove the possibility of defeasance by decease before the end of the trust ([25]); but both before and after that amendment, the interests were vested but defeasible by the exercise of dispositive discretions.

is a prior vested interest that satisfies the beneficiary principle.[72]

The interest of a named default beneficiary, even if defeasible by the exercise of a power, must be vested, not contingent

Are the labels 'residuary beneficiary', 'default beneficiary', and 'long stop beneficiary' anything other than 'beneficiary' with a vituperative epithet?[73] The logic of the trust device is that it exists to benefit beneficiaries, with the result that beneficiaries have certain rights that flow from the accountability of trustees. It is fine to add objects of powers, but they cannot enforce the trust; they have no right to any property.[74] The trustees do not owe *obligations* to those objects regarding the benefit of the property.[75] But why would anyone think that we can take rights away from the so-called real beneficiaries, making them only objects of powers, and not end up with those rights being held by the default beneficiary? The default beneficiary must be a real beneficiary. The only alternative is that there is no trust (in either the wide or the narrow sense). As Millett LJ also said in *Armitage:* 'If the beneficiaries have no rights enforceable against the trustees there are no trusts.'[76] He was not talking about the objects of powers.

I am not sure that this aspect of *Schmidt* can be taken as the last word on the subject. This, then, could constitute another risk of massively discretionary trusts. If the default beneficiary is left as a purpose, then the invalidity risk that I described in the previous section arises. If this is avoided by naming a particular person, such as a corporate charity, or some of the same persons who are named as objects of the powers, then I would expect those persons to be treated by the courts as beneficiaries, since it is they who stand between validity and invalidity. This implies that they have a right to be told about their interests from the moment the trust arises, and to be provided with the trust deed, accounts and other information.[77]

Saunders v Vautier

Why would a named charity want to fight for information about a trust from which it cannot realistically expect to benefit? I can think of at least one reason, namely the rule in *Saunders v Vautier*.[78] This allows a trust to be terminated, contrary to its terms, and the property to be distributed among its objects as they agree.[79] It is perfectly possible for a charitable entity to agree with other beneficiaries to bring a trust to an end in this way. It happened in 2002 in *Re Barton*,[80] the first English case decided under the Hague Trusts Convention. The will trust was ended against the vociferous objections of the testator's widow, who was one of the trustees. The property was divided between the testator's son and a corporate charity, even

72. cf n 37.

73. With acknowledgement to Millett LJ in *Armitage* (n 18) 254: '. . .Willes J. famously observed that gross negligence is ordinary negligence with a vituperative epithet'.

74. See the section 'Terminology', subsection 'Beneficiaries'.

75. They may owe them some limited obligations (see text at nn 14–15) but not the core obligation that makes a trust of property: the obligation to ensure that the benefit of that property accrues to another.

76. See n 18, 253.

77. In this sense, I fail to understand the approach of the Jersey judge who thought it was unnecessary to give notice to the Attorney-General of litigation involving a trust with three named charities as beneficiaries, on the ground that 'in practice' they would not receive anything: *Re GEA Settlement* (1992), reported at (1999) 13 Tolley's Trust Law International 188, 189 and quoted in Matthews, 'In the Land of the Blind' (n 53). This seems to be assisting a settlor to misuse the law of trusts.

78. See n 47. For a careful analysis, see RB Cantlie, 'A Case of Mistaken Identity: The Rule in *Saunders v Vautier* and Section 61 of the Trustee Act of Manitoba' (1986) 15 Man LJ 135.

79. The rule does not apply in most states of the USA, nor in Alberta or Manitoba (subject to the analysis of Cantlie, ibid). It is not by accident that this rule features as prominently in this article as the beneficiary principle and the related principle that the common law does not allow non-charitable purpose trusts. One could argue that the rule in *Saunders* is only a consequence of the rule against non- charitable purpose trusts. Trusts for persons exist for the benefit of those persons, and once those persons, the beneficiaries, are fully capacitated they are not bound by what the settlor (who, by assumption, is not a beneficiary and so has no interest in the trust property) thinks is best for them. See J Langbein, 'Mandatory Rules in the Law of Trusts' (2004) 98 Northwestern U L Rev 1105; J Langbein, 'Burn the Rembrandt? Trust Law's Limits on the Settlor's Power to Direct Investments' (2010) 90 BU L Rev 375. The rejection of the rule in *Saunders* allows, in a sense, the creation of a non-charitable purpose trust, rather like a trust to burn the Rembrandt. See P Matthews, 'The Comparative Importance of the Rule in *Saunders v Vautier*' (2006) 122 LQR 266.

80. See n39.

though this was clearly contrary to the intentions of the testator.

The rule in *Saunders v Vautier* can operate by agreement among all the beneficiaries of a trust, and requires that they all be of full legal capacity. In relation to the risks related to using massively discretionary trusts, I would argue that there is uncertainty about what this principle requires when the trust structure includes dispositive discretions. In fact, I would argue that there are two levels of uncertainty. The first level is whether the rule takes account of the interests of objects of powers at all; if it does, the second level is whether it draws any distinction between different kinds of objects. I will look at each in turn.

There is uncertainty about what this principle requires when the trust structure includes dispositive discretions

First, take the simple case in which property is held in trust for A, but the trustees hold a dispositive power in favour of B. A is the only beneficiary, and is of full legal capacity. On one view, A could invoke the rule in *Saunders v Vautier* and demand all of the property, because A is the only beneficiary. B's interest is not relevant on this approach, because B has only a hope that the power will be exercised in his favour; he has no right to any of the property. In *Underhill and Hayton*, this is presented as one possible view of the law, with an *obiter dictum* from Lord Upjohn in support.[81] Now the danger of the massively discretionary trust with one or more named default beneficiaries is clear: on this view of *Saunders v Vautier*, those beneficiaries would be entitled to demand all of the property at any time, defeating the hopes of the objects of the discretionary powers.

Lewin on Trusts states that such a result would be 'wholly contrary to the settlor's intentions'.[82] It is crystal clear, however, that such a consideration is irrelevant to the operation of the rule. One way of stating the beneficiary principle, going back to the well-known words of Sir William Grant MR in *Morice v Bishop of Durham*, is as follows: 'There must be somebody, in whose favour the court can decree performance.'[83] That somebody, in a massively discretionary trust structure, is the default beneficiary, and not any mere object of a power, because the court cannot decree performance in favour of the object of a power. The object of a power does not have any right to any of the trust property.[84] And it is arguable that that somebody, the one in whose favour the court will decree performance, is the one who can invoke the rule in *Saunders v Vautier*.

An alternative view of the rule in *Saunders v Vautier* is also presented in *Underhill and Hayton*.[85] This view is more arithmetical. It sees the rule as involving not merely beneficiaries in the strict sense, but as requiring agreement among all of those who might possibly benefit. We can return to the earlier example of property held in trust for A, with the trustees holding a dispositive power in favour of B. On this second view, because B might get some, or perhaps all of the property, only by agreement between A and B could the trust be ended. In *Schmidt*, Lord Walker said in *obiter dicta* that the object of a power has the ability to 'block' the operation of the rule in *Saunders v Vautier*.[86]

There is some logic to that, of course. But there is also some logic to the first position, and there is clearly uncertainty as to what the law is. And I come now to the second uncertainty in the law. Let us assume that it is correct that objects of a power may be able to block the operation of the rule in *Saunders v Vautier*. Does this mean any object of any power? Take the same structure, with property held in trust for A and a dispositive power in favour of B. Now assume that we add another power, one which allows the trustees to add anyone in the world to the class of objects of the dispositive power; such a

81. See n4 [66.12].
82. See n 60 [24–13].
83. *Morice v Bishop of Durham* (1804) 9 Ves Jun 399, 32 ER 656 (MR), 405, 658, aff'd (n 36).
84. See section 'Terminology', subsection 'Beneficiaries'.
85. See n4 [66.13].
86. See n 20 [41].

power is common in massively discretionary trusts. If we take a wide view of Lord Walker's dictum, then this structure could never be subjected to the operation of the rule in *Saunders v Vautier*. But as we have already seen, in relation to access to information, Lord Walker seemed willing to distinguish between beneficiaries or objects who have only a remote possibility of actually benefitting, and those who do not. I have expressed some doubt about that, but if this is right, does it mean we should also distinguish between objects of powers for the purposes of the rule in *Saunders v Vautier?* If so, we might find that there is only a relatively small number of objects who have a realistic prospect of benefitting from the trust. If those few are fully capacitated, then it may be that in agreement with the residuary beneficiary, they can collapse the trust whenever they wish. The result would be something like what happened in *Re Barton:* the settlor's family members could, in combination with the residuary beneficiary, bring the trust to an immediate end.

We have seen that there is a kind of massively discretionary trust in which the residuary beneficiaries are not charities, but rather are members of the settlor's family.[87] In this variation, it is possible to exclude the risk of trust termination via the rule in *Saunders v Vautier*, by ensuring that some of the potential default beneficiaries are unidentifiable during the life of the trust.[88] Even here, however, a variation of the trust, which may bring it to an end, is not out of the question.[89]

Misleading appearances

In this section, I begin by returning to the idea that even though the default beneficiary is the only beneficiary, it may not be considered to be a 'real' beneficiary in relation to standing to seek information.[90] As we saw earlier, the idea is that in such a case, of a 'long stop' beneficiary, everyone knows that the trust property will be distributed to the objects of the dispositive discretions.

It is worth stopping for a moment to ask: how do we know that? Typically, we do not know that by reading the trust deed. The trust deed may indeed be drafted to conceal that;[91] at the very least, it does not typically announce it. If the goal is to ensure that those who are to benefit are not to have the rights of beneficiaries, then the trust deed must make it clear that they are merely objects of powers, with no right to any property. And as we have seen, this leaves the default beneficiary as the only beneficiary propping up the whole structure.

Imagine that the trustees chose not to exercise any of their discretionary dispositive powers, which on the face of things is up to them, since they hold the discretions in question and do not have to exercise them.[92] The result would be that all the property would go to the default beneficiary, say a named charity. The assumption, in the books and cases that treat this beneficiary as having no substantial interest, seems to be that something will have gone badly wrong. But on the face of it, the trustees have complied with their obligation to their only beneficiary, and have simply chosen not to use powers which, in their nature, are not obligations but only powers.

Imagine that the trustees chose not to exercise any of their discretionary dispositive powers, which on the face of things is up to them

87. See text at n 29.

88. See, for example, the trust deed in *Clayton* (n 1). The default or 'final' beneficiaries were the children of the settlor, but that included future children (cl 2.1 'final beneficiaries); moreover, in the case that a child should die before the trust came to an end, the issue of that child would become beneficiaries (cl 10.1 (b)); and if all children and their issue failed, the beneficiaries would be the next of kin of the settlor (cl 10.1 (c)). The effect of this is that there was an unknowable class of possible future beneficiaries. Again, however, if *Schmidt* were taken to its logical conclusion, would beneficiaries be ignored for the purpose of *Saunders* when it is highly unlikely that they will benefit? In my view they should not be, and this again casts doubt on the reasoning in the case.

89. Most jurisdictions have legislation allowing the court to vary or revoke a trust where this is for the benefit of those who are not able to consent for themselves. It may be possible (for example, through the purchase of irrevocable insurance) to create an arrangement that terminates the trust in a way that ensures a benefit for any future beneficiaries who may come into existence: *Waters' Law of Trusts in Canada* (n 30) 1389–97. The trend of the case law is that the settlor's intention is irrelevant on such an application, which is consistent with *Saunders*: ibid 1402–03; *Goulding v James* [1997] 2 All ER 239 (CA).

90. See section 'Rights to information'.

91. See the text at n 52.

92. *Re Manisty's Settlement* (n 14) 25: 'The court cannot insist on any particular consideration being given by the trustees to the exercise of the power.'

Let us return to first principles. How do trustees *ever* know what they are supposed to do? Sometimes, they have clear obligations: for example, to pay the income to a particular person. In our context, although they must have some obligations (as a result of the beneficiary principle), they also have wide and overriding discretionary powers, which are not obligations. How do they know, or how do they decide, what they are to do with these powers?

Trustees, of course, are bound by obligations of loyalty that they owe to the beneficiaries.[93] This means that in general, they must be guided by what they consider to be the best interests of the beneficiaries. In the case of dispositive discretions held in a fiduciary capacity, this formulation does not help the trustees very much, because the exercise of the discretion will typically *harm* the interests of the beneficiary by defeating its interest and directing the property elsewhere. That is, if the dispositive discretion had to be exercised in what the trustee considered the best interests of the *beneficiary*, then it would be a rare case in which the discretion would be exercised at all. But the trustees certainly cannot be bound to use their dispositive discretions in what they think are the best interests of the objects of those discretions, disregarding the interests of the beneficiaries. That would have the opposite effect: it would be a rare case in which they could *not* exercise their discretions. Indeed, such a norm would be inconsistent with the idea that these are only *discretions*, not duties, and it would turn the objects into beneficiaries.

And so the courts have adopted a different test for fiduciary discretions: they are required to be exercised in what the holder considers to be the best manner of fulfilling the *purpose* for which the power was granted.[94]

In traditional drafting, a discretionary power might itself signal the purpose for which it was created. For example, a power to use capital for the education of an object gives some indication of the purpose, and guides the holder of the power. The holder of the power can reason in terms of what would best accomplish the goal of educating the child, in the light of their needs, the property available, other resources, and so on.

In the massively discretionary school of modern trust drafting, however, wider discretions are better, as they give more flexibility and they do not restrict trustees to predefined purposes. They do not restrict them, but they do not guide them much either. If the trustees have power to dispose all of the income and all of the capital to a class of objects, for any reason at all, and indeed a power to add objects to that class so that in principle it includes just about everyone in the world, then they seem to have the power to give all of the trust property to whomever they wish, but rather little guidance as to the purpose for which this power was granted.[95]

It is not surprising that the rise of massively wide discretions has led to the rise of letters of wishes, memoranda of wishes, and other expressions of settlors' desires. Not very long ago, these were relatively peripheral phenomena, at least in the onshore world. But due to the rise of massively discretionary trusts, the discussion of these documents in legal textbooks is now substantial. The reason should by now be obvious. How else would the trustees know that the charity named as default beneficiary is not actually supposed to get anything? These expressions of

93. We have noted that it is not at all clear that the fiduciary obligations of a trustee are owed to objects of discretionary powers (text after n 15). If a trustee of a Red Cross trust were to acquire an unauthorized profit through the use of his office, would anyone but the charity have standing to sue for it? As noted earlier (n 30), such trusts typically feature a protector with the power to remove and appoint trustees; can this person be given the rights of a beneficiary to enforce the administration of the trust? As with granting enforcement rights to the objects of powers, enforcement by a protector would be directly inconsistent with the beneficiary principle and the concomitant rule against non-charitable purpose trusts.

94. *Vatcher v Paull* [1915] AC 372 (PC) 378; *Klug v Klug* [1918] 2 Ch 67, 71; *McPhail v Doulton* [1971] AC 424 (HL) 449, 457; *Re Hay's Settlement Trusts* [1982] 1 WLR 202 (ChD) 209; *Turner v Turner* [1984] Ch 100 (ChD) 109–110; *Re Beatty* [1990] 1 WLR 1503 (ChD) 1506; *Hayim v Citibank N.A.* [1987] AC 730 (PC) 746; see also *Eclairs Group Ltd v JKX Oil & Gas plc* [2015] UKSC 71, [15].

95. Typically, the trustees cannot use the powers to benefit themselves. Even this restriction, however, is not always in place; see again the trust deed in *Clayton* (n 1), cl 14.1, and note also cl 11.1 which authorized the trustee to treat the beneficiaries and objects of powers (of which he was one) unequally.

wishes are the means by which the trustees will know what the settlor really wanted but did not say in the trust instrument. The less the instrument says, the more important the wishes become.

It is not surprising that the rise of massively wide discretions has led to the rise of letters of wishes, memoranda of wishes, and other expressions of settlors' desires

And yet, these wishes are typically not terms of the trust.[96] The standard doctrine is that while the settlors' wishes are a relevant factor, the trustees must make their own decisions. But how are they to make them? Their decisions have to be based on something; their own personal preferences and desires are not relevant. If the express terms of their discretions give them no guidance at all, it may well be the case that the wishes of the settlor take on a predominant significance. The trustees have nothing else to go on; nothing else is legally relevant.

Paradoxically, the settlor's wishes, which are not binding and are not terms of the trust, are controlling. They tell the trustees how to act. Some might say that a trust which is effectively governed by the settlor's wishes—wishes that are not actually terms of the trust—is in danger of being a sham.[97] A finding of sham is certainly likely if the trustees, who on the face of the deed hold overriding discretions of the widest kind, are actually simply doing what the settlor tells them.[98] The courts will not ignore the fact that the settlor is in control.[99] Quite apart from a finding of sham, this control might mean that the settlor is a de facto trustee.[100] In turn, this could mean that the settlor is in a fiduciary relationship with the beneficiaries and accountable to them.[101] Settlor control could also have significant taxation implications.[102]

Paradoxically, the settlor's wishes, which are not binding and are not terms of the trust, are controlling

To avoid such findings, it is said that the trustees must make their own decisions, and not simply follow the settlor's directions. But in this context, this looks almost like sophistry. They are not to follow the settlor's directions, but the only thing they have to go on is the settlor's wishes. The problem is only worse when we find that this seems to mean the settlor's wishes as they evolve from time to time (at least if the settlor is still alive).[103] But if the wishes are not legally binding, why should they not change? Can the settlor write a new letter every day?[104] One case on beneficiaries' rights to information discussed the oral expression of the settlor's wishes, treating this as unobjectionable.[105] Presumably such wishes can be countermanded as easily as they can be communicated, for example by a quick telephone call.

96. It is possible that a letter of wishes is legally binding: *Underhill and Hayton* (n 4) [56.51] ('an exceptional case'). The reason it is unusual is that such a letter is on an equal footing with the trust instrument, so there is no obvious reason to put it in a separate document. It would not be possible to amend it, except to the extent that the trust permitted this. Moreover, it would have to be disclosed to anyone who had the right to see the trust instrument. Disclosure of non-binding letters of wishes is discussed in the next section.

97. This was precisely the holding in *Pugachev* (n 1) [424], [434], [437], as an alternative to the holding that the defendant's non-fiduciary powers as a protector made him the beneficial owner of all the trust assets (see n 31).

98. *Pugachev*, ibid and *Underhill and Hayton* (n 4) [4.6], discussing the case in which the trustee simply holds the trust property 'to the order' of the settlor.

99. The problem may be even more profound where the settlor is also the sole trustee, as in *Clayton* (n 1). The Court ([118]–[127]) left unresolved the issue whether the settlor had even successfully created a trust at all, since he could do whatever he wished with the property, including giving all of it to himself.

100. *Dubai Aluminium Co v Salaam* [2002] UKHL 48, [2003] 2 AC 366 [138]. A finding of sham requires a shared understanding between the settlor and the trustees *Shalson v Russo* [2004] EWHC 1637, [2005] Ch 281 [190]; Mowbray (n 60) [4-22]; but note the holding in *Pugachev* (n 1) [434], that this may be satisfied if the trustee 'had no intention independent of' the settlor); a finding of de facto trusteeship does not. Moreover, such a finding may well mean that the *de jure* trustees are in breach of trust.

101. *Dubai Aluminium Co,* ibid.

102. In *Fundy Settlement v Canada* [2012] 1 SCR 520, 2012 SCC 14, practical decision-making was in the hands of the beneficiaries, who were resident in Canada, not the trustees, who were resident in Barbados. It was held that the trusts were resident in Canada. Trusts do not have any residence at common law but when taxation is based on residence it may be necessary to assign a residence to a trust, and the Supreme Court of Canada held that this is done on the basis of where control lies.

103. The assumption in Kessler (n 33) [7.16] is that non-binding expressions of wishes can be changed at any time.

104. In *Minwalla v Minwalla* [2004] EWHC 2823 (Fam), [2005] 1 FLR 803 [48], two contemporaneous but inconsistent letters of wishes were produced. When the plaintiff wife succeeded and sought to enforce her English judgment in Jersey against the trustees there, a third letter of wishes emerged: *CI Law Trustees v Minwalla* [2005] JRC 099 [25].

105. *Breakspear v Ackland* [2008] EWHC 220, [2009] Ch 32, which is discussed below.

Presumably such wishes can be countermanded as easily as they can be communicated, for example by a quick telephone call

Even if we can convince ourselves that it is possible to imagine the trustees acting independently, when the only legally relevant constraint on them is the settlor's wishes, we must still ask what kind of trust this is. In *Antle v Canada*, Noël JA said that for a finding of sham, '[i]t suffices that parties to a transaction present it as being different from what they know it to be.'[106] Thus, there can be a sham even if the trustees act independently. This means that it is certainly arguable that a 'Red Cross' trust is a sham from the moment of its creation, inasmuch as the settlor's wishes tell the trustees that the only beneficiary named in the trust deed is not actually supposed to benefit. It is understood between the settlor and the trustees that the intended outcome is not accurately reflected in the trust deed. If the named charity is not intended to benefit, so that the default clause is a sham and ignored, then there will be a resulting trust.[107]

Moreover, a version of the same problem arises even in the 'family' version of the massively discretionary trust, in which the default beneficiaries are family members. If there were to be a conflict between the settlor's expressed wishes and the trustees' assessment of the best interests of those default beneficiaries, which consideration was intended by the settlor to prevail? To ask the question is to answer it. Even if we assume independence in trustee decision-making, this seems to be a situation in which the trustees are intended to hold the property *in order to implement the settlor's wishes*, rather than for the benefit of the named beneficiaries. On that view, one could argue that the genuine intention of the settlor was to create a non-charitable purpose trust, which is not allowed by the common law of trusts.[108] If the trust was actually a trust for the beneficiaries, and the trustees were acting independently, then the trustees' assessment of the best interests of the beneficiaries would necessarily prevail over the mere expression of a wish by the settlor.

If there were to be a conflict between the settlor's expressed wishes and the trustees' assessment of the best interests of those default beneficiaries, which consideration was intended by the settlor to prevail? To ask the question is to answer it

And if the settlor's genuine intention was to create a non-charitable purpose trust, and the trustees knew that and went along with it, then the trust deed is misleading in naming the default beneficiaries as the beneficiaries.[109] This yields, again, a resulting trust for the settlor.

Accountability

I pass to a final risk that may be associated with massively discretionary trusts. This is the risk of litigation, which may well be increased by the presence of wider discretions. *Schmidt v Rosewood Trust Ltd*[110] heralds a move towards understanding trustees' obligations to provide information as based on their accountability, which is a core feature of the trust. Modern trust

106. (2010) FCA 280 [20]. Similar is *Clayton* (n 1) [113]: a sham is '. . . a document that does not evidence the true common intention of the parties'. See also *Pugachev* (n 1) [441]–[442] for a suggestion of a wider notion of sham as a document that is drafted to mislead others.

107. This is the suggestion in Matthews, 'The Black Hole Trust' (n 53). This could leave the dispositive discretions in place, but it makes the settlor the only beneficiary of the trust. See also Mowbray (n 60) [4-23] on the effect of a finding a sham.

108. See n 8. It is possible to create non-charitable purpose trusts in some jurisdictions, but even there it is a separate question whether the purpose of 'doing what the settlor wishes from time to time' would be a legally permissible one. In Quebec, for example, it is certainly possible to create non-charitable purpose trusts, and it is arguable that all trusts, even if they have beneficiaries, are purpose trusts (see Civil Code of Québec, arts 1260, 1266–73). But a trust for the purpose of complying with the settlor's wishes would be invalid, as the purpose would be considered inconsistent with the intention to create a trust (*Bank of Nova Scotia v Thibault* 2004 SCC 29, [2004] 1 SCR 758 [41]; cf n 99).

109. On the requirement that the trustees be implicated in the sham, see n 100. No other conclusion seems possible if the trustees take the view that the settlor's expressed wishes are controlling, rather than the trust instrument. In this regard, note the holding in *Pugachev* (n 1) [434], supporting the alternative finding of sham, that the trustee 'had no intention independent of' the settlor.

110. See n 20.

structures with enormously wide discretions mean that none of the objects of powers has any right to any of the trust property; they only have a hope that a discretion will be exercised in their favour. The residuary beneficiary, of course, has a right to trust property; that is necessary for the structure to work; but it is defeasible by the exercise of those wide discretions. In other words, the trustees' decisions are the only things that matter.

When everything rides on trustees' decisions, rather than on the terms of a document, those who are aggrieved may well choose to litigate. At the very least, they will wish to understand the reasoning behind the decisions that were made. My suggestion is that the accountability of trustees points inevitably in the direction that trustees will have to provide reasons for their decisions. I am aware of the principle articulated in *Re Londonderry's Settlement*,[111] that trustees cannot be forced to disclose their reasons for the exercise of their discretions; and its affirmation in *Breakspear v Ackland*,[112] leading to the conclusion that a letter of wishes need not generally be disclosed. I am not convinced that this is the last word on the matter.

Leaving aside some *non sequiturs* in the reasoning in both cases,[113] the primary reason for allowing secrecy was expressed this way in *Breakspear*:

> It is in the interests of the beneficiaries because it enables the trustees to make discreet but thorough inquiries as to their competing claims for consideration for benefit without fear or risk that those inquiries will come to the beneficiaries' knowledge. They may include, for example, inquiries as to the existence of some life-threatening illness of which it is appropriate that the beneficiary in question be kept ignorant. Such confidentiality serves the due administration of family trusts both because it tends to reduce the scope for litigation about the rationality of the exercise by trustees of their discretions, and because it is likely to encourage suitable trustees to accept office, undeterred by a perception that their discretionary deliberations will be subjected to scrutiny by disappointed or hostile beneficiaries, and to potentially expensive litigation in the courts.[114]

It is difficult to know what to make of this. The final sentence is much more about protecting trustees than beneficiaries; and it is not mainly about protecting them from harm (since they are entitled to be indemnified when they litigate in good faith), but from having to explain themselves. What is wrong with subjecting them to scrutiny as to the 'rationality' of their decisions?[115]

The first sentence claims that this protection of trustees is for the benefit of the beneficiaries, but no reason is given other than, again, the benefit of the trustees. The only reason is in the middle sentence, which seems contrived and difficult to understand.[116] As to the reference to reducing litigation,

111. [1965] Ch 918 (CA).

112. See n 105. In this case, the court ordered the disclosure of a letter of wishes and records of orally expressed wishes of the settlor, but affirmed that in general, such disclosure would not be ordered.

113. In *Breakspear*, Briggs J adopted part of the reasoning of Danckwerts LJ in *Re Londonderry* (n 111, 936) to the effect that trustees have a confidential role to play and so their reasons should remain confidential. This is a conflation of two senses of the word. The primary sense of 'confidential' and 'confidence' is not about secrecy, but about trust; see M Lupoi, '"Trust and Confidence"' (2009) 125 LQR 253, 255–61. 'Con' in this setting means 'thoroughly' and 'fides' means, roughly, 'trust'. All trustees, and all fiduciaries, are in a relationship of confidence in this sense—with their beneficiaries, not with the settlor. The sense of 'confidential' as meaning 'private' or 'secret' is different, secondary, derivative, and later.

114. *Breakspear* (n 105) [54]. The judgment as a whole is focused on 'family' trusts (see [6]–[8]). *Underhill and Hayton* (n 4) [56.58] say that it is 'by no means certain how far these principles apply to other kinds of trusts'. To the extent that the reasoning is based partly on the aim of preserving 'family harmony', this may make sense; but leaving aside the trustees' personal wishes in the matter, it is not clear whether family harmony is better served by secrecy than openness. Furthermore, there have not traditionally been different rules of trust law for 'family trusts', apart perhaps from the now-outdated rules on 'marriage consideration'.

115. See the cases in n 94, which presuppose that such scrutiny is normal.

116. The example of the life-threatening illness is not obviously relevant to the disclosure of a letter of wishes (as opposed to a particular decision trustees might be considering). And how often are trustee decisions based on life-threatening illnesses, as opposed to assessments of needs, maturity, desert, resources, and (again—the real issue, especially when a letter of wishes is in issue) the wishes of the settlor? Surely Briggs J did not mean to imply that it might be in the interests of a beneficiary to be kept ignorant of *his or her own* life-threatening illness? We could imagine that trustees become aware of the illness of one beneficiary or (more likely) object of a power, generating financial need, and could not tell this private information to others. But I am not arguing for a position that would require trustees to disclose everything, including information which is private or secret (confidential, in the sense of 'confidential information': n 113). I am arguing *against* a position that says that trustees need not give any reasons at all when they give away property that does not beneficially belong to them, nor disclose the letter of wishes that is probably the most crucial document in the whole trust structure.

this is not at all clear. If beneficiaries are dissatisfied, they can always litigate, seeking disclosure or alleging improper decision-making.[117] Conversely, when beneficiaries understand the reasons for trustees' decision-making, then if those reasons were rationally defensible, this if anything would seem to reduce the likelihood of litigation; even if the beneficiaries do not agree with the decision, it is clear enough that the decision does not belong to them.

Trustees may find their role a difficult one, and disclosure of their reasons may make it more difficult still. But it seems to me that accountability cannot stand comfortably with secrecy. This is especially so in the context of massively discretionary trusts, where, as we have seen, a letter of wishes may at one and the same time be not legally binding, and yet the most important document in determining who will benefit from the trust.[118] It is at least strange to think that beneficiaries have the right to see the trust deed,[119] but not the letter of wishes without which the deed is unhelpful and probably actively misleading.[120]

Accountability cannot stand comfortably with secrecy

Trustees with massively wide discretions can exercise them well or badly. One of the ways in which they can exercise them badly is by exercising them for the wrong reasons.[121] And the wider are the discretions, the more likely it is that this is just about the *only* way in which they can exercise them badly, since the *terms* of their powers are not constraining at all. Are trustees really accountable if they are not required to provide reasons? They are administering property that does not belong to them beneficially. And every time they exercise their discretionary powers in favour of one object, they are taking away from someone else. They are diminishing the *rights* of the taker in default, since whenever property is subject to a power, there is a taker in default who will otherwise get it. The object of the power has a hope; the taker in default has a defeasible right. Thus, trustees who exercise a power are making that person less well off than they were before. It is hardly a lot to ask that some reasons should be provided.[122]

The principle as stated in *Breakspear* may therefore be one that is still evolving. Whatever virtues they may have, massively discretionary trust structures seem more likely to invite litigation than fixed trusts, because the trustees' decisions control the destination of the trust fund far more than any of the provisions in the trust instrument. Those who are disappointed will want to know why, and trustees who are making independent decisions for defensible reasons should not be afraid to disclose them.

Conclusion

History teaches that Henry I died from consuming a 'surfeit of eels'. This can be taken as a particular example of a more general principle, that just because

117. An iron rule against disclosure would make it futile to seek disclosure without a claim based on improper conduct; but recall that in *Breakspear* itself, disclosure was ordered. See also *Underhill and Hayton* (n 4) [56.62] on beneficiaries' application to the court for disclosure. *Schmidt* (n 16) suggested that disclosure is always under the control of the court and so discretionary.

118. In the section 'Misleading appearances'.

119. *Underhill and Hayton* (n 4) [50.2]; this is subject to *Schmidt* (n 16), but my reservations on that have already been expressed in the Section 'Rights to information'.

120. The settlor may have communicated the letter to the trustees intending that it remain secret (confidential, in the sense of 'confidential information': n 113). But the settlor is not at liberty, even in the trust deed, to override the accountability of trustees to the beneficiaries: *Underhill and Hayton* (n 4) [56.22]. Where the trust deed is meaningless without the letter of wishes, it is not obvious why the settlor should be able to restrict access to the letter.

121. See n 94.

122. As noted by Briggs J [30], in *Hartigan Nominees Pty Ltd v Rydge* (1992) 29 NSWLR 405 (CA), Kirby JA, dissenting, would have ordered disclosure of a letter of wishes, partly on the basis that 'Australian society accepts a generally greater level of accountability than has, until now, been accepted by the law of England.'

something is good, it does not follow that more of it is better.

Just because something is good, it does not follow that more of it is better

I am not opposed to discretion in trust structures. However, massively wide discretions do potentially create a series of legal risks. Let me summarize some of them. First, one version of such a structure aims to avoid having any beneficiary at all, through the use of a default clause that directs the trustees to apply the property to charitable purposes. I have argued that such a clause is invalid, as it purports to create a trust for charitable purposes but which is not exclusively charitable. Other types name one or more persons as default beneficiaries, who may or may not be charitable trustees or entities. This avoids the invalidity problem but it creates other risks. I have argued that the default beneficiary may well have rights to information about the trust, and that suggestions to the contrary are difficult to justify. The beneficiary is necessary for the existence of the trust, and denying information to that beneficiary on the basis that it is somehow not a *real* beneficiary seems, at the least, rather inconsistent.

The rule in *Saunders v Vautier* presents another risk, exacerbated by some uncertainty. If only beneficiaries are entitled to invoke the rule, then the default beneficiary, who may not be intended to benefit at all, could demand all of the property at the moment the trust is constituted. Even if objects of discretionary powers have standing to be considered in relation to the operation of the rule, the question is whether this standing applies only to a sub-set of such objects. If it does, then again the trust may be subject to termination contrary to the wishes of the settlor.

Finally, massively discretionary trusts create certain risks inasmuch as the decision-making processes of the trustees become the final word—one might say the only word—as to who benefits from the trust. If trustees take too much direction from the settlor, there is a risk of a finding of sham or that the settlor is a de facto trustee. But even if they aim to decide independently, the terms of the trust give them precious little to go on. The wishes of the settlor take on a dominant role, so much so that the structure seems to be a kind of purpose trust. If it were found that the genuine intention of the settlor, shared by the trustees, was that the trustees should implement the wishes of the settlor (rather than act in what the trustees perceive to be the best wishes of the beneficiaries), then there is a serious risk of a finding of invalidity and hence of a resulting trust. This is a risk for both the 'Red Cross' variant and the 'family' variant of massively discretionary trusts.

Even where trustees' decisions control everything, English law continues to hold that trustees are not required to give reasons for their decisions, or to produce letters of wishes, at least in family trusts. I suggest there is a serious possibility that this principle is subject to revision in a higher court, or to not being followed in other jurisdictions, or both. Accountability is part of the irreducible core of trusteeship, and secrecy does not stand comfortably beside accountability. But however the rules on disclosure may evolve, it seems clear that a massively discretionary trust invites more litigation than a trust with constrained discretions, because in the former context, all the benefits that are derived from the trust come from the decisions made by others in the exercise of (usually fiduciary) powers. Those affected will at least want to know the reasons. I do not think that hiding that information from them will reduce the litigation risk.

What all these risks have in common, in my view, is that massively discretionary trusts are a kind of deformation of the trust device. The common law trust is an enormously flexible institution. It does, however, have a certain logic to it. Trusts have features that are definitionally present, in the sense that if those features are not present, the structure is not a trust. Because, by definition in the common law, a trust is an obligation regarding the benefit of property that is owed to one or more beneficiaries, a trust needs a beneficiary. And because, by the same definition, the trust exists to benefit the beneficiary, the trustee is accountable to the beneficiary and must

provide her with all relevant information about the trust.[123] Those who create massively discretionary trusts seem to wish to create trusts that do not have one or both of these basic features. It is a deformation of the trust to create a structure in which there is no real beneficiary; and it is a deformation of the trust to create a device in which beneficiaries have no significant rights.[124] They are, in the end, the same deformation.

Because, by the same definition, the trust exists to benefit the beneficiary, the trustee is accountable to the beneficiary and must provide her with all relevant information about the trust

The evidence of this is the supreme importance of the letter of wishes. Of course, an express trust is an expression of the wishes of the settlor. But the central axis of the trust is the legal relationship between the trustees and the beneficiaries. To the extent that the wishes of the settlor become terms of the trust, they are built into that relationship.[125] To the extent that they do not, they are not. A settlor who wants to create a structure in which his wishes are controlling, but are at the same time not legally binding, so that they can be variable and secret, has misunderstood the nature of the trust.

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As in many fields of the common law, there has been a gradual evolution, over long years, in styles of trust drafting. This kind of gradual evolution may make it more difficult for judges to notice when a line has been crossed, from what is acceptable to what is impossible. A common law trust with no beneficial interests is impossible. It is a violation of the beneficiary principle and a violation of the rule against non-charitable purpose trusts.[126] A common law trust in which the trustees do not owe duties of accountability to the beneficiaries is also impossible. If you want people to hold property without being accountable to beneficiaries, then you do not want a trust. A trust in which the trustees are to be guided, not by the best interests of the beneficiaries but by the wishes of a person who is neither a beneficiary nor a trustee, is also impossible according to the common law. It is either a trust for that person, or a non-charitable purpose trust, and since the latter is impossible, it leads to a resulting trust.

Massive discretions can sometimes be a smokescreen to try to make possible the impossible. Courts should be vigilant.

Massive discretions can sometimes be a smokescreen to try to make possible the impossible

123. John Langbein has compared trusts to contracts, in pursuit of an argument that favours maximum flexibility of trust terms and prioritizes the settlor–trustee relationship over the trustee–beneficiary relationship (J Langbein, 'The Contractarian Basis of the Law of Trusts' (1995) 105 Yale LJ 625). But Langbein accepts that this is only an analogy, because many features of trusts are mandatory. These include the rule that a trust must benefit the beneficiaries, regardless of idiosyncratic wishes of the settlor; it follows directly that trustees' accountability to the beneficiaries is also mandatory: see the articles cited in n 79.

124. DWM Waters, 'The Future of the Trust from a Worldwide Perspective' in D Hayton (ed), *The International Trust* (3rd edn, Jordans 2011) 837. See also the comments of Young J in *Gregory v Hudson* (1998) 41 NSWLR 573 (SC), 586–87; aff'd (1998) 45 NSWLR 300 (CA).

125. Subject to the rule in *Saunders* (n 47), which ensures that the trust does not become a kind of non-charitable purpose trust (see n 79).

126. In some of the settings in which this article was presented, the observation was made that settlors who wished to create such arrangements could always take advantage of other legal systems that do permit them. Of course, this is true, but I never quite understood the point of the observation. If it was to say that money is mobile and people are generally free to move it, then it is difficult to disagree. If it was to argue that the common law should follow suit, whether by judicial development or by legislation, then on the contrary it is difficult to agree. Even a child is not permitted to argue that a course of conduct is acceptable merely because others are doing it. Arguments for law reform must go to the substance, and in this context must show why settlors should be able to launch assets into a plane in which no one seems to have any right to benefit from them, except the settlor whose settlement, and probably subsequent wishes, control the application of the assets, even while he is to be able to say that he has given them away when it comes to dealing with his own liabilities. For arguments against following the trend of offshore trust legislation, see Smith (n 8).

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