The New Trusts Act and What Trustees Need to Know

Executive Summary

This paper discusses the new Trusts Act 2019 and its implications for trustees' obligations and duties.

The new Act will come into force in February 2021 and modernises and clarifies trusts law in New Zealand. For trustees the Act specifies:

- key default and mandatory duties to fulfil, and
- an obligation to keep and make information available so that beneficiaries can enforce their rights.

The new disclosure of information provisions will improve transparency, as informed beneficiaries are better able to enforce their rights and interests. It should also improve end outcomes for beneficiaries through clarifying trustee duties, especially the general duty of care and the duty to invest prudently.

For trustees overseeing the management of assets and investments the new Act raises the standard expected in the exercise of their fiduciary duties. With this comes potentially heightened reputational and liability risks if these duties are not performed well.

To help meet your obligations as a trustee it is important that sound investment governance processes and practices are well-understood and followed. The **Prudent Practices for Investment Stewards** offered through Fi360 training programs and support provides a tried and tested practical framework for Trustees. In this paper we provide information on how the Prudent Practices relate to trustee's duties under the Act.

Introduction

A significant part of New Zealand's assets and wealth is held and managed in a trust, and it is estimated that there is one trust for every twelve people.[1] This includes family trusts, Māori and Iwi trusts, charitable trusts and foundations, and other special purpose trusts. For this reason, the governance of trusts and trusts legislation is critical.

In 2009, the Law Commission began a comprehensive review of New Zealand's trust law, which resulted in the introduction to Parliament of the Trusts Bill 2017. After a two year passage through Parliament, the Bill received Royal Assent on the 30 July 2019, with the passing of the new Trusts Act 2019 (the Act). The Act comes into effect in February 2021.

The new Act replaces the Trustee Act 1956 and the Perpetuities Act 1964. The Trustee Act 1956 was described by the law Commission as containing "some of the most lengthy and technical provisions on our statute book" and being "increasingly irrelevant to modern day legal practice".[2] Historically, the law of trusts, has neither been well understood nor easily accessible for many trustees and

[1] MoJ Hon Andrew Little, transcript of third reading of the Trusts Bill.
[2] At [4.46] and [4.37].

beneficiaries. The 1956 Act was very complex, and many fundamental trust principles were found in common law rather than presribed in the old Act.

The new Act clarifies duties and information obligations for trustees. It sets out trustees' obligations that were previously mainly found in case law. One of the guiding principles of the new Act is to ensure trustee's duties directly relate to the terms, context and objectives of a particular trust[3]. For trustees who oversee investments in a trust, this means **a core requirement is to know standards, laws and trust provisions.**

In regard to information, the Act specifies that trustees have an obligation to keep and give information.[4] Trustees will need to keep core documents relating to the trust. These documents should contain the information necessary for the administration of the trust and include trusts deeds, records of trustee decisions, financial statements and financial records.[5]

The provisions for the disclosure of trust information are also clarified in the Act.[6] A trustee's duty is to be accountable to beneficiaries and manage a trust in accordance with the terms of the trust. The Act places a presumption that a trustee must provide information and sets out factors that trustees must consider with respect to what is provided.[7] At present, many trustees are unaware of what their obligations are when faced with this situation.[8]

Under the new legislation, beneficiaries will have the right to access information such as the financial performance of their assets, trust distributions, and trust administration.[9] The **Act's approach to disclosure paves the way for increased awareness of beneficiaries' right to be informed and hold trustees to account.** This is in-line with the transparency and accountability focus of the new Financial Advisers Amendment Act (2019), which regulates advice provided to retail investors, and increasing transparency in larger scale 'wholesale' investment entities, such as KiwiSaver providers and New Zealand Community Trusts.

An implication is that the new **Trusts Act will only increase the reputational and liability risks trustees face if they do not properly apply prudent investment governance practices and oversight.** The Act also makes it clear that it will not be possible for trustees to be "indemnified for dishonesty, wilful misconduct, or gross negligence that is intentionally in breach of the terms of a trust".[10]

What is Investment Governance?

Investment governance is a specialised discipline focusing on the legal duties of care and loyalty (fiduciary obligations) owed by **investment fiduciaries**. Investment fiduciaries are usually people who either give investment advice or oversee the assets of another party and who stand in a special relationship of trust, confidence and legal responsibility. In this paper, we focus on those investment

[3] Section 4(a).
[4] Subpart 3.
[5] This list is not exhaustive refer to Section 45.
[6] Section 51-55.
[7] Section 52(a) and 53.
[8] Issues in this area were under the spotlight in the New Zealand courts, culminating in the Supreme Court's judgment in *Erceg v Erceg*,[8] which clarified the approach trustees should take in deciding how to respond to a beneficiary's request for trust information. The Act incorporates many of the elements of this case.
[9] MoJ Hon Andrew Little, transcript of third reading of the Trusts Bill.
[10] MoJ Hon Andrew Little, transcript of third reading of the Trusts Bill.

fiduciaries in governance roles, **Investment Stewards**. Investment Stewards are often trustees who oversee the investment of money or assets for the benefit of other people or charitable purposes.

Investment governance seeks to define what investment fiduciaries should do and the systems and processes they should have in place in order to fulfil their fiduciary obligations relating to investments. It involves working to a defined, objective fiduciary standard, and being able to demonstrate that this is consistently and effectively applied. Good investment governance helps ensures trustees follow sound decision-making processes when devising an investment strategy, and when selecting and monitoring investments and investment service providers.

Fi360 Pacific provides education and training in investment governance best practices with reference to an objective fiduciary standard devised by Fi360 in the United States and MyFiduciary (a sister company to Fi360 Pacific). Fi360 Pacific and MyFiduciary assist organisations and boards with the implementation of investment governance practices.

Trustee's Duties and Investment Governance

The new Act sets out the duties of trustees. Trustees' duties are divided into those duties that cannot be excluded or modified by the terms of the trust (mandatory duties) and those duties that can be modified or excluded by the terms of the trust (provided such modification or exclusion is not inconsistent with any of the mandatory duties).

The focus of investment governance as a discipline is to help entities put practices and processes in place to ensure trustees fulfil their duties in respect of a trust's investments. In regard to the duties as set out in the Act, it can help with:

- the **duty to know the terms of trust**: A trustee must know the terms of the trust[11] (mandatory duty);
- duty to **act in accordance with the terms of the trust**[12] (mandatory duty);
- duty to **act honestly and in good faith**[13] (mandatory duty);
- the general **duty of care**: when exercising any power or performing any function in relation to a trust (other than the exercise of a discretion to distribute trust property), trustees must exercise the care and skill that is reasonable in the circumstances (default duty);[14]
- the **duty to invest prudently**: when exercising any power of investment of trust property, trustees must exercise the care and skill that a prudent person of business would exercise in managing the affairs of others (default duty);[15] and
- the duty to **avoid conflict of interest**: trustees must avoid a conflict between the interests of the trustee and the interests of the beneficiary (default duty)[16].

[11] Section 23.
[12] Section 24.
[13] Section 25.
[14] Section 29.
[15] Section 30.
[16] Section 34.

Sound investment governance helps trustees meet their duties to their beneficiaries. For example, a trustee-owned, governance-orientated Investment Policy Statement (IPS) enables trustees to follow processes consistent with their trust's objectives. The IPS defines the duties and responsibilities of all parties involved in the investment process. It sets out due diligence procedures for trustees' selection of investment service providers which help avoid conflict of interests. It defines monitoring criteria to assist trustees exercise the necessary care and skill when making decisions about investments, their performance and costs.

The IPS helps trustees to have an investment strategy that is consistent and aligns with the objectives of the trust. In the Act a trustee "*exercising any power to invest may have regard to the following matters, so far as they are appropriate to the circumstances of the trust… the trustee's overall* ***investment strategy****."*[17] In the instances of a breach of the duty to **invest prudently**, the Act specifies the Court needs to consider whether trusts investments have been **diversified** and whether they have been made in accordance to the **investment strategy**. [18]

Good investment governance practices both increase the likelihood of improved investment outcomes and lessen potential reputational and liability risks. For investment trusts it means trustees must effectively use resources, people, processes and policies to fulfil their duties to their beneficiaries. Trustee obligations are not perfunctory, as they have a **duty of care**. These cannot be fulfilled by a simple process of "box-ticking". Investment Governance is continuous and dynamic, it is a process that is repeatable, defensible and documented.[19]

Trustee's Obligations to Keep and Give Information to Beneficiaries

The Act significantly improves the accessibility of the legal principles that should guide trustees when managing trust information and its disclosure to beneficiaries.

The Act attempts to balance the general principles from case law affirmed by the Supreme Court in *Erceg v Erceg*. A beneficiary has a right to have the trust properly managed and hold trustees to account, which is a key foundation of trusts, and the right to seek disclosure of trust information from trustees is ancillary to this.[20]

What does the Act actually say about the obligation to keep and give trust information?

The Act specifies that trustees have an obligation to keep and give information.[21] Trustees must **keep core documents relating to the trust**.[22] These are documents necessary for the administration of the trust and include the trust deed, trust property, records of decisions, accounting and financial statements etc.[23]

[17] Section 59(1)(n).
[18] Section 128.
[19] Investment Governance for Fiduciaries, 2019. E, Drew and A, Walk.
[20] *Erceg v Erceg* [2017] NZSC 28, at [49].
[21] Subpart 3.
[22] Section 45.
[23] This is not an exhaustive list refer to Section 45.

Good investment practices and processes can help fulfil this obligation. For example, Fi360 global fiduciary practice on keeping a "fiduciary file" requires a trustee to safe-keep and organise documents of the trust in a centralised location.[24] Documents in the fiduciary file will generally at least include:

- Trust documents;
- The investment policy statement (IPS);
- Service agreements with Advisers or other providers;
- Due diligence files;
- Investment performance reports;
- Committee Meeting minutes; and
- Custodial and brokereage statements.

Trustees will be entitled to keep the reasons for their decisions confidential.[25] However, much of the information trustees hold regarding investments could potentially be subject to a beneficiary's request for information if these documents could assist in enforcing the trust.[26] Relevant documentation could include, for example:

- the Investment Policy Statement (IPS) or any other investment policy document (e.g. SIPO) of the trust;
- documents that evidence monitoring of investments and investment service providers; and
- documents evidencing the efforts trustees went to carry out due diligence on providers before engaging them. This is particularly important as the bar is rising as to what constitutes acceptable due diligence.[27] Also, in today's world of information access, it has never been easier for beneficiaries to do their own research into providers and make their own judgments against which to measure trustees' decisions.

The Act establishes two presumptions in favour of disclosure of information to beneficiaries. Trustees may decide not to comply only if certain factors weigh against disclosure.

The first presumption is that a "trustee must notify basic trust information" to beneficiaries.[28] This means that trustees should provide basic trust information to beneficiaries and will need to consider whether to make this information available at regular intervals. The Act defines **basic trust information** to include[29]:

- the fact that that person is a beneficiary of the trust;
- the name and contact details of the trustees;
- any appointment, removal and retirement of a trustee; and

[24] Fi360 Global Fiduciary Practice 1.2.3
[25] Section 49(b).
[26] Section 49(a)(ii).
[27] refer to article *Trustees – now's the time to recalibrate your provider radar,* June 2016 available at www.fi360.co.nz for further explanation
[28] Section 51.
[29] Section 51(3).

- finally, the fact that the beneficiary has a right to request a copy of the terms of the trust or trust information.

The second presumption is that when a beneficiary requests trust information, trustees must give them that information within a reasonable period of time following the request.[30]

Trustees can only decide against making information available despite the above presumptions after considering certain factors, bearing in mind their general obligation is to disclose enough trust information to enough beneficiaries to enable the trust to be enforced.[31] The factors that trustees must consider are[32]:

- the nature of the interests in the trust held by the beneficiary making the request and other beneficiaries, including the likelihood of the beneficiary receiving trust property in the future;
- whether the information is subject to personal or commercial confidentiality;
- the expectations of the settlor at the time of settlement of the trust as to disclosure of information to beneficiaries;
- the age and circumstances of the beneficiary making the request and of the other beneficiaries;
- the effect of disclosing the information on trustees, other beneficiaries and any third parties;
- in the case of family trusts, the effect of disclosing the information on relationships;
- in a trust that has a large number of beneficiaries or unascertainable beneficiaries, the practicality of giving information to all beneficiaries or all members of a class of beneficiaries;
- the practicality of imposing restrictions and other safeguards on the use of the information (for example, by way of an undertaking or restricting who may inspect the documents);
- the practicality of disclosing some or all of the information in redacted form; and
- the nature and context of a beneficiary's request for information.

The Act leaves room for trustees to withhold information where it would be damaging to disclose it, as was the case in *Erceg v Erceg*.[33] However, whether and what information should be disclosed will depend on the obligation the beneficiary is seeking to enforce and other considerations, such as confidentiality.[34]

[30] Section 52(1).
[31] Section 50(1).
[32] Section 53.
[33] In that case, the plaintiff sought a wide variety of documents and the trustees declined to disclose any of them to the plaintiff. The Supreme Court upheld this decision for several reasons, including, for example, the beneficiary's remote interest in the relevant trusts (he was not a named beneficiary of either trust, but one of a class of primary, secondary or final beneficiaries), commercial confidentiality of some documents sought and the potential for the plaintiff to harass other beneficiaries if their identity was disclosed.
[34] Section 51 (2)(b) and Section 53(b).

In deciding whether to disclose trust information, trustees must identify the course of action that is most consistent with proper administration of the trust and the interests of all beneficiaries, not just the beneficiary requesting disclosure.[35]

The Act's presumptions in favour of disclosure as well as the requirement that trustees provide beneficiaries basic trust information will improve transparency and accountability. Informed beneficiaries are better able to enforce their rights and interests. Trustees will face more scrutiny which increases reputational and liability risks. Trustees most at risk will be those who do not have good investment governance practices. This means having an Investment Policy Statement (IPS) and ensuring sound due diligence and monitoring processes are followed.

What Can Trustees who are Investment Stewards do to Prepare for the Trusts Act?

Many busy trustees, especially professional trustees, have relied on the simple yardsticks of brand, apparent costs and client satisfaction for investment provider selection or referrals. However, these measures are not suitable from a fiduciary perspective. A good place to start in preparing for the new Trusts Act and any increases in disclosure of trust information is for trustees to consider systemising the approach to investment governance responsibility. A key ingredient of doing so is adopting processes that are aligned against a defined investment governance standard, such as that developed by Fi360. This is equally applicable to all trustees, including professionals offering independent trustee services to clients.

Special Considerations for Professionals Acting as Trustees

The Act includes the common law principle that, for the purposes of the general duty of care and the duty to invest prudently, the standard of care and skill expected of trustees with particular skills and experience as professional trustees will be higher than the standard expected of other trustees. The Act proposes that performance of these duties will be assessed with regard to:

- any special knowledge or experience of a trustee;[36] and
- if a person is acting as trustee in the course of their business or profession, any special knowledge or experience that is reasonable to expect of a person acting in the course of that kind of business or profession.[37]

This will likely affect many lawyers and accountants and other professionals who act as independent trustees for clients, companies that provide professional trustee services and those with special legal, investment or financial knowledge who volunteer their time and skills as trustees of charitable, Māori and other trusts. It will be important for these type of trustees to adopt good investment governance as well as access good support services and information.

[35] Section 53(g).
[36] Section 29(b) and 30(a).
[37] Section 29(b) and 30(b).

Conclusion

The new Trusts Act will significantly improve the clarity and accessibility of New Zealand's trust law for both trustees and beneficiaries. The proposed provisions regarding disclosure of trust information to beneficiaries will likely alert beneficiaries to their rights and interests, resulting in increased transparency and increased risk for trustees. Trustees who oversee investments in capital markets must take care to ensure they are fulfilling their duties, especially the duty to invest prudently. Employing best investment governance practices and following an objective investment governance standard can be of great assistance in achieving this.

About MyFiduciary's Investment Governance Support Services

Good investment governance can prevent trustees from potentially breeching their fiduciary obligations of care. For example, we would argue it is not a good governance practice for trustees to get in the weeds of investment management (e.g. choosing or approving individual security or fund selections); instead this is a task that is best delegated to investment professionals (such as advisers or asset consultants). In turn selecting such providers needs a proper evidentiary basis.

MyFiduciary offers support services to trustees and professional firms who either offer independent trustee services to clients, or wish to offer guidance on good investment governance and valid provider referrals. Our support services include:

- Investment governance training: We provide Fiduciary Education courses and in-house workshops, as well as on-line training that meet various PD requirements.
- Investment governance assessments: We provide confidential assessments for Trustees as well as assessments that garner the internationally recognised Centre of Fiduciary Excellence (CEFEX) accreditation.
- Provider due diligence: We provide structured due diligence reports on providers (Advisers, Fund Managers and Custodians).
- Fiduciary management: We assist investment entities develop investment policies and strategies, review providers, and manage assets. This includes economic commentary, asset allocation, model portfolios, approved product lists, investment due diligence, and monitoring and reporting.

For more information, visit our websites at www.MyFiduciary.com and www.fi360.co.nz

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