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RELATIONSHIP PROPERTY AND TRUSTS: THE "BUNDLE OF RIGHTS" THEORY?

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Contents

Abstract

This dissertation examines the "bundle of rights" theory as it meets at the intersection of trust and family property law. Drawing on conceptions of property, the principles and purposes of the Property (Relationships) Act and contrasted with trust law, a theory is adopted to explain why family property law has presumptive power over trust principles.

Orthodox trust principles are discussed to explain why trust assets are protected from third party claims, the importance of the laws of powers and fiduciary obligations, the problems created by settlor or appointor control and the reason a "controller" is a beneficial owner of trust assets.

The dispositions of relationship property to trusts and the limits on compensatory payments are discussed alongside the significance of the abolition of gift duty, other statutory remedies and judicial responses. Case authorities are explored, similarities with Australian alter ego *trusts are drawn upon, and the application of the "bundle of rights" theory is discussed with reference to the valuation of debts and occupation orders.*

The dissertation concludes that the "bundle of rights" theory draws on an expansive meaning of property, it is a principled approach but confined to the Act.

Word length

The text of this paper (excluding abstract, table of contents, footnotes and bibliography) comprises approximately 34,475 words.

Subjects and Topics

Property- Bundle of Rights
Property (Relationships) Act 1976–Family Law Act 1975 (Australia)
Trust Powers-Fiduciary Obligations-Discretionary Trusts

I Introduction

This dissertation discusses aspects of the meaning of property under the Property (Relationships) Act 1976 ("PRA").[1] That definition of property includes the phrase rights or interests and recently Judges have considered that in certain circumstances a spouse, civil union or de facto partner[2] may have a property interest in a discretionary trust. This development in the law has become known as the "bundle of rights" doctrine.

This doctrine is highly controversial because orthodox trust principles are based on a presumption that a discretionary beneficiary has no more than a mere expectancy of an interest in the trust's assets until the trustees exercise their discretion and make a capital or income distribution to that particular beneficiary. Until that day arrives a discretionary beneficiary has no property interest in the assets of the trust.

The possibility that interests in discretionary trusts can be given a property status has polarised those who practise in trust and family law. To some trust lawyers the doctrine has been viewed as unprincipled because it disregards the trust relationship and cuts across the importance of a trustee's fiduciary obligations to its beneficiaries.

However, from the family lawyer's perspective the use of many discretionary trusts is seen as a device used to create an illusion of separate ownership of assets as a means of sheltering wealth that has accumulated during the relationship and should not be allowed to defeat the principles and purposes of the PRA. An expansive meaning of property which includes interests in discretionary trusts is seen as justified in the context of social legislation which regulates the rights and obligations of those in qualifying relationships.

This dissertation examines the "bundle of rights" principles and the way in which the law in this area is likely to develop without the intervention of Parliament. As will be seen trust and family law has met at a critical intersection and this dissertation considers whether there is some theory that can explain the circumstances when the law grants property status to some rights and interests at the expense of others, whether the use of the modern discretionary trusts are eroding orthodox trust principles, whether the doctrine

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1 Property (Relationships) Act 1976, which will be referred to throughout this dissertation as the "PRA."

2 As the PRA affects those who are married, in a civil union or a de facto relationship, this dissertation will refer to those in these three classes either as a spouse and/or a partner or as a party.

draws upon the *alter ego* trust principles which have developed in Australian family law and whether the "bundle of rights" doctrine is a species of family property and not transferable to the general law of property between strangers.

It is in these circumstances that this dissertation examines the current PRA, its structure; the way in which it currently responds to the disposition of property into a trust during a qualifying relationship and remedies that may be available at the end of the marriage or de facto relationship. No attempt is made to consider possible statutory reforms although this dissertation does consider the current mixed and inadequate statutory responses to the disposition of relationship property into discretionary trusts. It is also acknowledged that the Law Commission[3] is currently reviewing the law of trusts and submissions have been called on its second issues paper which considers the use of trusts in both relationship property and other contexts.

[3] Law Commission "Some Issues with the use of trusts in New Zealand: Review of the law of trusts second issues paper" (NZLC IP20, 2010).

II Property and its Meaning and Power

A Theory

Property has been powerfully described as "an assertion of self and control of one's environment and provides human beings with a place of deep psychological refuge. With its concreteness and its unfailing assurances, property promises to protect us from change and from our fear that we will leave no evidence of our passage through this world."[4] During our lifetime, property is often the way in which individuals assert their sense of self-worth and at times of great emotional distress, when personal relationships disintegrate, property provides security and helps to restore a sense of equilibrium in times of psychological chaos.

Ownership of property can also be a reflection of financial, emotional and psychological power in a relationship. It comes as no surprise that, at the time of separation, parties to a relationship will often exhibit negative feelings, distrust and fear which are heightened in situations where the ownership and control of wealth, produced during the relationship, is controlled by one party. An imbalance in power and control has long been recognised as inequitable and should not be allowed to defeat the principles of the PRA[5] that men and women are of equal status and all forms of contribution to their relationship are to be treated as equal.

The following is a general discussion of the meaning of property and is not an attempt to examine a vast body of literature on property theories or to draw together a conceptual understanding of property in the context of family or trust law. Instead, the focus is on the conflict that arises when the law recognises and protects property rights and interests for hundreds of years and these legal principles are then challenged by social legislation where the meaning of property has been extended to include rights and interests which traditionally have not been given the status or property. The question that then arises is whether there is a conceptual theory which can explain when and why some property rights and interests will be given priority over others.

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4 Laura S Underkuffler *The idea of property: its meaning and power* (Oxford University Press, New York, 2003), ch 1 at 1.

5 Property (Relationships) Act 1976, s 1N.

What does the word property mean? The word is simple and arises from the Latin *proprietas* or ownership but on its own the word only conveys a sense that property is associated with things that are owned. For the lawyer, property is sometimes referred to as a "bundle of rights" and presents a picture that property is a collection of rights over things enforced against others.

William Blackstone[6] had an immense influence over the development of concepts of property and in his books entitled "Of the Rights of Persons" and "Of the Rights of Things" he distinguished between the rights in respect of persons and things and drew a distinction which has provided " … the basis for a general structure of legal concepts. It is within that general structure that myriads of judgments and statutes have been written."[7] Yet it is important to acknowledge that Blackstone did not attempt to define the scope of property and his commentaries, written nearly 250 years ago, illustrate his underlying anxiety and uncertainty as to the boundaries of the meaning of property.

Professor A M Honore, in a classic treatment of the nature of ownership, identified eleven elements that he claimed provided the widest conception of property to be found within a mature legal system. He said:[8]

> Ownership comprises the right to possess, the right to use, the right to manage, the right to the income of the thing, the right to the capital, the right to security, the rights or incidents of transmissibility and absence of term, the duty to prevent harm, liability to execution and incident of residuary.

This picture of property, as a conglomeration of rights, provides a broad understanding as to what may be included in the definition of ownership but it does not identify any core features which must be present if a right is to be given legal status.

This hunt for a definitive understanding of what constitutes property has eluded theorists and Underkuffler has described it as "a complex package of normative choices that are not fully or adequately explained by any of the conventional understandings of property."[9]

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6 W Blackstone "*Commentaries on the Laws of England*" (1765).

7 *Z v Z* (No 2) [1997] 2 NZLR 258 (CA) at 278.

8 A M Honore "Ownership" in *Making Law Bind* (Clarendon Press, Oxford, 1987) at 165 and also referred to in Bruce Ziff *Principles of Property Law* (Thomson Canada Ltd, 4th ed, 2006) Ch 1 at 2.

9 Ibid above n 4 at 1.

In addition the difficult task that property theory has faced is:[10]

> The construction of a workable theory for determining property's presumptive power while acknowledging that the values that property claims assert are socially constructed, changeable and often contentious in nature. There is a tendency in the pursuit of property theory either to ignore the socially constructed and volatile nature of property, in an attempt to provide predictive power for a proffered theory or to acknowledge and then effectively end the enquiry.

Underkuffler argues that traditional theories of property have focused on a theory of rights and space. A theory of rights enables consideration of the rights, privileges, powers and immunities of individuals. However, on its own this dimension does not explain the ability of a property owner to engage in activities which either erode or affect another property owner's interest.[11]

A dimension of space fits easily within a framework of land or other corporeal things but where property is of an incorporeal nature descriptions such as 'scope' 'extent' or 'limits' are more appropriate descriptions of this dimension.[12]

In addition, property also needs to be seen through the dimensions of stringency and time. Stringency refers to the degree of protection afforded to a right. A hierarchical ordering of rights has been called "one of the essential sticks in the bundle of rights"[13] and the degree of protection afforded to that right will be indicative of whether, in law, it is granted a property status. Finally, the dimension of time is necessary to determine not only when a property right comes into existence but also to assess whether it is fixed or variable.[14] To put it simply, the devil is in the detail.[15]

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10 Ibid above n 4 at 7.

11 Ibid above n 4 at 20.

12 Ibid above n 4 at 22.

13 Ibid above n 4 at 25.

14 Ibid above n 4 at 29.

15 Ibid above n 4 at 5.

B Conceptions of Property

Conceptions of property are important because they indicate the circumstances when competing rights could be given priority over other property rights. A common conception of property involves an assumption that when individual interests are recognised as property and protected they are then presumed to be superior to all conflicting claims thereafter. On the other hand an operative conception of property is based on the theory that property represents "the outcome of individual/collective tensions, determined and redetermined as circumstances warrant."[16] Therefore a proponent of a common conception of property places a high value on the prevention of arbitrary changes whereas a proponent of the operative conception of property acknowledges that property claims involve conflict, fluidity and change.

However, whilst dimensions of property and legal conceptions of property do offer a theoretical explanation as to the development of individual rights and interests they do not explain the variable power of rights and why some rights are given presumptive power over others. Often, it is assumed that the law recognises the presumptive power of rights on a principled basis because the interests that underlie those rights involve values that are more important or more worthy than competing rights.[17] How the law assesses the values that underpin a property right necessarily involves an examination of conflicting and changing social attitudes over time.

This normative hypothesis for the power of rights is in keeping with common notions of what rights are and why they are recognised in law. Under this hypothesis, the presumptive power of rights adheres only if the values that the right involves are not shared. Consequently, if the claimed rights have been recognised in law then they will continue to have presumptive power because the core values are different in kind.

Whereas, in situations where the core values between competing rights are the same in kind, then they are viewed as presenting competing interpretations about the nature of foundational rights that they both rely upon. In those circumstances "the conflict between them is a struggle that is internal to that right, over that right's definition, scope and meaning. The claimed right and the competing public interest are of presumptively equal power".[18]

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16 Ibid above n 4 at 62.

17 Ibid above n 4 at 74.

18 Ibid above n 4 at 75.

I will consider the opposing and shared core values that give substance to the meaning of 'rights or interests' under the PRA together with the meaning of rights or interests afforded to beneficiaries of a discretionary trust and the rights of trustees to manage and appoint property to themselves as a discretionary beneficiary.

Underkuffler provides a model which predicts when claimed rights should have 'trumping power' over other rights.[19] In particular, traditionally claimed rights will have presumptive power over competing interests when the core values under the claimed right are different to the competing interests.

However, where the claimed rights and competing public interests share the same core values they are viewed as competing for the same foundational right and the "conflict between them is a struggle that is internal to that right's definition, scope and meaning"[20] and in those circumstances each competing right and interest are of presumptively equal power. For instance, a publisher of pornography may seek to justify publication on the basis of a right to free speech, whereas those that oppose publication do so on the basis that it has the effect of silencing those who are degraded by it. In these circumstances both sides are relying on different aspects of the core values of freedom of speech such as "the promotion of personal autonomy and the need for a vibrant and varied public discourse."[21]

This model also recognises that property rights are not necessarily constant and unchanging. The meaning and extent of property rights are always subject to the "wider context"[22] which is driven by what society decides are core values which should be protected over others. Consequently, a right or interest which required the protection of the law a hundred years ago may have a weaker foundational claim to that protection in the modern context.

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19 Ibid above n 4 at 74.

20 Ibid above n 4 at 75.

21 Ibid above n 4 at 78.

22 *Z v Z (No.2)* above n 7 at 279.

C Core Values in Trust and Family Law

In order to apply this model it is necessary to consider the protection afforded by equity to the power to appoint assets of a discretionary trust as well as administer the trust with the core values that underpin the definition of property under the PRA. This is not to suggest that all discretionary trusts share the same core values with the principles and purposes of the PRA. However, there are an increasing number of discretionary trust deeds where the power to control the trust is centralised and given to a spouse or partner and it is the writer's view that these types of discretionary trusts share three shared core values with the principles and purposes of the Act, namely the control, protection and preservation of property for those in qualifying relationships.

To expand on this proposition it is necessary to consider the function of the discretionary trust, its characteristics and codes of regulation. The express trust has been described as "equity's imposition of stringent personal obligations upon a legal owner to hold property for the benefit of another, with the result that a trustee cannot treat the property as their own."[23] The discretionary trust is one form of an express trust and it enables the trustee to select who is to get what benefit from the trust's income and assets and generally has no obligation to distribute all of the trust's income and assets, at any time, leading up to the date of final distribution. This structure is inherently flexible, can meet changes in circumstances and needs of beneficiaries as well as protect the trust's assets from third party claims.

The growth in popularity of the modern discretionary trusts is also a product of a risk-adverse society which seeks protection from the arms of the unsecured creditor, the Official Assignee, endeavours to obtain state funded benefits such as residential home care subsidies as well as minimise tax liabilities. Not infrequently, the discretionary trust structure is seen as a means of side stepping the statutory safeguards provided by the PRA to those in a qualifying relationship.

The ability to control the trust fund is found in the unfettered discretions granted to trustees to make payments to beneficiaries. Fiduciary obligations play a central part of the law of equity[24] and it is the means by which equity regulates the exercise of power by trustees and thereby protects the beneficiary from a trustee using their powers for

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23 J E Penner *The Law of Trusts* (6th ed, Oxford University Press, New York, USA, 2008) at 1.16.

24 Andrew Butler (ed) *Equity and Trusts in New Zealand* (2nd ed, Thomson Reuters, Wellington, 2009) at [17.1] [*Equity and Trusts*].

improper purposes and also to ensure that the trustee acts in good faith and in the best interests of the beneficiaries.[25] The public policy which underlies fiduciary law rests on a foundation of promotion and preservation of a trusting relationship. The strict application of fiduciary obligations is seen as providing effective protection.[26] In this way the law protects the rights of trustees to exercise their discretions without interference provided they act in a bona fide way.

The policies and principles of the PRA are also deeply embedded in the preservation and protection of property rights for those in qualifying relationships. The Act is neither a technical statute nor a part of the law of property in any traditional sense. The Act represents the culmination of a gradual process of statutory reform which leaves the property of the persons within its jurisdiction to be dealt with by a set of rules very different from those which govern the property of strangers in common law.[27] It is social legislation of the widest general application.[28]

Historically, in New Zealand, the common law approach to marital property was to vest title, control and ownership in the husband. This approach to domestic property was referred to as the unitary system. However, the Matrimonial Property Act 1976, created a deferred community property approach whereby property acquired during the marriage belonged to the community of both spouses but the rules of property ownership did not apply until the marriage ended either in separation or death. This system of deferred community property was extended to de facto relationships[29] and those in civil unions[30] and it spells out a strong bias in favour of equal entitlement of spouses and de facto partners to property created by their efforts during the relationship.[31]

The purpose of the Act[32] recognises the equal contributions made by qualifying spouses or partners to a relationship, that when that relationship ends there is to be a 'just'

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25 At [17.2.2(1)].

26 At [17.2.9].

27 *Family Law in New Zealand* (looseleaf, ed, LexisNexis) at 7.301 [*Family Law in NZ*].

28 At [7.302] also referring to *Reid v Reid* [1979] 1 NZLR 572, 580, 605 and 610 per Woodhouse and Richardson JJ.

29 Property (Relationships) Act 1976 s 2D, defines a de facto relationship and the Act came into force on 1st February 2002.

30 Property (Relationships) Act 1976 s 2B defines a civil union – came into force following the 2005 Amendment Act.

31 *Family Law in NZ* above n 27 at [7.302].

32 Property (Relationships) Act 1976 s 1M.

division of property in accordance with the rules contained in the Act. The principles which are intended to guide the achievement of the purpose are that the equal status of men and women should be maintained and enhanced, that all forms of contribution are to be treated equally, a just division has to take into account the economic advantages and disadvantages of the period of cohabitation and finally that questions "should be resolved as inexpensively, simply, and speedily as is consistent with justice." [33]

The recognition of equal contributions to the relationship also illustrates that a qualifying relationship is to be regarded as a partnership and "… not as a unity nor as a legal relationship between two strangers" and that the contributions of each party during the relationship are presumed to be of equal worth.[34] Further, the division of property is not about taking away from one party to give to the other because the principle of partnership recognises that each has an entitlement to share in their partnership assets. In this way common law concepts of property ownership have been subsumed under a framework of statutory rules aimed at protecting property interests for those in qualifying relationships to ensure that each should share equally in the material wealth generated by their partnership.

The gradual reform of family property law has been one steeped in notions of justice and common sense which have overcome legal formalism. By way of example, characteristics of 'debts' under the PRA may be subject to different interpretations to those in common law because:[35]

> That broad objective suggests that as far as possible there should be a general balancing of the benefits and burdens in the partnership ledger without fine regards to the technicalities which words such as 'debt' might attract in other contexts.

The PRA also provides a code of protection of property entitlements through its definition of relationship property,[36] conversion (in certain circumstances) of separate property to relationship property,[37] an ability to grant compensation[38] together with the

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33 Property (Relationships) Act 1976 s 1N.

34 *Family Law in NZ* above n 27 at [7.302].

35 Robert Fisher QC (ed) "*Fisher on Matrimonial and Relationship Property*" (on line looseleaf ed) Characteristics of 'Debt' and 'Owing' at [15.6].

36 Property (Relationships) Act 1976, s 8.

37 Property (Relationships) Act 1976 s 9 and s 9A.

38 Property (Relationships) Act 1976 s 15, 18A-C, s 44C.

safeguards imposed on parties who wish to contract out of the PRA.[39] In this way the PRA recognises the breadth of property entitlements as well as providing rules to ensure those rights are not unilaterally usurped.

Assuming that some discretionary trusts and family property law share the same core values then it is still necessary to consider whether case authorities favour a common or operative conception of property. In *Z v Z (No 2)* the Court of Appeal considered that the definition of property meant that:[40]

> The consistent, cumulative use of that definition and its use in this particular case strongly indicate that the conventional understanding of 'property' is being drawn on in this statute. That proposition is of course subject to the point that the concept of 'property' is fluid and has extended over the years to include interests which might not earlier have been covered by it. Its meaning and scope must also be affected by the statutory and wider context in which it is used. … The wider context includes changing social values, economic interests and technological developments …

In that case the Court had been asked to consider whether the husband's enhanced earning capacity could be a property interest. The Court of Appeal declined to expand the definition of property to include a spouse's future earnings. Nevertheless, it recognised that the husband's interest in his legal partnership was property despite the partners' agreement that their interest in the goodwill of the firm had a 'nil value'[41] and that interest could not be sold or transferred to a third party. The property interest was the 'bundle of rights' derived from the partnership which included the client base "which assists a partner to generate income"[42] in excess of an individual partner's output and a consequential right to share in these super profits, a retirement benefit as well as an expectation of continued membership until the date of retirement.

A common conception of property would focus on the retirement benefit as the property in question. Yet the Court adopted an operative conception by granting property status to the 'bundle of rights' arising out of the husband's membership of the law partnership.

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39 Property (Relationships) Act 1976, s 21 and s 21A.

40 *Z v Z (No.2)* above n 7 at 279.

41 At 289.

42 At 290.

It is the writer's view that despite the Court's reference to 'conventional'[43] understandings of the meaning of property, *Z v Z (No.2)*[44] illustrates that the PRA draws on operative concepts of property and consequently conflicting property rights and interests will involve fluidity and change. That is not to suggest that the courts have a general mandate to extend the meaning of property beyond that which Parliament has been willing to legislate but rather it recognises that in certain circumstances the courts have and will continue to expand the meaning of property to interests which traditionally did not have a property status. This is a result of a continual process of examination and evaluation of core values which justify the classification of those interests into either property or non-property status.

Consequently, within the boundaries and framework of the PRA, this dissertation will argue that an expansive meaning of property can include interests in some discretionary trusts particularly where a spouse or partner can control the administration and disposition of trust assets. An expansive meaning of property gives some interests in discretionary trusts a property status which is not recognised at common law. In these circumstances the family property rights are given 'trumping 'power over orthodox trust principles.

Before considering whether an expansive meaning of property can extend to interests in discretionary trusts it is necessary to consider the trust orthodoxy and the reasons that the law protects trust assets from third party claims.

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43 At 279.

44 Ibid above n 7.

III The Trust Orthodoxy

This chapter considers the way in which discretionary trusts operate in practice, the powers vested in trustees and their fiduciary obligations which regulate the trust relationship. It needs to be acknowledged that there are many differences within discretionary trusts and it is not intended to suggest that the matters raised in this chapter are comprehensive and applicable to all discretionary trusts.

However, the purpose of this discussion is to consider equity's response to the types of discretionary trust where trust powers are centralised and given to an individual who is a trustee and beneficiary and may also hold the power to 'hire and fire' other trustees. The essential question is whether orthodox principles are realistic and applicable to situations where wealth generated during a relationship is held in a trust fund.

A Features of Discretionary Trusts

As discussed in chapter 2 the structure of discretionary trusts are varied but they are inherently flexible, can meet changes in circumstances and needs of its beneficiaries.
To understand the dilemma between trust and family property law it is necessary to consider the features of discretionary trusts which culminate in the orthodox view that trust assets cannot fall within the definition of property under the PRA.

The starting point is that a discretionary beneficiary has no proprietary interest in the trust's assets but only a mere expectancy or hope that one day the trustees may in their absolute discretion decide to make a distribution to that beneficiary.[45] Until that decision has been made a discretionary beneficiary has a limited property right to the due administration of the trust, can hold trustees accountable for acting irrationally, capriciously or improperly, prevent trustees from breaching their fiduciary obligations and can trace misappropriated trust assets.[46] Nevertheless these rights do not create a property interest in the trust fund.

In contrast, under a fixed trust the beneficiaries are the equitable owners of the trust property and can deal with their interest, for instance by offering it as security for other

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45 *Gartside v Inland Revenue Commissioners* [1968] AC 553.

46 Nicola Peart "Relationship Property and Trusts" (paper presented to NZLS Intensive Relationship Property – your big (legal) day out. August 2010 at 5–10 ["Relationship Property and Trusts"]).

borrowings. The beneficiaries effectively own the entire equitable interest and if they are of full age and agree they can compel the transfer of the legal interest to themselves.[47]

Generally, the trustee's discretion to distribute assets is referred to as a 'bare power' which means it is a personal power – "which can be exercised only by the person or persons to whom it is given"[48] and cannot be assigned. Further it is a 'bare power' because the trustee is not under any obligation to periodically consider whether to exercise the power.

A power to distribute capital and/or income amongst a class of beneficiaries[49] may be – " … 'general' in that the donee is allowed to exercise it in favour of anyone he chooses, 'special' in that it can only be exercised in favour of specified persons, or purposes .. or 'hybrid' in that it is exercisable in favour of anyone except for specified persons of purposes."[50]

There is a significant difference between a general and a special power which Tipping J in the recent Supreme Court judgment of *Kain v Hutton* explained in this way:[51]

> A general power of appointment entitles the donee/appointor to appoint to anyone at all, including himself. There cannot therefore be excessive execution of, or a fraud on, such a power because it is logically impossible for the donee/appointor to exceed the donor's mandate. By contrast a special power enables the donee/appointor to appoint only to those specifically permitted by the donor's mandate. A special power is one where the objects of the power are limited by the terms upon which power is granted. An appointment to a person who is not a permitted object will usually represent an excessive execution of the power.

The modern discretionary trust deed tends to favour 'special' powers of appointment but concerns have grown that when a beneficiary effectively 'controls' the trustees then the power appears to be closer to a general power. However, before commenting further on the issue of 'control' it is necessary to consider the conceptual distinction between a

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47 *Saunders v Vautier* (1841) Cr & Ph 240; 41 ER 482.

48 Geraint Thomas *"Thomas on Powers"* (1st ed, Sweet & Maxwell Limited, London, 1998) at [1-48].

49 At [1.55].

50 At [1.55].

51 *Kain v Hutton* [2008] 3 NZLR 589 (SC), at [47] Tipping J.

'power' and 'property' and it is useful to repeat the often quoted passage from in *Re Armstrong*, when Fry LJ stated:[52]

> The question is whether the general power of appointment given to the bankrupt is her "separate property" within the meaning of sub-s 5 of s 1 of the Act of 1882. To my mind the question is one of the most elementary description, and if it had not been argued as it has, I should have thought it unarguable. No two ideas can well be more distinct the one from the other than those of "property" and "power". This is a "power" and nothing but a "power". A "power" is an individual personal capacity of the donee of the power to do something. That it may result in property becoming vested in him is immaterial; the general nature of the power does not make it property. The power of a person to appoint an estate to himself is, in my judgment, no more his "property" than the power to write a book or sing a song. The exercise of any one of those three powers may result in property, but in no sense which the law recognises are they "property" of the person in whom they are vested, because every special capacity of a person may be said to be his property: but they are not "property" within the meaning of that word as used in law. Not only in law but in equity the distinction between "power" and "property" is perfectly familiar, and I am almost ashamed to deal with such an elementary proposition.

The court's justification for the conceptual separation between 'powers' and 'property' has been explained by Congreve in the following way:[53]

> The consistent refusal of the Courts to characterise powers of appointment as proprietary interests reflects the view that powers are merely a form of contingent event. If a proprietary interest is defined as a right in or relating to property, a power or capacity to alter legal relations with respect to property might be regarded as carrying a property interest. However, the Courts have always regarded the donee of a power of appointment as merely a conduit for the conveyance of the donor. A donee of a power has no more than the capacity to act, to appoint or not to appoint, and the effect of the appointment derives from the instrument creating the power.

Whilst 115 years ago the distinction between a power and property was one of "most elementary description" it may not be so clear with the modern discretionary trust when dispositive powers are increasingly centralised and given to trustees who are also

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52 *Re Armstrong* (1886) 17 QBD 521 at 531-532.

53 Anthony Grant "Cradle to the Grave: the Interface between Property and Family Law" at 14 quoting from Dr R L Congreve "The Nature and Extent of Trustees' powers of appointment, selection and disposition" (PhD Doctorial Thesis) at 2-07.

beneficiaries. The ability by trustee/beneficiaries to benefit themselves makes it difficult to rationalise the proposition that a power is a form of contingent event when the distinction between legal and equitable interests is blurred.

A more compelling reason that powers cannot be equated with property rights rests on the platform that a trustee's discretions and beneficiaries' interests in the 'due administration' of the trust are protected by the shield of the laws of powers and fiduciary obligations which equity has evolved for the purpose of supervising the activities of those who are entrusted to act in the interests of others.[54]

The law of fiduciary obligations has been described as a "central part of the law of equity"[55] because the fiduciary is expected to act in the interests of the beneficiary and the law discourages behaviours which are inconsistent with the nature of the relationship between trustee and beneficiary.

This code of regulation occurs at two levels: firstly at the decision making stage where there is a duty not to delegate discretions, not to act under another's dictation; not to place fetters on discretions and to consider whether a discretion should be exercised. The second level refers to the exercise of powers where the court considers whether the trustee intends to defeat or depart from the intention of the settlor and these duties include: to exercise powers for relevant consideration and for the purposes for which they were given; not to act for the fiduciary's own benefit, or the benefit of a third person, to treat beneficiaries equally if they have similar rights, to treat beneficiaries fairly if they have dissimilar rights and not to act capriciously or totally unreasonably.[56]

If there are breaches of fiduciary duties then the trustee may have acted in 'excess' of the exercise of a power (although much depends on the scope of the specific power)[57] and if the trustee acts deliberately by breaching the implied obligation not to exercise that power for an ulterior purpose then this will amount to a 'fraud on a power' and consequently voidable.[58]

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54 John Glover "A challenge to established law on discretionary trust? Re Richstar Enterprises" (2007) 30 Aust Bar Rev 70 at 3 and 10.

55 *Equity and Trusts in New Zealand* above n 24 at [17.1].

56 *Thomas on Powers,* above n 48 at Ch 6(1) p 261 to 333.

57 At [8-02].

58 At [9-01 – 9-02].

Despite its centrality, fiduciary law is a difficult area because there is great uncertainty as to the core underlying principles and the obligations imposed on fiduciaries. It has been said that fiduciary law is "a concept in search of a principle".[59]

Consequently, when there are concerns that a discretionary beneficiary may be in a position to 'control' or 'influence' trustees' decisions then how does equity respond? What are the circumstances surrounding the decision-making process and what is meant by the unanimity rule? When can a trustee obtain a benefit from the trust fund? Can a trustee also be a beneficiary? In what circumstances can the holder of a power of appointment 'hire and fire' trustees?

B Fraud on a Power

Fraud on a power is based on the concept that a trustee cannot exercise a power for an improper purpose. In such situations wrongful appointments are voidable. The law against fraud on a power applies to both dispositive and administrative powers as well as the exercise of a discretion. There has been controversy over whether a power can be exercised to benefit a non-object of the trust.

In *Wong v Burt*[60] and Hammond J summarised the law as follows:[61]

> The particular expression, 'a fraud on a power' rests on the fundamental juristic principle that any form of authority may only be exercised for the purposes conferred, and in accordance with its terms. This principle is one of general application.

And in relation to the central question as to what makes the exercise of a discretion or power 'improper':[62]

> … The central principle is that if the power is exercised with the intention of benefiting some non-object of the discretionary power, whether that person is the person exercising it, or anybody else for that matter, the exercise is void. If on the

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59 *Equity and Trusts* above n 24 at [17.1].

60 *Wong v Burt* [2005] 1 NZLR 91 (CA).

61 At [28] Hammond J.

62 At [30] Hammond J.

> other hand, there is no such improper intention, even although the exercise does in fact benefit a non-object, it is valid.

Therefore as Kenny concludes the test for a fraud on a power "revolves around the power holder's purpose or intention in exercising the power. It must align with the proper purpose of the power; and a fraudulent exercise of a power is totally invalid unless the improper part can be severed."[63]

Another gray area arises when the power holder's purpose is a mixture of both proper and improper purposes. This was the situation in the case of *Kain v Hutton*[64] when the trustees exercised the power of appointment in favour of a beneficiary but on the understanding that the beneficiary would immediately resettle the assets on a new trust for the benefit of herself but also her spouse and children who were not beneficiaries of the original trust.

The Supreme Court found that the trustees had not committed a fraud on the power because the trustee's 'dominant purpose'[65] was to benefit an object of the trust and it did not matter if the power holder had another purpose of benefitting non-beneficiaries as well.

Many modern discretionary trust deeds incorporate wide powers to bring forward the date of distribution of the trust fund and/or resettle the assets of a trust onto a further trust where the beneficiaries may be different. Following a separation a spouse or partner may want to wind up a trust and/or resettle the assets on a class of beneficiaries which do not include the other spouse or partner. Whilst there may be other available remedies for the prejudiced party[66], the test for fraud on a power, illustrates the difficulty that a party faces in relying on the trustees' fiduciary obligations to challenge a disposition of property to a

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63 *Equity and Trusts* above n 24, Jeff Kenny "Requirements for valid exercise of a Trustee's power" at [6.5(4)].

64 *Kain v Hutton* [2008] 3 NZLR 589 (SC).

65 *Equity and Trusts* above n 24 and 63 at [6.5] the author queries whether the majority of judges in *Kain v Hutton* were referring to 'actuating purpose' in line with earlier authorities when they concluded the trustees had not committed a fraud because the trustees 'dominant purpose' was to benefit an object of the trust.

66 See Chapter 6 for remedies under the Property (Relationships) Act 1976, s 44C and Family Proceedings Act 1980 s 182 but only for prejudiced spouses or those in civil unions in certain circumstances.

new trust for the benefit of one party to the qualifying relationships together with different beneficiaries.

C Unanimity

The unanimity rule is expressed in Garrow and Kelly *Law of Trusts and Trustees*[67] as follows:

> All trustees must concur in the exercise of powers conferred on them with reference to the trust estate. Unless the trust document says otherwise, the act of the majority of the trustees cannot bind a dissenting minority or the trust estate. The dissenting minority may of course defer to the judgment of the majority as long as they act in good faith.

In *Rodney Aero Club Inc v Moore* Hammond J observed[68] that the unanimity rule is a corollary of the non-delegation principle so that if trustees cannot delegate, it follows that they must all perform the duties attendant upon execution of the trust.

As a dissenting trustee can defer to the judgment of the majority this can be problematic in a situation where a settlor can 'influence' or persuade another trustee to follow his or her views. In many family trust arrangements the trustees are likely to be appointed from a group of individuals who are known to the settlor and family dynamics are likely to play a significant role in influencing outcomes. A lack of unanimity may become difficult to prove.

Another significant issue with the unanimity rule is the degree of participation required by all trustees particularly when important decisions have to be made regarding the distribution of trust capital and/or income. *Dever v Knobloch*[69] illustrates the difficulties that can arise when a trustee consents by acquiescence and therefore participates in the decision making process but in a limited way. Dobson J took the view that:[70]

> …formal endorsement of the documents following the decision being made by other trustees is not sufficient to meet what is a requirement for substantive participation

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67 Noel Kelly(ed) *Law of Trusts and Trustees* (6th ed, LexisNexis, Wellington, 2005) at [19.3.8].

68 *Rodney Aero Club Inc v Moore* [1998] 2 NZLR 192 at 195.

69 *Dever v Knobloch* HC, Napier, 29 October 2009, CIV-2008-441-000537, Dobson J.

70 At [34].

> by all trustees in what was a fundamentally important decision to distribute the Trust.

Whilst this decision reinforces the importance of actual participation during the decision making process it still leaves open the issue of 'influence' and deference to the wishes of other trustee(s). Further as many small family trusts are poorly administered the trail of records may be few and in many cases non-existent. In summary, equity's response to the rule of unanimity offers a discretionary beneficiary the opportunity to challenge the decision making process but it will only apply to historical decisions and cannot be used to predict a possible lack of unanimity.

D Conflicts of Interest and Self-Dealing

Subject to the terms of the trust deed, a trustee cannot earn unauthorised remuneration and/or obtain a financial benefit from their position as a trustee. This rule of equity is "part of a wider rule that a trustee must not place him or herself in a position where the trustee's duty and interest may conflict".[71]

As Butler notes:[72]

> Not all cases of personal interest however are straightforward. Some will involve fine judgment calls, and will depend on whether there is a preference for the prophylactic approach or a conscience-based approach. In *Jones v AMP Perpetual Trustee Co NZ Ltd* … Thomas J held the view that: "Whether there has been a breach of this underlying principle will, to a large extent be a question of fact and degree. His Honour favoured Lord Upjohn's dissenting view in *Boardman v Phipps* that there must be objectively "a real sensible possibility of conflict" …

The self-dealing rule applies to conduct of trustees only in their capacity as a trustee and prevents trustees from profiting from their position as legal owners of the trust assets. Therefore "if a trustee sells trust property to himself or herself, the sale is voidable by any beneficiary however fair the transaction".[73]

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71 *Law of Trusts and Trustees* above n 67 at 4.13] referring to *Boardman v Phipps* [1966] 3 All ER 721, 756-757, Lord Upjohn.

72 *Equity and Trusts* above n 24 at [17.3.1(2)].

73 *Law of Trusts and Trustees* above n 67 at [4.13].

However, the self-dealing rule does not apply to decisions on distributions to beneficiaries of trust assets. Further a trustee who is also a beneficiary can benefit from the trust[74] because the Privy Council has made it clear that a person can be both a trustee and beneficiary.[75] Consequently a trustee "who is also a beneficiary can exercise his or her discretion as a trustee to benefit him or herself, and equity does not intervene in such cases".[76]

This then raises the question as to whether a trustee's decision to benefit himself or herself as a beneficiary can be held to be unreasonable. As Dobson J held in *Dever v Knobloch*:[77]

> … On the approach in *Craddock v Crowhen*[78], the test to establish unreasonableness against trustees is a high one, namely whether the decision was one that no reasonable trustees, properly advised, could possibly have come to.

As can be seen equity's response to claims of conflicts of interest and self-dealing are limited and do not apply in all circumstances where a trustee is also a discretionary beneficiary.

E Power to Add and Remove Beneficiaries

Most modern discretionary trust deeds include a power to add or remove beneficiaries. In the context of a separation this is a powerful tool and can be used to remove the former spouse or partner and later add a new spouse or partner and his or her children. This can be particularly unfair when the trust fund is largely derived from relationship property of the first qualifying relationship.

Whilst trustees owe fiduciary duties when exercising their power to add or remove beneficiaries they are "not required to exercise this power impartially as between classes

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74 *Law of Trusts and Trustees* above n 67 at [4.14.1].

75 *Commissioner for Stamp Duties of the State of New South Wales v Perpetual Trustee Co Ltd* [1943] AC 425 referred to *Law of Trusts and Trustees* above no 67 at [4.14.1].

76 *Sargeant v National Westminster Bank* (1990) 61 P&CR 518. referred to in *Law of Trusts and Trustees* above n 67 at [4.14.1]

77 *Dever v Knobloch* above n 69 at [64].

78 *Craddock v Corwhen* (1995) 1 NZSC 40,331.

of beneficiaries, nor do they have to act in the best interests of all the beneficiaries."[79] If the facts support a breach of fiduciary obligations then the court can intervene if the trustees have acted improperly[80] or capriciously. Capricious conduct has been defined as "acting for reasons that could be said to be irrational, perverse or irrelevant to any sensible expectation of the settlor."[81]

If a settlor reserves this power and is not a trustee then there is no fiduciary obligation and the settlor can remove or add the beneficiary without giving reasons.

Again, whilst it may be possible for a former spouse or de facto partner to challenge the trustees' decision to add or remove beneficiaries the evidential threshold is high and depends upon who holds the power to add and remove beneficiaries.

F Power of Appointment: The Power to Hire and Fire Trustees

Most discretionary trust deeds provide for a nominated power holder to have the authority to remove and replace trustees, that person may ultimately have the ability to 'control' the decision making of the trustees by being able to appoint sympathetic trustees and remove those who are unwilling to support a power holder's views on the exercise of both administrative and dispositive powers.

The power to appoint and remove trustees is a limited power under a trust deed but must be exercised honestly and without ulterior motives. In the classic text of *Farwell on Powers*[82] the author puts the principle this way:

> A person having a limited power must exercise it bona fide for the end designed; otherwise the execution is corrupt and void.

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79 *Hills v Public Trust* HC Auckland CIV-2008-404-2217, 15 March 2010 at [152].referred to in "Relationship Property and Trusts" above n 46 at p 6

80 *Wong v Burt* above n 60 for the meaning of 'improper'.

81 "Relationship Property and Trusts" above n 46 at p 5.

82 George Farwell *Farwell on Powers* 3 ed (Stevens & Sons Ltd, London, 1916) at p 457.

In many modern discretionary trust deeds it is not uncommon for the settlor to be the power holder and may not need to give reasons for the removal and replacement of trustees. The orthodox view is that a donee of such a power cannot appoint him or herself as a trustee. In *Re Skeats' Settlement* Kay J held that a donee's decision to appoint himself was invalid because the power was fiduciary in character:[83]

> The universal rule is that a man should not be judge in his own cause: that he should not decide that he is the best possible person, and say that he ought to be the trustee … to appoint himself among other people, or excluding them to appoint himself would certainly be an improper exercise of any power of selection of a fiduciary character such as this is. In my opinion it would be extremely improper for a person who has a power to appoint or select new trustees to appoint or select himself.

Yet, many discretionary trust deeds permit the power holder to appoint themselves as trustees and the Trustee Act 1956 provides "that express powers of appointment contained in the trust instrument take precedence over the statutory powers contained in the Act".[84]

This issue is of particular interest in family law because the power holder's ability to exercise this power to 'hire and fire' trustees and appoint him or herself as a trustee has led some judges and commentators to suggest that it is likely the donee will use this power to their advantage. Consequently the proposition in *Re Skeats Settlement* that equity would hold such an appointment as invalid has not been accepted.

Certainly this is the position in Australia, *In the Marriage of Goodwin*[85] the Family Court of Australia approved an earlier decision of *In the Marriage of Reynolds* when the Court said:[86]

> We do not find the decisions in *Re Skeats Settlement* (supra) and *Re Crawshay (Dec'd)* (supra) of any real assistance. These cases were dealing with trusts and powers of appointment of a completely different nature and were decided in circumstances which bear no resemblance to the present proceedings. In particular the power of appointment in the present case is not a fiduciary power but a power

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83 *Re Skeats' Settlement* (1889) 42 Ch D 522 at 524.

84 *Law of Trusts* above n 23 at [4.37] referring to Trustee Act 1956, s 2 and s 43(1).

85 *In the Marriage of Goodwin* (1990) 101 FLR 386.

86 *In the Marriage of Reynolds* (unreported, Family Court, Full Court, 27 April 1990) at p 391.

> which by the terms of the deed the husband may exercise for the purposes of controlling the trust for his own benefit if he so chooses.

Another family property case where the Courts were not convinced that the rule in *Re: Skeats* still applied is the United Kingdom Court of Appeal judgment of *Charman v Charman.*[87] This case concerned a non-resident trust. The wife claimed that the husband had an interest in that trust fund which should be considered his 'financial resource'[88] and that interest should form part of the pool of matrimonial property. The husband had a power of removal of trustees and the argument for the wife was that he could use that power to replace a trustee who declined his request for a distribution from the trust fund.

The husband relied on the rule in *Re: Skeats' Settlement* and argued that his ability to remove trustees was a fiduciary power and he could not lawfully remove a trustee because he refused to accede to his request. The husband's argument was raised on the first day of the appeal and the Court held:[89]

> There is no need for us to decide this *peripheral* issue. It has arisen very late and has not been fully argued on either side. We consider that exploration of the difficult interface between the likely exercise of powers in the real world and what must for the court be the dominant requirements of the law is better left to another occasion.

Apart from Australia (which is discussed in Chapter 4), the interface between what is likely to happen and equity's response to breaches of fiduciary obligations has not been fully argued.

Critics who reject the concept that a power holder can 'control' the trust focus on two principal reasons: firstly, wrongful appointments can be restrained by the court and secondly, a power to dismiss trustees does not entail control of the trustees' decision making until the power has been exercised. In other words likely conduct is not a ground for supporting a suspicion that the power holder will exercise 'control' by misusing the power to 'hire and fire' trustees.

This is one of the fundamental dilemmas between the approach taken in family law where social realism is the benchmark and Family Courts are used to making predictive

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87 *Charman v Charman* [2007] 2 FCR 217 (CA) Sir Mark Potter P.

88 Matrimonial Causes Act 1973, s 25(2)(a).

89 Ibid n 87 at [55(f)] (the writer's emphasis).

judgments regarding future events (particularly in the area of income maintenance, economic disparity claims and in some valuation exercises). There is no such approach in equity where "equity follows the law" and until a breach of fiduciary obligations can be established, on the balance of probabilities, what may or may not happen in the future is largely irrelevant.

It is useful at this point to pause and consider the circumstances when the courts can appoint new trustees "either under the inherent jurisdiction derived from its general supervisory jurisdiction over trusts or under the specific provisions of s 51 Trustee Act 1956".[90]

In *Mendelssohn v Centrepoint Community Growth Trust*[91] Tipping J "held that the Court's task in appointing a trustee under s 51 is to appoint the person or persons best suited to administer the trust in the circumstances prevailing."[92] The Court of Appeal were guided by the principles described in *Re: Tempest*[93] and "have regard to the settlor's intentions; neutrality between beneficiaries and promotion of the purposes of the trust." With regards to the settlor's intentions Tipping J stated:[94]

> If … it can be seen that either expressly or implicitly the author intended the trustees to be of a certain description, the Court will give considerable weight to that expression of the author's wishes. But … the Court is not bound by those wishes and is entitled to depart from them if good cause is shown. Here it was. The second point is that trustees must be neutral and even-handed as between beneficiaries with different interests.

Whilst the High Court does have the ability to supervise the exercise of the donee's power to 'hire and fire' trustees it does not mean that in that process the court will review appointments based on a suspicion of likely abuse of fiduciary obligations.

G Conclusion

As can be seen equity's response to wide dispositive powers in the hands of a trustee/beneficiary is a mixed bag. On the one hand strict adherence to fiduciary

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90 *Equity and Trusts* above n 24 at [5.2.3(4)].

91 *Mendelssohn v Centrepoint Community Growth Trust* [1999] 2 NZLR 88 (CA).

92 *Law of Trusts* above n 23 at [4.37.1].

93 *Re Tempest* (1866) LR 1 Ch App 485.

94 *Law of Trusts* above n 23 at [4.37.1].

obligations is a means of ensuring that trustees do not exploit their position of trust but case authorities are not straightforward, impose tests with difficult thresholds and require a fine balancing of facts on a case by case basis. In family situations there is a strong likelihood that the enforcement of fiduciary obligations will slip below the radar as both legal cost and judicial uncertainty make adherence to obligations difficult to enforce.

Consequently, there in an uncomfortable relationship between the principles and purposes of the PRA and the equitable principles which protect trustees’ powers and obligations. For reasons that will emerge in the next chapter, in Australia, the judiciary have been largely unimpressed with justifications to protect discretionary trusts from spousal claims by relying on the laws of powers and fiduciary obligations.

IV Australia – The Meaning of Property and the Discretionary Trust

A Introduction

This chapter explores the meaning of 'property' within the Australian Family Law Act 1975 ("FLA"). The reason that Australian case law is of particular interest arises out of the recent High Court of Australia's decision in *Kennon v Spry*[95] which has opened the door to not only a wide interpretation of the meaning of property but has also peeled back the protections afforded to discretionary trust assets in family law claims.

It has been suggested that it is inappropriate to rely on the Australian definition of property as a guide to interpret the meaning of 'property' and 'owner' under the Property (Relationships) Act 1976.[96] Whilst it is accepted that there are many differences between the property sharing schemes in each country, there is one common theme: jurisdiction in both statutes is only invoked when there is property to be distributed between the parties.

In both countries the definition of property is broadly stated and is silent on whether interests in discretionary trusts are or can be given property status. In the absence of any legislative guidance judges have wrestled with orthodox trust law principles in the context of family law legislation. In both countries similar questions have been asked: Does a spouse who has 'control' of a discretionary trust have a property interest in the assets of the trust? Can discretionary interests be proprietary interests? Should orthodox principles prevail and have presumptive power over the claims of those in qualifying relationships?

For the reasons set out in this chapter, Australian judges have preferred to expand the meaning of property at the expense of conventional trust principles. The way that property interests in trusts has developed in Australia is instructive for two reasons: firstly the recent New Zealand development of the concept of a 'bundle of rights' in family trust cases has an uncanny resemblance to the Australian concept of the *alter ego* trust. Secondly, the development of the *alter ego* trust illustrates Underkuffler's proposition

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95 *Kennon v Spry* (2008) 251 ALR 257 (HCA).

96 *Equity and Trusts* above n 24 Ch 41, Nicola Peart "Equity and the Property (Relationships) Act 1976" at [41.2.2] ["Equity and the PRA"].

that property rights evolve as a consequence of conflicting and changing social attitudes over time.[97]

Before commencing this discussion it is important to reflect on the features of the PRA[98] which differ from the FLA.[99] The most significant difference lies in the scheme of property entitlements. For the reasons explained in chapter 2 the PRA is a deferred property sharing scheme.[100] During the period of cohabitation the parties are free to deal with their property[101] but upon separation, death or an application to the Family Court the property of the parties is classified into relationship[102] or separate property[103] and then divided on the assumption that there should be an equal division[104] of all relationship property. Timing issues are significant not only because they affect the property available for division but also the date of valuation of those assets.[105]

In Australia, the starting point for matrimonial property law is the "ordinary rules of law and equity relating to real and personal property" despite the intervention of the FLA.[106] However, the FLA revised the ordinary rules in respect to the property of the parties in two significant ways: firstly, it brings all property disputes between spouses within the jurisdiction of the Family Court and secondly, it enables the court to "alter the property interests" of the parties at any time during their joint lives.[107]

The FLA gives courts wide discretionary powers to alter the parties' property interests to achieve a result that is just and equitable. Although the discretion is wide it "is not at

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97 See chapter 2 above n 17.

98 Property (Relationships) Act 1976 ("the PRA").

99 Family Law Act 1975 ("FLA") This statutory regime is confined to parties to a marriage whereas the Property (Relationships) Act extends to de facto relationships as well as parties to a civil union.

100 Robert Fisher QC *"Fisher on Matrimonial and Relationship Property"* (online looseleaf ed, LexisNexis) at [1.2] [Fisher on Relationship Property].

101 Property (Relationships) Act 1976 s 19(a).

102 Property (Relationships) Act 1976 s 8.

103 Property (Relationships) Act 1976 s 9 -10.

104 Property (Relationships) Act 1976 s 11.

105 Property (Relationships) Act 1976 s 2F.

106 Anthony Dickey *Family Law* (The Law Book Company Ltd, Sydney, 1985) at Ch 20 *Introduction to Matrimonial Property* at [2(1)] on p 474.

107 At [2(1)] at p 492.

large: s 79(4) sets out the factors to be taken into account in property distribution"[108] which include past financial and non-financial contributions together with future means and needs. Consequently, the FLA does not classify assets nor does it presume that there is to be an equal division of the value of assets between the parties. Timing and valuation issues remain relevant but do not assume the same importance as under the PRA.

In terms of procedural matters, the PRA provides safeguards against the disposition of property to third parties by enabling a spouse or a partner to register a claim against the title to land under the Land Transfer Act.[109] The Family Court can also restrain the disposition of assets to a third party, if its purpose is to defeat the rights or claims of a spouse or partner[110] and can set aside a disposition if it has been made "in order to defeat the claim or rights of any party"[111] otherwise in good faith and/or for valuable or adequate consideration. Whilst the Family Court does have the power to make ancillary orders "varying the terms of a trust or settlement,"[112] and provide compensation for relationship property disposed of into a trust[113] these provisions have provided only limited relief for a dispossessed party for the reasons discussed in chapter 6.

By contrast the FLA enables a court to grant an injunction in proceedings "in relation to the property of a party to the marriage"[114] and again this provision has been given a wide interpretation. Essentially, there are two requirements for an injunction; that there is an existing or potential claim to an order altering property interests and a danger that the claim may be defeated or prejudiced unless such an injunction is granted.[115] The court can also grant an injunction against a third party.[116] There is also power to restrain and set aside dispositions which may defeat an existing or anticipated order in the proceedings "irrespective of intention."[117] The court can also make an order altering the property interests of the party which is binding on a third party provided the third party

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108 HA Finlay, RJ Bailey-Harris, MFA Otlowski *Family Law in Australia* (5th ed, Butterworths, Australia, 1997) Ch 6 Property Division at [6.26].

109 Property (Relationships) Act 1976 s 42.

110 Property (Relationships) Act 1976 s 43.

111 Property (Relationships) Act 1976 s 44.

112 Property (Relationships) Act 1976 s 33(1)(m).

113 Property (Relationships) Act 1976 s 44C.

114 Family Law Act 1975 s 114(1)(e).

115 Richard Chisholm (ed) *Australian Family Law* (loose leafed, LexisNexis Butterworths Australia) at [114.24].

116 Family Law Act 1975, s 90AA.

117 Family Law Act 1975 s 106B.

has been accorded 'procedural fairness' and the court is satisfied that the order is 'just and equitable.'[118] Finally, there is power to appoint a person to "do all acts and things necessary to give validity and operation to the deed or instrument."[119] In summary the FLA provides a more robust structure to claw back third party assets into the property pool, provide injunctive relief as well as make orders that are binding upon third parties.

B The Meaning of 'Property' in Australia

The starting point is to consider the statutory definition of the word 'property' under the FLA.

Property is defined in s 4(1)(a) as:[120]

> (a) property to which those parties are, or that party is, as the case may be, entitled whether in possession or reversion

Section 79 provides:[121]

> (1) In property settlement proceedings, the court may make such orders as it considers appropriate:
>
> (a) in the case of proceedings with respect to the property of the parties to the marriage or either of them – altering the interests of the parties to the marriage in the property; …

Section 79 then requires the court to take a four step approach to:[122]

> (a) assess the extent of the property of the parties and determine its value;
>
> (b) consider what contributions have been made by the parties, including direct and indirect contributions of a financial character and non-financial character,

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118 Family Law Act 1975 s 90AE.

119 Family Law Act 1975 s 106A.

120 Family Law Act 1975 s 4(1)(a).

121 Family Law Act 1975 s 79(1)(a).

122 *Australian Family Law* above n 115 "General Principles in Exercising Discretion under s 79: Four step approach" at [79.151].

> and contributions to the welfare of the family, including contributions as home-maker and parent;
>
> (c) consider the circumstances which relate to the present and future needs of the parties and to their means, resources and earning capacity, actual and potential;
>
> (d) consider the effect of the above findings and resolve what order is just and equitable in all the circumstances of the particular case.

Section 79 distinguishes between three sources of wealth; being income, property and financial resources and each may be considered in deciding the manner in which the property of parties should be divided but the Court can only make orders in respect of the property of one or both spouses.[123]

The courts have a broad discretion to reallocate property as a result of two factors:[124]

> (1) the jurisdiction extends to all of the property of the husband and wife, whenever acquired; and (2) there is an absence of legislative guidance regarding how s 79 should be interpreted and applied …

The Court's ability to consider all property of either spouse has raised important questions regarding the boundaries of the marriage partnership, particularly the extent to which the duration of the marriage is relevant and the property over which the marriage partnership extends. Consequently, judges are often divided over whether to take a partnership or individualistic approach to the pool of property available for division. A partnership approach is more likely to result in all the parties' property being available for division whereas the individualistic approach focuses on the link between the marriage and particular assets in question.[125]

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123 Stephen Parker, Patrick Parkinson, Juliet Behrens *Australian Family Law in Context* (The Law Book Company Limited, Australia, 1994) at p 597. [*"Australian Family Law in Context"*].

124 Belinda Fehlberg & Juliet Behrens *Australian Family Law: The Contemporary Context* (Oxford University Press Victoria, Australia, 2008) [*The Contemporary Context"*] at p 468 and quoting from Patrick Parkinson "Quantifying the Homemaker Contribution in Family Property Law" (2003) 31 Federal Law Review 1, 5.

125 At p 468.

Further as s 79 gives the Courts a broad discretion which allows for outcomes to reflect the facts of each case but is also affected by individual judicial values. These tendencies have been enhanced by the High Court of Australia's insistence that the Court's discretion should not be fettered by formulaic approaches. As one commentator has noted:[126]

> … [t]he effect of this is that the discretion of trial judges, broad enough by the terms of the legislation is effectively even broader because of the Full Court's inability to create firm rules control the exercise of that discretion

This legislative and judicial background is also reflected in the expansive way that the courts have applied the definition of property to the assets of the parties. The meaning of property has been given a very broad construction under the FLA. The starting point is illustrated in one of the earliest FLA cases *In the Marriage of Duff*[127] when the Full Court supported the definition of 'property' found in an old English case of *Jones v Skinner*[128] that "Property is the most comprehensive of all terms which can be used inasmuch as it is indicative and descriptive of every possible interest which the party can have".

This broad definition of 'property' extends to real and personal, corporeal and incorporeal property and the words "whether in possession or reversion" have been interpreted as words of extension and not limitation.[129] Yet, as Justin Gleeson SC[130] commented the terminology of 'possession or reversion' "… invokes notions of strict property law" found in statutes from the nineteenth century such as the Matrimonial Causes Act 1857 (UK) rather than looser and broader conceptions which have developed in Australia."

Whilst the definition of property does not extend to mere personal rights[131] (such as the right to occupy the family home) nor a mere hope or expectation of acquiring an interest

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126 At p 468, quoting from Richard Ingleby "Introduction: Lampert and Lampposts: The End of Equality in Anglo-Australian Matrimonial Property Law?" (2005) 19 International Journal of Law, Policy and the Family 137 at 146.

127 *In the Marriage of Duff* [1977] FLC 90-217, 76-133.

128 *Jones v Skinner* (1835) 5 LJ Ch 90.

129 *Australian Family Law* above n 115 at [79.69].

130 Justin Gleeson SC "Spry's case: Exploring the limits of discretionary trusts" (2010) 84 ALJ 177 at 184 ["Spry's case"].

131 *Mullane v Mullane* (1983) 45 ALR 291.

or receiving a benefit such as a discretionary payment under a trust, it can include future contingent interests.[132]

As the statutory definition of property refers to 'entitlement' the Courts have considered whether or not property has to be alienable. *In the Marriage of Best* the Full Court considered a case where the husband was a partner in a large law firm. The couple had few assets so the husband's interest in his legal practice took on special significance. The Court held that the husband's interest was property despite the fact that the Partnership Deed contained limitations on the ability of partners to assign their interests[133]. The Court held that:[134]

> [i]nalienability does not deprive an interest of the characteristic of property except where it is an inherent characteristic of the right that it is both personal and unassignable and hence not proprietary in character, the most common example of which is a personal right to sue for damages.

The court went on to explain[135] that disincentives or practical difficulties associated with alienation did not prevent the interest from constituting property. Nevertheless the practical difficulty is that the court could not assign the husband's interest in his law practice and therefore the husband retained his partnership interest, was ordered to pay substantial spousal maintenance (together with his child support obligations) and the wife retained the balance of property.

As commentators have noted[136], the outcome of this case made it unnecessary for the Court to decide if the partnership interest was property. For all practical purposes the interest could have been treated as a 'financial resource' of the husband but for reasons that are explored further in this chapter it will be seen that there is a significant advantage to the non-owner spouse if a right or interest is defined as 'property' rather than a 'financial resource'.

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132 *Australian Family Law* above n 115 at [79.69].

133 *The Contemporary Context* above n 124 at p 471.

134 *In the Marriage of Best* (1993) 16 Fam LR 937 at 952.

135 At 954.

136 *The Contemporary Context* above n 124 at p 471.

In the recent High Court of Australia decision of *Kennon v Spry*[137] Gummow and Hayne JJ considered standard forms of statutory interpretation within FLA and also cases where a 'right' may not ordinarily be considered as 'property' and they held:[138]

> The phrase … 'with respect to the property of the parties to the marriage or either of them' should be read in a fashion which advances rather than constrains the subject, scope and purpose of the legislation. In particular, as statements by this court illustrate the term 'property' is not a term of art with one specific and precise meaning. It is always necessary to pay close attention to any statutory context in which the term is used. In particular it is, of course, necessary to have regard to the subject-matter, scope and purpose of the relevant statute.
>
> The questions that arise in these matters raise a dispute about the construction of the Act. That dispute is not resolved by considering only the ways in which the term property may be used in relation to trusts of the kinds described as 'discretionary trusts'. As Binnie J, writing for the Supreme Court of Canada, has recently said (albeit in a different statutory context):[139]
>
> > [16] … The task is to interpret [the relevant statutes] in a purposeful way having regard "to their entire context, in their grammatical and ordinary sense harmoniously with the scheme of the Act, the object of the Act, and the intention of Parliament.
>
> And … because an interest (in that case, a fishing quota):
>
> > [16] … may not qualify as 'property' for the general purposes of the common law does not mean that it is also excluded from the reach of the statutes. For particular purposes Parliament can and does create its own lexicon.

To summarise, the current position in Australia is that the definition of 'property' is interpreted in a purposeful way having regard to the FLA and the factual context of each case. If an interest does not gain a property status at common law or in another statutory setting that does not mean that it does not qualify as property under the FLA.

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137 *Kennon v Spry* (2008) 251 ALR 257 ("Spry").

138 At [89-90] per Gummow and Hayne JJ.

139 *Saulnier v Royal Bank of Canada* 2008 SCC 58 at [16].

C 'Property' or 'Financial Resource'?

For the reasons already touched on there is an important distinction between the definition of property and a financial resource under the FLA. The term financial resource is not defined in the FLA but case authority has developed definitions which include: [140]

> a financial stock or reserve over which a party has sufficient control as a matter of fact to draw upon when necessary towards supplying some financial want or deficiency of the party

And: [141]

> The term "financial resource" must add something not covered by the term "income and property". For example, a contingent interest or benefits which a party actually receives or is likely to receive, whether legally entitled thereto or not …

The Court has no jurisdiction to make orders redistributing a party's financial resources. Section 4(1) requires that only property to which a spouse 'is entitled' can be the subject of an order. This involves establishing that a spouse has legal control over the asset in question.[142]

There is considerable significance between defining an asset as 'property' as opposed to a spouse's interest in a 'financial resource'. As the authors of *Australia Family Law*[143] note the benefit of treating an asset as 'property' is that the non-owner's contribution to that asset will be considered at the second step in the division of assets. At this stage the Court considers the parties' contributions (both financial and non-financial) and where the Court's adopt the 'partnership approach' the financial award for a non-owning spouse is likely to be significant. However, when the Court considers a 'financial resource' at the third step (often referred to as the 'offsetting' stage) of the reallocation of property interests and historically those awards are less generous.

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140 *Australian Family Law* above n 115 at [75.9] also referring to *In the Marriage of Kelly (No 2)* (1981) 7 Fam LR 762.

141 At [75.9].

142 *The Contemporary Context* above n 124 at p 472.

143 At p 470-471.

A finding that a spouse's interest is a 'financial resource' may be of little benefit to a non-owner spouse if the property pool available for division is small or non-existent because there may be insufficient property to offset a 'financial resource' award. This distinction between property and a financial resource is similar to the position in New Zealand when the Family Court is asked to make a compensatory payment for the disposition of relationship property to a discretionary trust.[144] The Court can be met with a similar difficulty if there is little or no property (either relationship or separate property) to pay compensation.

As will be seen, in the context of discretionary trusts, these practical implications have been influential in expanding the category of interests that are given property status and some of the earlier 'financial resource' case authorities have become redundant.

D Control and the Alter Ego Trust

In Australia, like New Zealand, the use of discretionary trusts is widespread and as Peter Nygh and Andrea Cotter-Moroz observe[145] the usual purpose of the modern discretionary trust is to create the illusion of separate ownership but nevertheless to retain real control over the disposition of trust assets even though it is the essence of a trust that the person who holds the office of trustee or appointor does not have any right of property in the assets of the trust.

The characteristics of control and illusion of separate ownership has been highly influential in the development of the meaning of property under the FLA. In the case of *Ascot Investments Pty Ltd v Harper*[146] the Full Court had to consider the type of orders which could be made against a company in circumstances where the evidence established that husband controlled the company. Gibbs J held:[147]

> The position is, I think, different if the alleged rights, powers or privileges of the third party are only a sham and have been brought into being, in appearance rather than reality, as a device to assist one party to evade his or her obligations under the Act. Sham transactions may always be disregarded. Similarly, if a company is

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144 Property (Relationships) Act 1976, s 44C.

145 Peter Nygh and Andrea Cotter-Moroz "The Law of Trusts in the Family Court" (1992) 6 Australian Journal of Family Law 4, 6 – 7 ["*The Law of Trusts in the Family Court*"].

146 *Ascot Investments Pty Ltd v Harper* (1981) 148 CLR 337; 33 ALR 631 ("Ascot").

147 At p 644 per Gibbs J.

> completely controlled by one party to a marriage so that in reality an order against the company is an order against the party, the fact that in form the order appears to affect the rights of the company may not necessarily invalidate it.

Following *Ascot* the concepts of third party interests being 'mere puppets' or the *alter ego* of the controlling spouse were more fully developed in the case of *In the Marriage of Ashton*[148] where the husband was the appointor and he appointed another trustee company in which he and his cousin were sole directors and shareholders (the cousin holding his share on trust for the husband). Whilst, the husband was not a beneficiary of the trust he handled the trust assets as if they were his own, dealing with trust property and income as he liked and for his benefit. Unsurprisingly, the court concluded that the trust was no more than the husband's *alter ego* and went on to say "the powers which the husband had in the Ashton family trust settlement gave him control of the trust either as a trustee or through a trustee which is his creature."[149] In those circumstances the husband had both de facto legal and beneficial ownership of the trust's assets.

Ashton's case was factually uncontroversial because the husband admitted treating the trust assets as if they were his own property. However, later cases raised more complex issues including: whether a trustee/spouse ability to make a self distribution of trust assets means that this is likely to happen; whether spouse/appointor's ability to appoint a compliant trustee is conclusive of finding that the appointor has 'control' of the discretionary trust; whether a trustee's ability to 'influence' another or other trustees is 'control' and finally whether a spouse who is a beneficiary, trustee and holds a power of appointment has de facto ownership of trust property.

Slowly, Australian case authority moved to a position where the courts were primarily concerned with the trust deed and what it enabled a spouse to do rather than what may or may not have happened during the marriage. This shift in judicial thinking increasingly opened the door for the courts to scrutinize discretionary trust structures in family property proceedings.

In the Marriage of Davidson[150] the husband was appointor and also had controlling interests in a company which was the trustee of the MAVK Trust. Like *Ashton* the Judge described the trust as 'the creature of the husband'. Whilst the husband conceded that he

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148 *In the Marriage of Ashton* (1986) 11 Fam LR 457 ("Ashton's case").

149 At p 462.

150 *In the Marriage of Davidson [No.2]* (1990) 101 FLR 373 ("Davidson").

could divert income and assets of the trust for his own purposes it was argued that such manipulation of the trust would amount to a breach of fiduciary duty. However the Court found:[151]

> Whatever may have been the position one hundred years ago; Australian courts today have to look at the reality of the situation and the purpose which family trusts serve today. A limitation as to the husband's power to control the assets and income of the trust in accordance with the provisions of the trust deed is inconsistent with the reasoning of the Full Court in *Ashton* …

In all these cases counsel made strenuous submissions that the Court was not at liberty to depart from trust principles that protected trust assets from third party claims. However, in the context of the FLA, the Courts showed little deference to orthodox trust and equitable principles. As Nygh and Cotter-Moxon observe[152] "[i]t is these trust devices, rather than any decision of the Full Court which has departed from the traditional law of trusts" and they then go on to explain:[153]

> As long as the object of the trust, upon proper construction of the trust deed and in light of the factual circumstances of the case, is advanced and not defeated by the orders of the court, such orders cannot be said to ignore the traditional law of trusts. Therefore where the object of the trust, as appearing from the trust deed, is to put a party into a position of complete and unfettered control just as if they were the owner of the trust property, an order of the Family Court effecting this reality is a result permitted by the trust deed itself. Therefore, such an order is not inconsistent with the traditional law of trusts.

This analysis is not without its critics because as many trust lawyers point out a discretionary trust presupposes that it is left to the trustee to decide how the relevant income or capital will be distributed and concepts such as unfettered control ignore the trust relationship.

Another major criticism is that the distinction between 'property' and a 'power' has been blurred to the point that the dictum in *Re Armstrong*[154] has been overruled and the power of a person to appoint "an estate to himself" is deemed to be a property interest.

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151 At p382.

152 "The Law of Trusts in the Family Court" above n 145 at p 16.

153 At p 18.

154 *Re Armstrong* (1886) 17 QBD 521 and see the discussions in chapter 2.

Despite these criticisms, these decisions do not mean that the trust structure is irrelevant or to be treated as a sham in family law but they do show that notions of justice and common sense will prevail over the legal formalism inherent in earlier decisions[155]. The courts will not permit a party to shelter assets behind a legal framework or allow one spouse to gain a financial advantage out of wealth that has accumulated during the course of that marriage.

Until 2007, there was little direct judicial consideration of the rule in *Gartside*[156] (that a discretionary interest cannot be a proprietary interest) and where it sat in relation to a growing body of case authority built around the concept of spousal control of a discretionary trust. However, in *Re Richstar Enterprises Pty Ltd: ASIC v Carey (No 6)*[157] (a tax case) the Federal Court observed that in the ordinary case the rule in *Gartside* applies but French J then said:[158]

> I distinguish the 'ordinary case' from the case in which the beneficiary effectively controls the trustee's power of selection … there is something which is akin to a proprietary interest in the beneficiary.

A proprietary inference can be drawn from effective control of a discretionary trust as follows:[159]

> the beneficiary who effectively controls the trustee's power of selection because he is the trustee or one of them and/or has power to appoint a new trustee has something approaching a general power and the ownership of the trust property.

Since *Richstar,* judges in other Australian jurisdictions have not universally accepted that orthodox principles of trust law can be discarded on the grounds of 'control'. The counter-view is explained in a recent Supreme Court of New South Wales case where White J in *Public Trustee v Smith*[160] considered the proposition that control of a trust gave a discretionary beneficiary a beneficial interest in the assets of the trust. He rejected

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155 "The Law of Trusts in the Family Court" above n 145 at 21.

156 *Gartside v IRC* [1968] AC 533.

157 *Re Richstar Enterprises Pty Ltd: ASIC v Carey (No 6)* (2006) 153 FCR 509 ("Richstar").

158 At [29].

159 At [37].

160 *Public Trustee v Smith* [2008] NSWSC 397.

that proposition on the basis that this "would mean that she was the beneficial owner of the trust property *prior to causing the trustee to appoint the property to herself*".[161]

E Kennon v Spry[162]

If there was any doubt that control of trustees could create a beneficial interest then it was settled by the High Court of Australia in *Spry's* case. The facts in *Spry* need to be fully explained in order to understand how the expansion of the meaning of property has eroded orthodox trust principles. Dr Spry settled a trust by parol in 1968. He prepared a trust instrument but did not execute it because of stamp duty. He married in 1978. The trust deed was signed and stamped in 1981. Dr Spry was settlor, trustee and a beneficiary. He had power to appoint and remove any other person as an additional trustee. He also had a power to vary the terms of trust provided that the variation did not increase his rights to the beneficial enjoyment of the trust fund. The beneficiaries included his wife and subsequently born children. He could apply any part of the income and capital to any of the beneficiaries. At the date of distribution the fund was to be divided amongst such beneficiaries as the trustee felt fit and in default equally amongst all male beneficiaries. Dr Spry as trustee had a power to invest or deal in the fund as if it was his own absolute property. In effect he had complete control of the trust.

In 1983 Dr Spry appointed his wife to be the trustee on his death or resignation, provided the appointment was revocable by him at any time. Dr Spry then abandoned all beneficial interests or rights which he might have as settlor and confirmed that by removing himself as a beneficiary.

When the marriage was in trouble in 1998, he revoked the appointment of his wife as the successor to him as trustee and instead appointed his two eldest daughters jointly. The terms of the trust were varied so that both Dr Spry and his wife were irrevocably excluded from receiving any part of the capital of the trust. This was unnecessary for Dr Spry if the 1983 Deed remained effective. Dr Spry's explanation in Court was that he had forgotten about the 1983 Deed.

In October 2001 the parties separated. In January 2002 Dr Spry established 4 separate trusts for each of his daughters by applying both capital and income from the original

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161 At [108] per White J (my emphasis).

162 *Kennon v Spry* (2008) 251 ALR 257 (*"Spry's case"*).

trust. He was the trustee of each of his children's trusts. The beneficiaries included the daughter as primary beneficiary plus the daughter's children, grandchildren, sisters, nephews, nieces and their spouses. Dr Spry had a power to apply all or any part of the income or capital for the benefit of any of the beneficiaries. Dr Spry was excluded absolutely from any interest in the fund.[163] The marriage was dissolved prior to the substantive property hearing.

In the Family Court the wife filed for property orders under s 79 and the trial judge included the assets of the daughters' trusts as part of the property pool. In order to include the trusts' assets the 1998 and 2002 instruments had to be set aside and once that had occurred there were two pathways to the approach that the trusts' assets were to be included as part of the marital property pool. Either, Dr Spry could reverse the 1983 deed and thereby reinstate himself as a beneficiary and then be able to distribute the whole of the assets of the trust to himself. Or, as Dr Spry had sufficient control over the assets of the trust and their distribution the assets should be regarded as his. The second approach was adopted by the trial judge who relied on earlier case authority described in this paper.

On appeal the Full Family Court by a majority agreed with the first approach, namely that it was open to Dr Spry to rescind the 1983 instrument and thereby reinstate himself as a beneficiary and if necessary with the consent of the wife. The majority did not approve the second approach because although Dr Spry had control over the assets of the trust through his ability to appoint/remove trustees he did not have an ability to benefit from distributions of income or capital and in those circumstances the Court was not prepared to accept that he had sufficient 'control'. Finn J, dissenting, took the orthodox approach and would have allowed the appeal in Dr Spry's favour.

Then Dr Spry appealed to the High Court on the basis that Finn J's dissent judgment in the Full Court was correct as it was not open to Dr Spry to reinstate, whether by agreement with the wife or otherwise, his position as a beneficiary. The assets of the trust post 1983 could never be considered to be his property.

The High Court concluded that whilst the 1983 deed remained in force, Dr Spry could not be considered as a beneficiary of the Trust and he could not apply its assets in his own favour. Therefore the assets in the Trust were not the property of the husband. Heydon J agreed. Keifel J[164] was more explicit in her agreement with Finn J but French CJ

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163 "Spry's case: Exploring the limits of discretionary trusts" above n 130 at p 177-178.

164 *Spry* above n 162 at [196] Keifel J.

expressly left open the correctness of the approach to reinstatement of Dr Spry as a beneficiary. Therefore four of the five judges held that, whilst the 1983 deed remained in effect, Dr Spry was not a beneficiary and the assets of the Trust could not be treated as property of him being one of the parties to the marriage.

Nevertheless the wife succeeded on the appeal and the reasoning of the High Court majority of French CJ, Gummow and Hayne JJ illustrates the way that the meaning of 'property' has been developed in the context of a discretionary trust. The majority took different approaches to the 'property' in question. French CJ's approach was expansive and consistent with his reasoning in *Re: Richstar* whereas the joint decision of Gummow and Hayne gave property a purposeful meaning but more confined to the facts of the case.

French CJ held that the relevant property were the trust assets[165] "…coupled with the trustee's power, prior to the 1998 instrument to appoint them to her and her equitable right to due consideration, that should be regarded as the relevant property "and he then concluded:[166]

> For so long as Dr Spry retained the legal title to the trust fund coupled with the power to appoint the whole of the fund to his wife and her equitable right, it remained, in my opinion, property of the parties to the marriage for the purposes of the power conferred on the Family Court by s 79. The assets would have been unarguably property of the marriage absent subjection to the trust.

In this way French CJ recognised that whilst assets may change their legal form they remain wealth accumulated during the marriage partnership and the characterisation of that property is not automatically lost in the process of disposition to a discretionary trust.

Gummow and Hayne JJ took a different approach and concluded:[167]

> … Furthermore, as an object of these powers the wife had a right in equity to due administration of the trust. The existence of such a right did not depend upon entitlement to any fixed and transmissible beneficial interest in the trust fund. The right of the wife was accompanied at least by a fiduciary duty on the part of the trustee, the husband, to consider whether and in what way he should exercise the power conferred by clause 6.

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165 *Spry* above n 162 at [62] French CJ.

166 At [66] French CJ.

167 At [125] Gummow and Hayne JJ.

The fact that the husband could not confer benefits on himself meant that whilst he did not have property in the assets of the trust he nevertheless had the power to benefit the wife and in this way Their Honours found:[168]

> Reference was made earlier in these reasons to the comprehensive sense in which the term 'property' is defined in s 4(1) of the Act. And it will also be recalled that the 'property' which may be the subject of orders under s 79(1) of the Act is "the property of the parties of the marriage or either of them". … The right of the wife with respect to the due administration of the trust was included in her property for the purposes of the Act. …. And in considering what is the property of the parties to the marriage (as distinct from what might be identified as the property of the husband) it is important to recognise not only that the right of the wife was accompanied at least by the fiduciary duty of the husband to consider whether and in what way the power should be exercised, but also that, during the marriage, the power could have been exercised by appointing the whole of the trust assets to the wife.

The Court also had to consider the position of the wife after the divorce. The husband argued that following the divorce the wife had no further interest in the trust as she could not fall within the definition of a beneficiary. Despite the lack of a beneficial status at the time of the hearing the court was prepared to consider her position 'as if' – "… changes to property rights ... had not occurred."[169]

Heydon J in dissent took the orthodox position and he started from the proposition that as the wife did not apply to set aside the 1983 instrument (which deprived the husband of any beneficial interest in the trust) then neither she nor her husband had any entitlement to the trust's income or capital unless the husband in 'his absolute discretion' decided otherwise. They were both the "object of a bare fiduciary power of appointment"[170] and consequently he accepted the husband's argument that the application before the court related to land, shares and money and not to the rights to have those assets duly administered.

The outcome of the case was that the earlier dispositions in 1998 and 2002 were set aside and in accordance with the earlier judgments Dr Spry was personally ordered to pay his

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168 *Spry* above n 162 at [126] Gummow and Hayne JJ.

169 At [129].

170 At [149].

former wife $2,182,302.[171] If Dr Spry wanted to satisfy his obligations by recourse to the trust assets then he could apply to the court for an appropriate order.[172]

However, Dr Spry did not pay the ordered sum and refused to apply to the court for an order that the trust made a distribution to satisfy the judgment debt. In 2009 the facts of the case returned to the Family Court of Australia in *Stephens v Stephens*[173] on the primary question as to whether any order could be made attaching to the assets of the trust. The court held that the FLA permitted such an order "that enables a party to the marriage who is in control of the trust to satisfy his or her personal liability to the other party to the marriage who is an object of the trust from the assets of the trust." [174]

As the facts in *Spry* were unusual it has been suggested that – "the precise ratio of the decision is impossible to state, perhaps little harm will be done. On one view it could be read down as an eccentric view on the width of 'property' as a term under the Family Law Act."[175]

However, Justin Gleeson SC explained the ratio as represented by the reasons of Gummow and Hayne JJ supported and expanded by French CJ as follows:[176]

> (a) Where at the date of commencement of the matrimonial cause, one party to the marriage has power under the trust instrument to appoint the entirety of the property in favour of the other party as one of the class of discretionary objects, the whole of the assets of the trust fall within the description of 'property' of the parties to the marriage to either of them" within s 79, and at full value;
>
> (b) It is within the power of the court to make an order for the payment of a money sum which assumes that the entirety of the assets of the trust are within the disposition of the first party, even if at the date of resolution of the property settlement proceedings the other party no longer remains with the class of objects;

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171 *Spry* above n 162 at [81], [130], [137] and [140].

172 At [138].

173 *Stephens v Stephens and Anor* (2009) 42 Fam LR 423 at [340].

174 At [355].

175 Lee Aitken "Muddying the waters further – *Kennon v Spry*: 'ownership', 'control' and the discretionary trust" (2009) 32 Aust Bar Rev 173 at 176.

176 "Spry's case: Exploring the limits of discretionary trusts" above n 130 at 183.

(c) Before exercising such a power, the court would consider the interests of the other members in the class of discretionary objects, but where they represent in large measure the children of the parties to the marriage and where the assets in the trust represent accumulated property over the life of the marriage, the children have no substantial claim against the making of the order.

(d) Where persons other than the parties to the marriage and the children fall within the class of discretionary objects, they would have standing to oppose the order but would need to establish a proper ground upon which it would be just and equitable to refuse or modify such order.

(e) Where such a money order is made, the court has power by way of further machinery orders under ss79 and 80 to order that the first party satisfy the liability to pay the money sum out of the assets of the trust.

The major criticisms, both judicial and academic, of the majority in *Spry* and some of the earlier authorities rests on the unravelling of the orthodoxy in a way that has no historical parallel in equity or in law by denying the applicability of fiduciary law principles. As the authors of *Australian Family Law: The Contemporary Context* explain it is the lack of adherence to an approach "that is familiar and correct to trust lawyers that is the real issue".[177]

The starting point to the criticisms of the High Court's approach in *Spry* is that a discretionary beneficiary can have a proprietary interest in the assets of a discretionary trust. Traditionalists remain loyal to the rule in *Gartside,* that an object of a bare power of appointment cannot have a proprietary interest in those assets, "but only a mere expectancy or hope that one day the power will be exercised in that object's favour".[178] Prior to appointment in their favour a discretionary beneficiary only has a right to due administration of the trust which is not a property right to the assets of the trust.

The next level of criticism looks at the proposition that, whilst trustees may have opportunities to misuse their office, it cannot be assumed that they will misuse their powers to gain a financial advantage over other beneficiaries. The orthodox view is that

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177 *"The contemporary context"* above n 124 at p 483.

178 *Kennon v Spry* (2008) 251 ALR 257 at [160].

this is the very reason that equity has developed stringent rules "restraining the self-interest of trustees and keeping them within the ambit of their powers".[179]

Even if it is assumed the spouse/trustee will make self-serving distributions then courts should not notionally include trust assets which have been unlawfully obtained. The analogy is to consider a situation where a spouse includes in the property pool assets which have been stolen at work.[180] The proper response should be that the spouse/trustee should be restrained from the wrong of breaching fiduciary duties and/or become liable for unlawfully receiving or dealing with trust property.

Other criticisms are that labels such as *alter egos*, 'puppets', or 'creature' do not amount to 'ownership' of the trust's assets.[181] Phrases such as 'de facto ownership' and 'effective ownership' mean that they may be in as good a position as if they were the beneficial owners but that does not establish actual beneficial ownership.[182]

The outcome in *Spry* shows that the High Court of Australia were not moved by submissions based on orthodox principles of trust law, they expanded the definition of 'property' rather than consider whether Dr Spry's interest in the trust was a 'financial resource' and despite the lack of valuation evidence the Court treated the whole of the trust fund as property of the marriage.

As can be seen the debate as to whether or not the principles in *Spry* are sound law continues. The controversy that arises out of Australian case authorities illustrates that both trust and family law are competing for the same foundational right to claim presumptive power over the other. In Australia, the contest has been settled and the meaning of property has been given trumping power over orthodox principles.

The question then arises as to what significance does this have for New Zealand? Certain aspects of the *alter ego* trusts principles are likely to be influential in the development of the meaning of property under the PRA.

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179 John Glover "Discretionary trusts, fiduciary duties and the Family Law Act: Has the Family Court acted beyond power?" (2000) 14 AJFL 184 at 186.

180 At 192.

181 *Public Trustee v Smith* [2008] NSWSC 397 at [118] White J.

182 At [138].

In the next chapter the discussion moves to the meaning of property under the PRA and considers the concept of property interests arising out of a ‘bundle of rights’ in a discretionary trust.

V New Zealand the Meaning of Property and 'Bundle of Rights' Theory

A The Definition of Property and Owner

This chapter considers the meaning of 'property' under the PRA and in particular the circumstances where a spouse or partner may have a property interest in a discretionary trust.

In order to understand what property can be affected by obligations owed under the PRA[183] it is necessary to identify what constitutes 'property,' who owns it and if property whether it is classified as either relationship or separate property.[184]

The PRA, as a whole, distinguishes between what may be relationship/separate property from assets owned by third parties. The Act provides immunity against claims against the legal owner of a trust fund in a number of ways. Firstly, s 4B[185] specifically provides that the Act does not affect the law that applies "where either the spouse or de facto partner is acting as trustee under any deed or will" and secondly s 19[186] expressly provides that nothing in the Act shall "affect the title of any third person to any property." At first glance these provisions appear conclusive in that the Family Court has no jurisdiction to consider trust assets or the position of a spouse or partner who is also a trustee. As will be seen the position with discretionary trusts is more complex.

The Act defines property as including:[187]

(a) real property;
(b) personal property;
(c) any estate or interest in any real property or personal property;
(d) any debt or anything in action;
(e) *any other right or interest*

The focus of this dissertation is on the meaning of 'any other right or interest' and for the reasons discussed in chapter 2 a property right describes a certain type of relationship

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183 Property (Relationships) Act 1976 ("the Act").

184 Nicola Peart (ed) *Brookers Family Law – Family Property* (loose leafed, Brookers) at [TU9.01] [*Brookers Family Law*"].

185 Property (Relationships) Act 1976, s 4 and s 4B.

186 Property (Relationships) Act 1976 s 19.

187 Property (Relationships) Act 1976 s 2 (my emphasis).

between a legal entity and an asset[188] and the degree of protection afforded to that right will be indicative of whether or not it has the status of property. In contrast an interest is conceptually more uncertain than a right and in *Leedale (Inspector of Taxes) v Lewis* Lord Wilberforce said:[189]

> The word 'interest' is one of uncertain meaning and it remains to be decided on the terms of the applicable statute which, or possibly what other, meaning the word may bear.

In New Zealand, property has been given an expansive meaning in the context of the PRA. In *Mackenzie v Mackenzie*[190] Doogue J held that "[t]he word "property" is not defined in the Act in any narrow or legalistic way, but rather as "including" certain defined matters to extend the meaning which might otherwise be given to it."[191]. Consequently, property includes a beneficial interest in the assets of a partnership[192] even in circumstances where that interest remains undivided, unallocated and subject to regulation by the Partnership Act.[193]

As the authors of *Brookers Family Law – Family property* note[194] "things to which rights can attach under the Act are extremely wide" and are not confined by conventional property law.

However, for an item identified as 'property' a spouse or partner must be its beneficial owner. Owner is defined as:[195]

> In respect of any property means the person who, apart from this Act, is the beneficial owner of the property under any enactment or rule of common law or equity.

The authors of *Brookers Family Law – Family Property* discuss the term 'beneficial owner' in s 2 and note that:[196]

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188 *Brookers Family Law* above n 184 at [TU9.01].

189 *Leedale (Inspector of Taxes) v Lewis* [1982] 3 All ER 810 at 816.

190 *Mackenzie v Mackenzie* [1992] NZFLR 120.

191 At p 127.

192 *Maw v Maw* [1981] 1 NZLR 25, 26.

193 *Rose v Rose* [2009] 3 NZLR 1 at [32].

194 *Brookers Family Law* above n 184 at [TU9.01].

195 Property (Relationships) Act 1976 s 2.

> The use of this expression in the Act is slightly confusing because it is otherwise usually used in contradistinction to the expression 'legal ownership'. The distinction only exists where some form of settlement dividing absolute ownership into legal and equitable estates has occurred. The expression 'beneficial owner' used in s 2 necessarily includes the 'absolute owner' of property as well as those who hold an equitable interest in property.

The question is whether the use of modern discretionary trust creates a type of beneficial ownership in circumstances where the division between legal and equitable estates is blurred because the purpose of the discretionary trust is to create "the illusion of separate ownership."[197]

A similar question has been raised by the Law Commission "where settlors never intend to give up control or beneficial ownership"[198] of property transferred into a trust. The proposition is that there may be grounds to invalidate a trust based on a lack of the equitable requirement for certainty of intention and the settlor has retained 'effective ownership' of the assets. Whether the courts would be prepared to invalidate trusts in this way is debateable but it is the writer's view that the same considerations arise when considering if 'effective ownership' means beneficial ownership under the PRA.

B 'Rights and Interests' in Discretionary Trusts

In recent years there has been a growing body of judicial opinion that rights and interests of one or both spouses or partners in a discretionary trust may be susceptible to claims under the Act.[199] For instance, in *B v M* Allan J said:[200]

> It is certainly arguable that the definition of the term 'property' in s 2 is sufficiently wide to cover the rights and interests of a spouse as a beneficiary under a discretionary trust. The difficulty lies in the valuation of that interest.

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196 *Brookers Family Law* above n 184 at [TU 9.01].

197 "The Law of Trusts in the Family Court" above n 145 at p 4, 6-7.

198 Law Commission: "Some issues with the use of trusts in New Zealand: Review of the law of trusts second issues paper" (NZLC IP20, 2010) at 5.32.

199 *Brookers Family Law* above n 184 at [10.03].

200 *B v M* [2005] NZFLR 730 at [98] (HC).

The possibility that such rights and interests could be given property status is almost revolutionary to a lawyer steeped in equitable principles and given the conventional orthodox view expressed by the Court of Appeal in *Hunt v Muollo*[201] that:

> It is generally regarded as settled law that a discretionary beneficiary's interest in a normal discretionary trust is no more than a mere expectancy. It is simply an expectation or hope (in Latin a spes) that the trustee's discretion may be exercised in the beneficiary's favour … an ordinary discretionary beneficiary has no interest, legal or equitable in the assets of the trust … it is only on the making of a distribution to the discretionary beneficiary that the beneficiary obtains any interest in property, and then only to the extent of the distribution.

In *Hunt v Muollo* the Court of Appeal had to consider whether the interests of a discretionary beneficiary in a trust is a species of property capable of coming within the meaning of 'assets' or 'means' pursuant the High Court Rules.[202] The Court held that the "rule must be construed and applied in the context of the general law of property. If the position were otherwise the ambit of the rule would have no clear or principled boundary."[203] It does however remain possible that the Court of Appeal has not finally determined this issue because this often quoted passage states that the law is "generally" settled and also refers to "a normal discretionary trust".

This leaves open the possibility that an 'abnormal' discretionary trust may be one where the beneficiary effectively controls the trustees' power of selection.[204] If the law develops in this way then it will carve out a general exception to the presumption that a discretionary beneficiary has no more than a mere expectancy.

In *Nation v Nation*[205] the Court of Appeal considered whether the interests of a discretionary beneficiary could constitute relationship property and took the traditional approach when it held:[206]

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201 *Hunt v Muollo* [2003] 2 NZLR 322 at [11].

202 High Court Rules r 621(2).

203 *Hunt v Muollo* [2003] 2 NZLR 322 at [13].

204 *Re Richstar* above n 157-159 at p 43 where French J carved out an exception to the rule in *Gartside v IRC* [1968] AC 553.

205 *Nation v Nation* [2005] 3 NZLR 46 referring to *Hunt v Muollo* [2003] 2 NZLR 322 and *Johns v Johns* [2004] 3 NZLR 202.

206 At [74].

> The conventional view is that a discretionary beneficiary has no legal or equitable interest in the assets of the trust until the trustees have exercised their discretion in favour of the particular beneficiary

Again there may be some room to doubt that this issue has been finally settled in the context of cases under the PRA because of the way that particular case had been argued and the evidence placed before the Courts.[207]

In *Johns v Johns*[208] the Court of Appeal considered the meaning of the term "future interest" under The Limitation Act 1950. The relevant section provided that the statutory period of limitation would accrue in the following circumstances:[209]

> Provided that the right of action shall not be deemed to have accrued to any beneficiary entitled to a future interest in the trust property until the interest fell into possession.

The Court of Appeal found that the plaintiff had three different interests in the trust property being: his interest as a discretionary beneficiary,[210] his residual interest[211] and his income interest in the trust fund.[212] In respect to the plaintiff's discretionary interest the Court of Appeal upheld its earlier decision in *Hunt v Muollo*[213] and also referred to *Armitage v Nurse*[214] a UK case involving an equivalent Limitation Act proviso[215] and held:[216]

> We respectfully agree that a right of that kind cannot properly be regarded as an "interest" in the trust property, whether present or future, for the purposes of the proviso to s 21(2). … They [counsel's submissions] cannot be reconciled with the authorities mentioned, or indeed with conventional concepts of what amounts to an

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207 The case on appeal was largely concerned with the application of s 44C Property (Relationships) Act 1976 and even that issue proved problematic because the Trust Deed was never produced and there was no valuation evidence.

208 *Johns v Johns* [2004] 3 NZLR 202 (CA).

209 The Limitation Act 1950 s 21(2).

210 *Johns v Johns* [2004] 3 NZLR 202 at [26] per Tipping J.

211 At [27].

212 At [28].

213 *Hunt v Muollo* above n 201.

214 *Armitage v Nurse* [1988] Ch 241.

215 The Limitation Act 1950, s 21(2).

216 *Johns v Johns* above n 208 at [33].

> interest in trust property. That interest must be either legal or equitable. It cannot extend to the so-called interest of a discretionary beneficiary which is neither legal nor equitable.

However, Tipping J said that in *Armitage v Nurse* Millett LJ emphasised the uncertainty of the meaning of the word 'interest'[217]and that the word must be ascertained from the legislative purpose in the relevant statute in which the word 'interest' appears. Tipping J added that a "discretionary beneficiary may well be able to bring proceedings to compel proper administration of the trust … that although a discretionary beneficiary has no proprietary interest in the trust assets he has sufficient standing to compel proper administration of the trust."[218]

On the issue of the residual interest the Court of Appeal held that in that case the 'future interest' was property and it did not matter that the interest "is contingent on survival to the date of distribution and on their being trust property available for distribution at that time does not prevent it from being an interest.[219] Further Tipping J said:

> The proper interpretation of the expression "future interest" for the purposes of the proviso must recognise the vital importance of the context, as Millett LJ emphasised in *Armitage v Nurse.* …. The crucial difference between contingent and vested interests on the one hand and discretionary interests on the other is that possession of the former interests if enjoyed at all, is enjoyed as of right; whereas discretionary interests are never enjoyed as of right; their enjoyment is always subject to the discretion of the trustees.

Hunt v Muollo[220] and *Johns v Johns*[221] were cases involving factual situations which have been considered in the context of general legislative provisions. The question this dissertation considers is whether these authorities are necessarily applicable to the PRA.

C 'Bundle of Rights' – Valuation of Debts

Since *Nation* the Court of Appeal has introduced a further strand to the meaning of property with the development of the concept that a spouse or partner may have a 'bundle

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217 *Armitage v Nurse* above n 214.

218 *Johns v Johns* above n 208 at [34].

219 At [45].

220 At [49].

221 *Hunt v Muollo* above n 201.

of rights' in the management of a discretionary trust which is property within the meaning of the PRA.

The development of this line of authority raises fundamental questions as to whether exceptions are being carved out of the conventional view expressed in *Gartside,*[222] *Hunt v Muollo,*[223] and *Nation*[224] and this requires careful examination.

In *Walker v Walker*[225] the Court of Appeal considered a question regarding the valuation of a debt owed to the husband by a discretionary family trust. The debt was relationship property and arose because the Trust had purchased the husband's shares in his company and a property that was jointly owned by the spouses. The trustee was a company of which the husband was the sole director, but both spouses held the power to appoint and remove trustees as well as the directors of the trustee company. The spouses were discretionary beneficiaries of the trust. When they separated the husband wanted to carry on the business and buy the wife out of the debt which then had to be valued.

The Court of Appeal held that private debts should be valued as any other asset, but taking into account that a spouse or partner is not an independent third party and may not want to realise the debt immediately. More importantly, the debt was related to a "package"[226] of assets that included the shares as well as the couple's discretionary interests in the trust and their power to appoint and remove trustees and company directors.

Apart from the implications this 'package of assets' has on the meaning of property it also raises important factors that the court should consider when assessing the value of the debt, namely: Can a private debt be anything less or more than its face value? When should it be valued? What factors need to be taken into account on valuation? Chambers J said:[227]

> We agree the fact the debt is a private debt can lead to complications in valuation. For instance, if a debt owed by a family trust cannot be paid or can be paid only in part, the devaluation of the debt may be compensated for, at least in part, by an

222 *Gartside v IRC* (1968) AC 553.

223 *Hunt v Muollo* above n 201.

224 *Nation v Nation* above n 204.

225 *Walker v Walker* [2007] NZFLR 772 (CA).

226 At [49] Chambers J.

227 At [38].

> increase in value of one party's or both party's interests in the trust – whether his, her or their interests as settlor, trustee, appointor or beneficiary, which interests may be relationship property.

Consequently the Court rejected an argument that a debt could never be less than its face value. The Court noted that a debt could fall in value if the trust has not the means to repay it and it may rise in value again if the trust's fortunes improve.[228] The debt needed to be valued at the date of hearing.[229] Importantly, attached to the debt the husband would retain: directorship of the trustee company; shares of the trustee company; power to appoint and remove directors of the trustee company; power to appoint and remove trustees of the trust and the parties' discretionary interests under the trust.[230]

Although the value of the debt increased as a consequence of the husband's skill and labour the Court was of the view that was only a part of the reason for the increase in value. The company had employees, all of whom would have contributed to the restoration of profitability. The company benefited from its capital base (which had been contributed by the parties to the relationship) and by the fact the wife had not insisted on repayment of the loan. The wife thereby effectively provided free working capital to the business with no prospect of any equity return and in circumstances where the best return she could have hoped for was the face value of the debt. The husband's skills in managing the company had been honed and fostered during the marriage as he had been freed from the domestic responsibilities which had been undertaken by his wife.[231]

The face value of the debt was not the correct methodology of valuation because it erroneously assumed that that an independent third party will be the buyer.[232] It also ignored the possibility that the parties themselves may be prepared to offer more for the debt than an independent third party[233] and a party to a relationship may not want an immediate payment but rather its long term potential.[234]

The heart of the valuation issue was explained by Chambers J when he found:[235]

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228 At [41].
229 At [46].
230 At [48].
231 At [51].
232 At [57].
233 At [58].
234 At [59].
235 At [60].

> Thirdly, it is wrong to focus on the debt in isolation to the rest of the package. Clearly all six items of property forming the package should have been valued on an assumption that they were for sale together. That would be a reasonable assumption in terms of maximising the value of the relationship property, for, as we have said, together they confer control of the company.

The concept that the husband had 'control' over the corporate trustee company was central to the Court's assessment of the value of the relationship property debt. This sentiment is also reminiscent of the High Court of Australia's approach *In the Marriage of Ashton*[236] where the husband's control of the trust amounted to the trust being the *alter ego* of the husband.

Then in *Harrison v Harrison*[237] the High Court took the position further when it considered an appeal on an application for interim distribution of relationship property. In that case the major assets, being home and a half share in a profitable business, had been transferred to a family trust. The settlor was the husband and wife and the trustee a company Cappa Harrison Trust Company Ltd (CHTC). There were relationship debts owed to the parties by the CHTC of approx $602,000.

Fogarty J looked at the 'substantial effect of the arrangement'[238] He went through the deed which provided wide discretionary powers and he found that the parties 'control the trustees'.[239] As the trustee company was under the complete control of the parties he concluded:[240]

> In short the husband and wife have the ability at any time, without the need to give any reason to the other contingent beneficiaries, to vest the entire assets of the 'trust' to themselves. It appears that the intention of the husband and wife when entering into the deed was to retain complete control over the use and enjoyment of all the assets transferred to the trustee, until at some later date when they might decide to transfer some or all of the assets to other persons. Given the ability and the apparent intention, there is a serious argument which the parties may yet engage in, that, upon a substantive analysis, for the time being the legal and equitable estates unite in the husband and wife.

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236 *In the Marriage of Ashton* (1986) 11 Fam LR 457 at 462.

237 *Harrison v Harrison* (2005) 2 FRNZ 2002 (HC) Fogarty J.

238 At [22].

239 At [25].

240 At [25].

Fogarty J then somewhat controversially said:[241]

> In situations where an entity such as CHTC holds the assets, but later a trust is not recognised by the Court, the entity can be treated by the Court as merely an instrument of the true owners, sometimes described as a puppet or alter ego.

As this was an appeal from an interim distribution of relationship property it was not appropriate for the Court to make final findings as to whether the trust was ineffective as the Court still had the option of considering the value of debts owed to the parties in CHTC.

An application was then made for Leave to Appeal to Court of Appeal which was granted[242] but the husband did not prosecute the appeal and in December 2009, the stay lapsed and the appeal was struck out. Importantly, Robertson J said in granting leave:[243]

> There was also a bundle of rights associated with their positions as discretionary beneficiaries under the CHFT and as joint holders of the power of appointment of the CHFT

Nevertheless, "the legal structures which the parties have mutually created must be the starting point for an assessment of what property is available for distribution at an interim stage."[244]

It is unfortunate that the *Harrison* case did not go on to an appeal because the boundaries around the doctrine of the 'bundle of rights' need clarification.

By way of example, Judge L J Ryan in *SMB v GAC*[245] considered a situation where a de facto partner transferred his interest in a superannuation scheme into a discretionary trust and throughout the relationship he continued to make contributions to the scheme out of his income. He was a discretionary beneficiary and had power to appoint and remove

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241 At [28].

242 *Harrison v Harrison* [2009] NZFLR 687 (CA).

243 At [10].

244 At [22].

245 *SMB v GAC* FC, North Shore, 19 November 2010, FAM-2007-044-000946 Judge L J Ryan.

trustees.[246] In these circumstances the de facto partner 'controlled' the trust and Judge Ryan held:[247]

> I regard the respondent's total control of the trust combined with his rights as a discretionary beneficiary as amounting to a "package of rights" as that term is used by the Court of Appeal. As such it is property as defined in the Act.

The difficulty with this conclusion is that it is not entirely clear from *Walker* if the Court of Appeal intended the "package of rights" to be considered independently to the valuation of the debt. Chambers J refers to - "... five items of property, plus the debt formed a very valuable package, as *together* they confer control of the company."[248]

Until the boundaries surrounding the "bundle of rights' doctrine are clarified there will be continuing conjecture as to the types of 'interests' in discretionary trusts which give rise to property rights. Nevertheless, it is the writer's view, drawing on the discussion in the last two chapters, that effective 'control' is likely to give rise to a property interest. It is for this reason that the Australian concept of *alter ego* trusts is similar to the 'bundle of rights' doctrine but with the caution that it is unlikely that the Courts in New Zealand will declare (as in the High Court decision of *Harrison*) that such trusts are ineffective as this could lead to a situation where discretionary trusts may generally collapse under attacks from third party claims.

Instead the *Walker* case finds a middle ground, within the context of family law claims, which recognises that the wealth created during the relationship is still available when the parties cease to live together because one (or both) 'control' not only the trust but the ability to benefit from that wealth. In these circumstances the illusion of separate ownership by a third party trust is cast aside in the valuation process. The relationship property enquiry remains in conventional territory as the focus rests on the value of the debt-back and all the components which are related to the debt.

This approach is also similar to that taken in *Z v Z (No.2)*[249] which involved the valuation of the husband's 'bundle of rights' in a legal partnership in circumstances where on the face of the partnership agreement his interest in the goodwill of the firm had a no value.

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246 At [35].

247 At [40].

248 *Walker v Walker* above n 225 [49] (my emphasis).

249 *Z v Z (No.2)* 2 NZLR 258 (CA) and discussed in chapter 2 above.

These cases also draw on the Australian position by looking at the social reality that the disposition of assets to a discretionary trust does not mean that wealth has lost its character as 'property of the parties to the marriage".[250]

D Gift Duty

Before leaving this line of valuation cases it is important to pause and consider how the concept of a 'bundle of rights' will be affected by the Government's decision to introduce legislation abolishing gift duty from 1 October 2011.[251] If there are no consequential amendments to the PRA then debts owed by discretionary trusts could be forgiven in one lump sum. In these circumstances a valuable asset will no longer exist at the end of the marriage, civil union or de facto relationship, and leaving aside the 'bundle of rights' principles, it may not be possible to claw back the original source of relationship property into the pool of property.

Currently, a trust can avoid gift duty either by paying for the asset or acknowledging the purchase price as a debt back to the original owner(s) ("donor"). The donor can then gift the value of the asset to the trust either in one lump sum or by instalments of $27,000 per donor per annum. If the gift is in one lump sum then gift duty is payable in accordance with the legislation.[252] Most family discretionary trusts do not have the capital to purchase assets outright and generally the debt back to the original owner is preferred with a gifting programme.

In this way gift duty has had a significant impact on trust practice in New Zealand. These practices have a number of advantages in relationship property cases: assets are valued at the time of disposition and generally a record is kept of the market value at that time and the debt to the original owner is quantified and usually recorded by way of a deed of acknowledgement of debt. Once a spouse(s) or partner(s) enter into a gifting programme a record is kept of the gifts with corresponding deeds of reduction of debt. This process not only means that dispositions of property to trusts may take many years but also provides a financial and evidential trail of gifts. Depending when the trust was settled the debt back may be the only substantial asset in existence at separation. Consequently, if

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250 *Kennon v Spry* (2008) 251 ALR 257 at [65] per French CJ.

251 "IRD Minister Peter Dunne "Announces abolishment of gift duty from October 1, 2011" (1 November 2010) www.interest.co.nz.

252 Estate & Gift Duties Act 1968 s 62, Schedule: Scale of rates of gift duty.

the Gift Duty is abolished debts owed to parties may be immediately forgiven and the valuation exercise set out in the *Walker* case may become redundant.

Another issue is that the gifting process requires the donor to participate in the gifting programme each year which in turn gives an opportunity for the individual to consider whether or not to continue with the gifting process. So at least there is an opportunity for individuals to obtain advice as to their legal position with a gifting programme as or if their circumstances change.

The distinction between gifts and loans has been the subject of dispute under the PRA in relation to sums of money that have created relationship property. Often these disputes arise when a member of the family provides a lump sum payment which goes towards the acquisition of property. When the relationship ends in separation or death an issue arises as to whether or not the funds were loans or a gift; the former but not the latter fall under the regime of debt sharing under the PRA.[253]

A gift has been described as a "present made without return of any kind"[254] and its distinguishing feature is the absence of valuable consideration. The essential elements of a gift are:[255]

(i) an intention to transfer the immediate ownership of the property or, where the legal title is retained, to relinquish immediately the beneficial ownership in favour of the donee;
(ii) an act or acts adequate to give complete effect to that intention; and
(iii) acceptance of the gift by the donee.

The courts have approached these disputes on a case by case basis and much depends on the evidence of whether there was the requisite intention to create a gift at the time of the advance. The courts have given due weight to documentary evidence but at the same time it has not been determinative of the issue.[256] For instance, in a case involving the disposition of a spouse's separate property to a discretionary trust an issue arose as to

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253 Property (Relationships) Act 1976 s 20D.

254 *Rennell v IRC* [1964] AC 173 at 192 per Lord Radcliffe.

255 NZ Forms & Precedents (looseleaf ed, LexisNexis) at [2504] referring to *Williams v Williams* [1956] NZLR 970.

256 *Young v Young* [2000] NZFLR 128 at 134 and *N v N [Division of Property]* [2009] NZFLR 757 but subsequently overturned on appeal *N v N [Relationship Property: loan]* [2010] NZFLR 161 (HC).

whether or not the wife consented to the disposition[257] and in that case the court found that she acquiesced but did not consent and consequently there was no gift. The lack of independent legal advice was a significant factor.

Recently, the Supreme Court has considered the distinction between consent and acquiescence in *Cashmere Capital Ltd v Carroll*[258] McGrath J referred to an earlier Court of Appeal case in both New Zealand[259] and quoting from Shaw LJ in *Bell v Alfred Franks & Bartlett Co Ltd*[260] he held[261]:

> If acquiescence is something passive in the face of knowledge, what does 'consent' mean? … The only sense in which there can be implied consent is where consent is demonstrated, not by language but by some positive act other than words which amount to an affirmation of what is being done and goes beyond mere acquiescence in it …

Consequently, there may be situations where a spouse or de facto partner has no independent legal advice and in those circumstances there may be grounds to consider whether the spouse or partner did consent to gifting a debt-back to the trust.

Alternatively, the common law has always recognised that a gift can be set aside on the grounds of fraud, duress, undue influence, mistake or incapacity.[262] The grounds of fraud and undue influence are most likely to give rise to applications to set the gift aside under the PRA. The issue of fraud is discussed in more detail at chapter 6 when considering applications to set aside dispositions to trusts[263] but there is no statutory ground of undue influence under the PRA.

In *Attorney-General for England and Wales v R*[264] the Court of Appeal considered the general principles of undue influence and the classic situation in which equity intervened

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257 *Fraser v Buxton* FC, Wellington, FAM-2005-085-000919, 23 April 2008 Judge J Johnston.

258 *Cashmere Capital Ltd v Carroll* (on appeal from *Cashmere Capital Ltd v Crossdale Properties Ltd*) [2010] 1 NZLR 577 (SC).

259 *NZ Fisheries Ltd v Napier City Council* (1990) 1 NZ ConvC at 190, 342 and 344 (CA).

260 *Bell v Alfred Franks & Bartlett Co Ltd* [1980] 1 WLR 340.

261 At [77] and [78] McGrath J.

262 NZ Forms & Precedents above n 254 at [2520].

263 Property (Relationships) Act 1976 s 44.

264 *Attorney-General for England and Wales v R* [2002] 2 NZLR 91, [70] to [82] Tipping J (CA).

when the relationship between the parties was one of trust and confidence. Tipping J referred to the leading English cases and held:[265]

> ... Cases in class 1 represent those in which the plaintiff can affirmatively prove actual undue influence. Class 2 involves cases in which undue influence is presumed unless it can be rebutted. In class 1 cases, the party asserting undue influence (X) proves that the other party (Y) in fact exerted undue influence upon X to enter into the impugned transaction. Cases within class 2 fall into two sub-classes. Class 2(A) involves certain relationships (such as solicitor and client or doctor and patient) which give rise to a legal presumption of undue influence. Class 2(B) represents cases in which although the relationship between X and Y is not of itself such as to raise a legal presumption of undue influence, X can show that there existed such a relationship of trust and confidence between the parties and the transaction was of such manifest disadvantage to X that it can reasonably be presumed that Y did in fact exert undue influence on X to enter into the impugned transaction.

However, Tipping J went on to say that the position of Class 2(B) cases had been modified by the House of Lords in *Royal Bank of Scotland v Etridge*[266]in that whilst:[267]

> "[t]he relationship may give rise to a presumption of trust and confidence, but not a presumption that such trust and confidence was abused by the exercise of undue influence. But when the nature of the transaction calls for explanation in the light of the relationship between the parties the evidential onus shifts to the defendant to demonstrate the absence of undue influence. The concept of manifest disadvantage which had caused some difficulties was thus retained as a relevant factor in the overall evidential assessment but was abandoned as a separate criterion.

As a consequence, when spouses or de facto partners sign a deed confirming their intention to gift the entirety of debt to a discretionary trust it may be possible to assert that the transaction is tainted by undue influence. A lot will depend on the facts in each case but if there is little or no explanation given to the donor that the gifting may extinguish a valuable relationship property asset then it may be open to the courts to set aside the gift and then return the debt-back to the relationship property pool.

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265 At [71] Tipping J.

266 *Royal Bank of Scotland v Etridge (No 2)* [2001] 4 All ER 449.

267 At [72].

Against this background the PRA recognises that parties are entitled to "deal with or dispose of any property"[268] during the relationship and there is no requirement that parties must have independent legal advice before disposing of assets into a discretionary trust. Therefore the process of challenging a gift is not straightforward.

In conclusion, the existence of gift duty has been a major inhibitor to the gifting of debts owed to spouses or partners by discretionary trusts. Once gift duty is abolished there is a strong likelihood that debts-back will be forgiven and there are then two ways a prejudiced party may be able to claw-back the lost wealth into the relationship property pool: either the gift is set aside on the basis of lack of consent, fraud or undue influence or the courts adopt an approach similar to *Kennon v Spry* by finding that a party who has 'control' of a discretionary trust has a proprietary interest in the trust fund. This will take the *Walker v Walker* principles one step further towards expanding the definition of property and establishing case authority that 'control' of a discretionary trust is not confined to valuation principles.

If these options do not apply then the abolition of gift duty will further exacerbate the situation which already exists when there is an insufficient pool of property to grant compensation to a disadvantaged party.[269]

E 'Bundle of Rights' – Occupation Orders

Another line of Family Court cases has developed over the practical problem of who is to occupy the family home following a separation when that property is owned by a third party trust(s). Section 27(1) of the PRA provides:[270]

> The Court may make an order granting to either spouse or partner, for such period or periods and on such terms and subject to such conditions as the Court thinks fit, the right personally to occupy the family home or any other premises forming part of the relationship property.

The issues the courts have considered are whether a trust property could be the family home or form part of the relationship property. There have been three decisions which take different approaches.

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268 Property (Relationships) Act 1976 s 19(a).

269 Property (Relationships) Act 1976 s 44C and discussed at Chapter 6.

270 Property (Relationships) Act 1976 s 27(1).

In *Gao v Elledge*[271] the Family Court considered an application for an occupation order could be made in circumstances where both parties were settlors and beneficiaries of a trust. Judge Robinson made an occupation order in favour of the wife because she had a beneficial interest in the property arising from a trust settled by both parties. On the question as to whether or not that beneficial interest was relationship or separate property the Court held that the evidence established that the property was being used as a family home and was therefore relationship property unless designated separate property by a s 21 agreement[272].

Then in *Keats v Keats*[273] the parties were trustees and beneficiaries of a discretionary trust. The children were the final beneficiaries. Judge P Grace adopted the conventional view in *Hunt v Muollo*[274] that a discretionary beneficiary's interest in a trust does not create a property interest and he concluded that such an 'interest' was not 'property'. *Guo v Elledge* was distinguished on the basis that the parties were sole beneficiaries of the trust and therefore held the equitable interest in its assets.

In *R v R*[275] an application was made for an occupation order where the parties had settled two mirror trusts which controlled a partnership trust which in turn owned the family home. Each party had powers of appointment, were trustees of each other's trusts as well as beneficiaries along with their children.

Judge Burns compared the two earlier family court decisions[276] of *Elledge* and *Keats* and concluded that the occupation order in *Elledge* was made because the parties had a beneficial and therefore a proprietary interest in the trust's assets. Further, the beneficiaries had the power to request transfer of the property to them, and the power to direct the trustees to deal with the property as the beneficiaries required.

On the other hand in *Keats*[277] the court was concerned with a situation where the parties where two of three trustees of a purely discretionary trust and were only discretionary

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271 *Gao v Elledge* [2003] NZFLR 378 ("*Elledge*").

272 Property (Relationships) Act 1976, s 10(4).

273 *Keats v Keats* [2006] NZFLR 403 ("*Keats*").

274 *Hunt v Muollo* [2003] 2 NZLR 322 (CA).

275 *R v R [Occupation Order: Trusts]* [2010] NZFLR 555.

276 At [46].

277 *Keats v Keats* [2006] NZFLR 470.

beneficiaries and the occupation order was declined for the reasons explained in *Hunt v Muollo.*[278]

Judge Burns noted in relation to the *Elledge* case that:[279]

> I accept … the reasoning adopted by Judge Robinson in that judgment that there can be cases where a relationship property interest can be found in property owned by trustees to provide jurisdiction for the Court to make an occupation order, i.e., the trustees hold the property not only pursuant to obligations under the Trust Deed, but in addition hold a beneficiary property interest for one or both parties or the children or one or both parties acquire a beneficial interest. *The situation for Trusts particularly in the context of a marriage or de facto relationship does not remain static after a Trust Deed is signed.* Often the parties continue to behave not only as husband and wife but as trustees, *and with conduct and with change of events that occur during the course of a marriage further rights and obligations can arise which can amount to property.* The question is what type of 'interests' can give rise to the Court having jurisdiction.

Judge Burns considered the meaning of the word 'interest' [280] and he referred to *Armitage v Nurse*[281] where Millett LJ cited Lord Wilberforce in *Leedale (Inspector of Taxes) v Lewis*[282] that word 'interest' is of uncertain meaning and has to be decided on the terms of the relevant statute. Also relying on Tipping J in *Johns v Johns*[283] Judge Burns then found:[284]

> Accordingly, based on the case law there is a spectrum of interests within different trusts. Those interests have been defined as variously rights, powers and property. At one end of the continuum is a mere expectancy which does not provide a property interest. At the other end of the range are a bundle of rights which can be properly identified as relationship property. *Keats v Keats* is an example of one end of the spectrum and *Yung Ping Guo v Elledge* and *Q v Q* are examples along the line of the continuum. Each case will have to be considered on its own merits as to where it

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278 *Hunt v Muollo* [2003] 2 NZLR 322.

279 *R v R* above n 275 at [46] (my emphasis).

280 At [51].

281 *Armitage v Nurse* [1998] CH 241.

282 *Leedale (Inspector of Taxes) v Lewis* [1982] 3 All ER 810 at 816.

283 *Johns v Johns* [2004] 3 NZLR 202.

284 *R v R* above n 275 at [60].

> falls on the continuum, and the law will have to be built up on a case by case basis. I cannot make a definitive general statement of the law.

Judge Burns then identified the relationship property as including:[285] a trustee resolution providing the spouses with a right to occupy the property, a distribution by the trustees to the parties thereby converting a discretionary interest into a property interest; the formation of a partnership between the two trusts and payments made by the partnership, the effective control held by each party by way of power of appointment; the parties are beneficiaries along with their children, a decision to allow the wife and children exclusive occupation of the home, the ownership structure whereby the trust Partnership has passed decision making from the two respective mirror trusts to the partnership where the husband and wife have exercised decision making not only as trustees but also as husband and wife.

It was in these circumstances that the Judge explained the rationale behind the extension of the meaning of 'property' when he said:[286]

> Because trust deeds vary so much it is difficult to generalise about what does or does not constitute relationship property interest in a trust. The variables are also affected by the context in which the property is settled on a trust. The Family Court does get concerned in those circumstances where relationship property is settled on a trust and one party seeks to use the trust as a device in order to try and convert that relationship property into separate property or to retain control. There are specific remedies under the Act, but the Court will be alert to ensuring that no injustice occurs in those circumstances where the property settled was relationship property prior to being settled on a trust.

The next question was whether the parties' interests in the trusts were their separate property.[287] He noted that property acquired from a third person[288] is separate property because the spouse is a beneficiary under a trust settled by a third person. Therefore in circumstances where the parties are settlors and beneficiaries under the trust their interests cannot be separate property. Judge Burns said that the amendments made to the Act were also significant:

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285 At [61].

286 At [63].

287 Property (Relationships) Act 1976 s10.

288 Property (Relationships) Act 1976 s 10(1)(a)(iv).

> It can be seen that the words changed. The important change was the adding of "from a third party"[289]. In my view, this change was important and is consistent with the general scheme of the Act to make a distinction between separate and relationship property. It is intended to capture a distinction between those cases where a party seeks to convert relationship property into separate property by the use of a trust. It also seeks to preserve where the original source of the property was separate, and its status (if not held by a trust) would be separate in any event to preserve that distinction. In this case the property settled on the trust was relationship property. There is a debt back which is also relationship property.

Taking all these matters into account Judge Burns concluded that the trust owned family home relationship property and he made an occupation order in favour of the wife particularly as she needed a home to provide for the children.

Another occupation order case which raises important interpretation issues on the meaning of 'property' and 'owner' is *M v M [Occupation Order]*.[290] In this case the application was for an occupation order under the Domestic Violence Act 1995 on the grounds that either party "owns or … has a legal interest .."[291] in a dwellinghouse.

The question of jurisdiction depended upon the meaning of 'owns.' The DVA has no definition of 'owner' and s 52[292] makes no mention of property but the Court found that when "interpreting the word 'owns' it raises the question of 'owns what'? The only logical answer is the word property."[293]

Unlike the PRA, the DVA definition includes property that a person does not own but "uses or enjoys."[294] Judge Burns found that the court did have jurisdiction to make an occupation order in a situation where the dwellinghouse was owned by a third party trust because:

> The words 'either party to the proceedings' owns or in which has a legal interest, that the Legislature by using the word 'owns' or 'had a legal interest in' intended an expanded definition so that an applicant or respondent does not have to only have legal ownership but it also is extended to use and enjoyment. This must be the case

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289 Property (Relationships) Act 1976 s 10(1)(a).

290 *M v M [Occupation Order]* [2010] NZFLR 746.

291 Domestic Violence Act 1995 s 52 ("DVA").

292 Domestic Violence Act 1995 s 52.

293 *M v M* above n 290 at [35].

294 Domestic Violence Act 1995, s 2.

> otherwise the words 'legal interest' would be redundant. … This expanded definition fits in with the purpose of the Act and the requirement to provide protection for applicants and children.

Consequently, the conventional view that property interests cannot include a discretionary beneficiary's interest in a trust was discarded by accepting that, in the context of the DVA, property interests in discretionary trusts occur as a consequence of the 'use' or 'enjoyment' of the dwellinghouse in question. This is yet another example of an operative conception of property in social legislation aimed at providing protection for applicants and children.

Returning to *R v R [Occupation Order]* the meaning of property depended on the terms of the trust deed, the conduct of the parties during the relationship as well as the degree of control exercised by one or both parties over the management of trust assets. This line of authority in occupation orders illustrates the fluid meaning of property under the PRA but in circumstances where the integrity of the trust fund is not affected by the court's order. Whilst the occupation order does affect the trustee's ability to make decisions regarding the sale of the property, pending final determination of relationship property proceedings, the trust fund is not being distributed or re-allocated and there is no need for those property interests to be valued.

However, before leaving the 'bundle of rights' cases it is important to consider those cases when interests in discretionary trusts may need to be valued.

F Valuation – Interests in Discretionary Trusts

This discussion on the valuation of interests in discretionary trusts is not intended to be an analysis of the meaning of 'value' or the methodologies that have been employed to value tangible and intangible assets under the PRA. Instead the focus remains on the kinds of interests in discretionary trusts that may be given a property status and factors that may need to be considered when valuing those interests.

Assuming that the 'bundle of rights' doctrine create property interests, beyond the valuation principles in *Walker v Walker,*[295] then these rights need to be classified and

[295] *Walker* n 225 above.

valued before there can be a division of relationship property.[296] For the reasons already discussed, this enquiry requires a careful examination of the facts in each case as there will be a 'spectrum' of interests in discretionary trusts which may or may not have a value. For instance on its own a discretionary beneficiary's right to due administration and consideration is so uncertain that it is difficult to envisage any reliable methodology to value such an interest.

At the other end of the spectrum there will be trust deeds which provide that both parties share the power of appointment and are discretionary beneficiaries. In these circumstances it is likely that the parties will use their 'control' to distribute the trust assets between themselves irrespective of the view of any additional trustee. Accordingly, there is no reason to depart from the principle of equal sharing of the trust fund as this flows from their joint control over administration and disposition of the trust's assets.

However, if the trust deed provides that one party retains effective 'control' over the use and enjoyment of the trust assets and on a proper construction of the trust deed is able to appoint all the capital and income to him or herself or the other party[297] then the likelihood that this party will take advantage of the trust structure and appoint some or all of the trust's capital or income raises the issue of valuation of that 'controlling' interest. This necessarily gives rise to a theoretical valuation for relationship property purposes.

The foundation of conventional valuation principles is to ascertain a "value at which a willing not but anxious vendor would sell and a willing but not anxious purchaser would buy."[298] However, the valuation of assets for those in qualifying relationships can arise where there is no market for the asset in question. As the Court of Appeal stated in *Z v Z (No 2)* when considering theoretical valuations [299]

> It may be that there will be great difficulty in arriving at a value but that does not mean that there is none. In the end the assessment must be approached as a jury question with the assistance of the best evidence available.

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296 Property (Relationships) Act 1976 s 2G and s 20D.

297 See the discussion at chapter 4 *Kennon v Spry* above n 162 at [62] French CJ.

298 *Hatrick v CIR* [1963] NZLR 641, 661 (CA).

299 *Z v Z (No.2)* [1997] 2 NZLR 258 at p 289.(CA).

Similar uncertainty and difficulty arises over the factors that need to be brought into account when assessing a compensation payment for economic disparity,[300] as well as contingent events that may or may not occur in the valuation of superannuation entitlements[301] such as widow's benefit[302] which may have considerable value if a party subsequently remarries.

In *Z v Z (No.2)*[303] the Court of Appeal acknowledged that as a consequence of the partnership deed the husband did not have a proprietary interest in the partnership's capital but nevertheless his membership of the firm gave him enhanced benefits which flowed from his membership of the partnership. This approach has been adapted in the *Walker* valuation model of the debts owed by the trust to the parties. The parties did not have a proprietary interest in the trust's assets but their 'control' gave them enhanced benefits which flow from the "six items of property forming the package." [304]

In theoretical valuations the courts have relied on well established principles such as an "approach akin to that identifying super profits,"[305] adjustments for future contingencies such as life expectancy, medical disablement, loss of employment and the like [306] to reach a value of the particular asset which accords with the principles and purposes of the PRA. Similarly the enhanced benefits approach could be adapted to the 'bundle of rights' cases.

The following are some factors which could be considered by the Court when making its jury assessment of the party's controlling interest: the settlor's intentions, the number and types of beneficiaries, the way in which dispositive powers have been exercised in the past, the relationship between the holder of the power to 'hire and fire' trustees with other trustees, the history of the management of the trust, the value of the trust fund, the financial circumstances of the party who has effective 'control' of the trust as well as the other party together with any dependent beneficiaries.

Unfortunately, there is little or no guidance that can be found in other jurisdictions. The Australian cases do not assist because the FLA enables the court to "alter the interests of

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300 Property (Relationships) Act 1976 s 15.

301 *Haldane v Haldane* [1981] 1 NZLR 554 (CA).

302 *Walkinshaw v Walkinshaw* (1992) 9 FRNZ 18 (HC).

303 *Z v Z (No.2)* above n 299 at p 290-291.

304 *Walker* above n 224 at [60] Chambers J.

305 *Z v Z (No 2)* above n 299 at p 131.

306 *Haldane v Haldane* above n 301.

the parties to the marriage in the property …"[307] and the valuation of such interests is not as critical as it is in New Zealand PRA cases.

In Canada case authorities discuss three possible methods of determining value. The courts can use an "if and when" approach[308] as to when the prejudiced party receives their share of the capital distribution by delaying it until the other party receives their capital or income distribution. In one case the court took a notional pro rata distribution of the value of the trust fund depending upon the number of capital beneficiaries.[309] The court can also examine the purpose of the trust to see if the other discretionary beneficiaries are likely to receive a distribution and if so how much.[310]

The first and second approaches are too problematic to be applied in New Zealand. The PRA does not lend itself easily to an "if and when" approach because it is inconsistent with the 'clean break' principles and purposes of the PRA.[311] The pro rata approach has been criticised and likened to a lottery ticket[312] and does not address the 'control' issues discussed above whereas the third approach is closer to the way in which the valuation exercise could be framed in 'bundle of rights' cases.

In conclusion, provided there is a full enquiry into the proper construction of the trust deed and assessment of the degree of 'control' exercised by one or both parties then it should be possible to adapt well established valuation methodologies to value controlling interests in discretionary trusts.

G Enforcement – Judicious Encouragement?

Having traversed the possibility that a 'bundle of rights' in a discretionary trust can be valuable property the residual question of payment still needs to be addressed. Again much will depend on the facts of each case. In situations where there are mirror[313] or

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307 Family Law Act 1975 s 79(1)(a).

308 *Da Costa v Da Costa* (1992) 7 OR (3d) 321 and referred to by Shelley Griffiths "Valuation of interests in discretionary trusts" NZLS Relationship Property Intensive – your big (legal) day out! August 2010 at p 62.

309 *Sagl v Sagl* (1997) 31 RFL (4th) 405 (Ont. Gen. Div).

310 *Kachur v Kachur* (2000) ABQB 709 (Alta. Q.B.).

311 Property (Relationships) Act 1976 s 1M(c) and s 1N(d).

312 "Valuation of interests in discretionary trusts" above n 308 at p 63.

313 *R v R [Occupation Order]* above n 275.

parallel trusts the division of the trusts' assets has largely occurred as a consequence of the trust structures. In the *Walker* debt-back valuation cases ancillary orders could be used, in conjunction with the PRA's compensation provisions[314] to vary a trust to enable payment to the disadvantaged party.[315]

However in those difficult cases where there is little or no property available for division and the trust does not generate an income[316] there is no jurisdiction under the PRA for the court to order trustees to make a capital distribution to satisfy any judgment debt. This does not mean that the judgment will be ineffective as the party who has been ordered to pay then has the responsibility to satisfy the judgment debt. The court can order payment in one lump sum or by instalments as well as include the payment of interest with or without security.[317] Failure to comply also exposes the defaulting party to the possibility of bankruptcy.

Some guidance can be found in case authorities from the United Kingdom. Their Act [318] applies the sharing principle to all property which may include discretionary trust interests as a 'financial resource'[319] of a spouse. Judges often regard discretionary trusts as devices to hide or obscure assets and their approach tends to be robust by treating trust assets as available to the settlor spouse.[320] Nevertheless the court has no power to make orders against the trustees directly but they will make an order against a beneficiary "[i]n the knowledge that it cannot be satisfied without recourse to trust assets. The assumption is that the trustees will go to the aid of the beneficiary as they are unlikely to stand by and allow the beneficiary to go to prison for contempt of court or face bankruptcy proceedings."[321] This has been referred to as "judicious encouragement."[322]

In *Thomas v Thomas* Waite L J said: [323]

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314 Property (Relationships) Act 1976 s 44C which is discussed in detail at chapter 5.

315 *MGS v BFM* FC Tauranga, 16th November 2006, FAM 2004-070-823 Judge Somerville.

316 Property (Relationships) Act 1976 s 44C(2)(c).

317 Property (Relationships) Act 1976 s 33(4).

318 Matrimonial Causes Act 1973.

319 At 25(2)(a).

320 William Massey "Threats to the Integrity of Trusts on Marriage Breakdown" IFLJ 2008 (18) at p3.

321 At p 4.

322 For instance this principle was applied in *Charman v Charman* [2007] 2 FCR 217 (CA (Civ Div)) which involved an off-shore trust and the husband was ordered to pay the wife £48 million.

323 *Thomas v Thomas* [1995] 2 FLR 668 at p 670.

> …where a spouse enjoys access to wealth but no absolute entitlement to it (as in the case, for example, of a beneficiary under a discretionary trust or someone who is dependent on the generosity of a relative) the court will not act in direct invasion of the rights of, or usurp the discretion exercisable by, a third party. Nor will it put upon a third party undue pressure to act in a way which will enhance the means of the maintaining spouse. This does not, however mean that the court acts in total disregard of the potential availability of wealth from sources owned or administered by others. There will be occasions when it becomes permissible for a judge deliberately to frame his orders in a form which affords judicious encouragement to third parties to provide the maintaining spouse with the means to comply with the court's view of the justice of the case. There are bound to be instances where the boundary between improper pressure and judicious encouragement proves to be a fine one and it will require attention to the particular circumstances of each case to see whether it has been crossed.

Such an approach could be applied in New Zealand as it does not affect the integrity of the trust but at the same time recognises that wealth that has been accumulated during a qualifying relationship should be made available to a party to settle their relationship property obligations.

The next chapter considers the PRA's response to the disposition of relationship property to a discretionary trust and where the 'bundle of rights' principles fits within the existing statutory framework.

VI Compensation, Setting Aside Dispositions, Resettlement of Trusts and Other Judicial Responses to the Use of Trusts

A Background

The emergence of the 'bundle of rights' doctrine is largely a response to the inadequacies of the statutory provisions that deal with the disposition of relationship property into discretionary trusts. As Peart has commented on a number of occasions there is an urgent need for reform[324] as "the Act's aim of achieving an equal division of the fruits of the partnership is severely undermined by trusts"[325]. Reform may be some years away and in the meantime courts need to work within the statutory framework.

The Court of Appeal in *M v B*[326] emphasised that the courts do not have an "open-ended discretion to achieve equality in accordance with an individual Judge's perception of what is fair and just" nor does it have a "generalised mandate which can avoid or obscure the structural framework which Parliament adopted" and whilst "… [t]he underlying philosophy and inspiration is always to be considered … [the] operational ambit must be evaluated within the particular statutory responses which Parliament has enacted. They do not permit Courts to go further than Parliament was willing to legislate for."[327]

This chapter briefly considers the framework Parliament has provided to protect spouses and partners from dispositions of relationship property to trusts.[328] This regime incorporates the following features which allow a spouse or de facto partner to:

- register a notice of claim of an interest under the Land Transfer Act 1952 to prevent the transfer of real estate to a trust;[329]
- restrain the disposition of property to a trust;[330]
- apply to the court to set aside a disposition of relationship property to a trust if it was done to defeat a claim or right under the Act;[331]

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324 *Equity and Trusts in New Zealand* above n 24 at [41.2.4 (4)].

325 "Relationship property and trusts" above n 46 at p 23.

326 *M v B [economic disparity]* 25 FRNZ 171(CA)

327 At [32] – [34] Robertson J.

328 Property (Relationships) Act 1976 s 42-44 applies to other types of disposition not just to trusts.

329 Property (Relationships) Act 1976 s 42.

330 Property (Relationships) Act 1976 s 43.

331 Property (Relationships) Act 1976 s 44.

- seek compensation if there has been a disposition of relationship property to a trust which has the effect of defeating a claim or right under the Act.[332]

In circumstances where a party is aware of the likelihood that property is going to be transferred or disposed of into a trust the PRA provides adequate protection. However, once the disposition of relationship property has taken place, and the parties then separate or the relationship ends in death, the safeguards are often inadequate.

B Setting Aside Disposition to a Trust

If the disposition has taken place then s 44 enables the courts to set it aside if it is satisfied that:[333]

> … any disposition of property has been made, whether for value of not, by or on behalf of or by direction of or in the interests of any person in order to defeat the claim or rights of any person under this Act …

A similar provision existed under the previous Act[334] but the Court of Appeal in *Coles v Coles*[335] held that an applicant had to prove that his or her spouse had a conscious desire to remove items of matrimonial property from the reach of the court. Therefore there had to be some improper action designed to deprive a spouse of property rights and there was no distinction between the purpose of the disposition and the transferor's intent. The threshold for proving that a party intended to defeat the other party's claim or rights was high and the section largely fell into disuse.

Recently the Supreme Court in *Regal Castings v Lightbody*[336] placed a broader interpretation on the meaning of the phrase "intent to defraud" in the context of a debtor/creditor relationship. Blanchard J said:[337]

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332 Property (Relationships) Act 1976 s 44C.

333 Property (Relationships) Act 1976 s 44 gives jurisdiction to the High Court, District Court and Family Court.

334 Matrimonial Property Act 1976, s 47.

335 *Coles v Coles* (1987) 3 FRNZ 101 at p 105.

336 *Regal Castings Ltd v Lightbody* [2009] 2 NZLR 433 (SCNZ) ("Regal Castings").

337 At [53]–[56].

> Whenever the circumstances are such that the debtor must have known that in alienating property, and thereby hindering, delaying or defeating creditors' recourse to that property, he or she was exposing them to a significantly enhanced risk of not recovering the amounts owing to them, then the debtor must be taken to have intended this consequence, even if it was not actually the debtor's wish to cause them loss …

Subsequently, the High Court in a relationship property case applied the principles from *Regal Castings* and in *Ryan v Unkovich*[338] French J held:

> Further I accept the principles enunciated in *Regal Castings* are sufficiently general to apply to s 44. In particular, I accept that in so far as the *Coles* formula fails to distinguish between intention and motive, it is contrary to the reasoning of the Supreme Court and should not be followed. Knowledge of a consequence can be equated with an intention to bring it about.

French J also held that the Court had jurisdiction to set aside dispositions before the Act came into effect on 1st February 2002 in circumstances where there is knowledge that consequence of defeating a relationship property claim.[339]

Whilst these recent decisions open the door to the possibility of setting aside a disposition to a trust, the onus of proof remains on the applicant and the evidential threshold to prove knowledge of the likely consequence remains problematic for a number of reasons. There are many reasons why trusts are settled including estate planning, creditor protection, social assistance policies such as residential care subsidies as well as minimisation of income tax liabilities. At the time of the disposition there may be no reason for a party in a qualifying relationship to consider or discuss the relationship property implications for the disposition of assets to a trust. Trust advisers come from a diverse background and even if they are lawyers it does not necessarily mean that they have the requisite legal knowledge to explain the relationship property consequences.

There are other factors which also limit the scope of this provision as the parties must have been in a qualifying relationship at the time of the disposition[340] and it must be a

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338 *Ryan v Unkovich* [2010] 1 NZLR 434 at [33] (*"Ryan").*

339 At [40] and [42].

340 At [38] also referring to *Genc v Genc* (2006) 26 FRNZ 67.

disposition of relationship property.[341] The court's jurisdiction is further curtailed if the recipient receives the property or interest for value, "in good faith" and has altered his or her position in reliance of having an "indefeasible interest" in the property and/or it would be inequitable to grant relief.[342] However, if a spouse or partner is a trustee then that person's knowledge is imputed to the other trustees.[343]

Even if the disposition has been made "otherwise than in good faith"[344] to a third party for inadequate consideration, the court has a discretion to transfer "any part"[345] of that property or direct that a sum "not exceeding the difference between the value of the consideration (if any) and the value of the property"[346] be paid and consequently that does not necessarily mean that full value of the property is returned to the relationship property pool.

C Compensation for Dispositions to a Trust

Concerns that discretionary trusts are being used to side step the principles and purposes of the PRA have been around for over 23 years. In 1988 the Labour Government established a Ministerial Working Group to update the then Matrimonial Property Act 1976. The Working Group identified discretionary trusts as a problem[347] because they removed property from the equal sharing regime. Their recommendation was to allow Courts the power to distribute capital from the trust or claw back specific assets into the matrimonial property pool.

Parliament decided not to go down that path and instead opted for a regime whereby the court could either compensate a disadvantaged spouse or partner from other property and

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341 *Equity and Trusts* above n 24 at [41.2.4(1)] referring to *JCW v FKW* FC Auckland, 15/3/05, FP 004/935/01 Judge Mather.

342 Property (Relationships) Act 1976 s 44(4).

343 *Regal Castings* above n 336 at [128] Tipping J. Note this would have assisted the applicant in *O v S* (2006) 26 FRNZ 440 (FC) where the requisite knowledge was established but the claim failed on the basis of a lack of knowledge by the co-trustees.

344 Property (Relationships) Act 1976 s 44(2)(a).

345 Property (Relationships) Act 1976 s 44(2)(a).

346 Property (Relationships) Act 1976 s 44(2)(b).

347 *Report of the Working Group on Matrimonial Property and Family Protection* Wellington (1988) at 30.

as a last resort from trust income.[348] The Government Administration Committee explained the reason as follows:[349]

> This acknowledges that trusts are created for legitimate reasons and should be permitted to fulfil that purpose, where there was no intention to defeat the spouse's claim at the time the trust was established. Bona fide third party interests are protected.

To qualify for compensation a spouse or partner's claim must meet the following criteria:

(a) There must be a qualifying disposition. Although the term 'disposition' is not defined in the Act it has been held to cover any form of alienation of a legal or equitable interest in property whether for value or not.[350] However, rental payments for the use of a home are not dispositions within the meaning of s 44C.[351]

(b) The disposition must be to an inter vivos trust and not one established by a will or other testamentary disposition.[352]

(c) There must be a disposition must be of relationship property. Consequently, if at the date of disposition the trust acquires an asset by borrowing from one spouse's separate property then there has been no disposition of relationship property. The subsequent use of the property as a family home does not convert the disposition to relationship property.[353] Consequently, the classification takes place at the date of disposition.

(d) The disposition must occur after the commencement of the marriage or de facto relationship.[354]

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348 Property (Relationships) Act 1976, s 44C.

349 Government Administration Committee Report on Matrimonial Property Amendment Bill 1998, 109-2 at xii.

350 *Re Polkinghorne Trust* [1988] 4 NZFLR 756.

351 *Kidd van den Brink* HC Auckland, 1/7/08, CIV-2007-404-6948 Stevens J.

352 Property (Relationships) Act 1976 s 44A.

353 Property (Relationships) Act 1976 s 44C(1)(a) and *P v B* [Relationship Property] [2009] NZFLR 773 (HC).

354 Property (Relationships) Act 1976 s 44C(1)(a).

(e) The disposition must be made by either or both spouses or partners[355]. Therefore neither dispositions by third parties nor if the trust acquires property directly from a third party qualify.[356]

(f) The disposition must be one that has the effect of defeating the claim or rights of one of the spouses or partners.[357] Consequently, if both parties are equally affected by the disposition then neither can invoke s 44C.[358]

(g) The relevant date for assessing the effect of the disposition is generally the date of hearing. The Court of Appeal in *Nation v Nation*[359] said:[360]

> As to the date at which the effect of the disposition is to be assessed, in our view that should be as at the date of hearing. That is the general rule as to the date at which the value of property is to be determined under s 2G of the PRA. It is true that the Court has a discretion to determine the value at another date. However there appear to us to be no discretionary factors which, in this instance, would militate against the application of the usual rule.

Finally, the disposition cannot be one which is caught by s 44[361] of the Act.

The cases have considered a variety of dispositions by a spouse or partner to a trust including: the sale of trustees of the family home, a rental property, a farm, company shares, the payment of mortgage instalments and the forgiveness of debts back. Similarly if relationship income has been used to pay a mortgage on a trust property or if relationship property has been used as security for a loan taken out by the trust[362] they will qualify as dispositions which trigger the discretion to grant compensation.

If a party has a qualifying claim for compensation then the court has a discretion to order compensation out of relationship or separate property[363]. If neither of these sources are

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355 Property (Relationships) Act 1976 s 44C(1)(a).

356 *Genc v Genc* [2006] NZFLR 1119.

357 Property (Relationships) Act 1976 s 44C(1)(b).

358 *P v P* [2005] NZFLR 689 at [96].

359 *Nation v Nation* [2005] 3 NZLR 46.

360 At [150].

361 See discussion above at page 79 – 81 above.

362 *Equity and Trusts* above n 24 at [41.2.4(2)(a)].

363 Property (Relationships) Act 1976 s 44C(2)(a)

sufficient to meet the quantum of compensation then the court may require the trustees to pay trust income either for a specified period of time or until the specified amount has been paid.[364] However, the court cannot require the trustees to pay trust income in circumstances where a third person in "good faith" has altered his or her position and is relying upon receipt of the trust's income.[365]

The court in exercising its discretion to award compensation has to consider the value of relationship property disposed of to the trust, the value of relationship property available for division, the date when relationship property was disposed of to the trust, whether the trust gave consideration for the property, the other beneficiaries of the trust and any other relevant matter.[366]

In *IRM v SJB*[367] the Court applied a formula where the current value of the property was taken and from that sum there were deductions for debts incurred in the acquisition of the trust property, the nett balance was then divided in half and that sum was to be paid to Mr M out of the relationship debt owed by the trust to Ms B.

Whilst the courts can require trustees to pay income to the dispossessed party, many family trusts produce no income as the trust fund comprises the ownership of assets such as the family home. Although the courts do have an ancillary power to vary the terms of a trust[368] it can only do so when making a substantive order under the Act.[369] Consequently, if there is no property and the trust cannot generate income then there is nothing the court can do to vary the terms of the trust.

However, if the court can order compensation then s 33(3)(m) could be used to change the vesting date[370], direct trustees to sell trust property and repay a debt to the spouse or partner[371], or appoint the dispossessed party as a beneficiary of the trust, or restrict or suspend the respondent's entitlement to benefit under the trust.

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364 Property (Relationships) Act 1976 s 44C(2)(c).

365 Property (Relationships) Act 1976 s 44C(3).

366 Property (Relationships) Act 1976 s 44C(4).

367 *IRM v SJB* FC, Wellington, 24 March 2010, FAM-2007-085-10 subsequently upheld on appeal *SJB v IRM* HC Wellington, 4 November 2010, CIV 2010-485-710, Simon France J.

368 Property (Relationships) Act 1976 s 33(3)(m).

369 *Equity and Trusts* above n 24 at [41.2.4(3)].

370 *PGD v IGD* FC Wellington, 2/8/05, FAM-2000-085-2601, Judge V Ullrich QC.

371 *MGS v BFM* FC Tauranga, 16/11/06, FAM-2004-070-823, Judge Somerville.

For the reasons already discussed s 44C is ineffective where there is an insufficient pool of relationship or separate property. This situation is likely to be exacerbated when gift duty is abolished in October 2011 when spouses or partners can gift the entire debt-back to the trust[372] as that will further diminish the pool of property available for division.

D Section 182 Family Proceedings Act 1980

In a different statutory setting and isolated from the relationship property regime a disadvantaged spouse or civil union partner can apply to the court for orders to vary the terms of ante-nuptial and post-nuptial settlements[373] when, or shortly after, the dissolution of a marriage or civil union. However, the remedy is not available to de facto partners.

Further this is not a general remedy to be used with reference to concepts of "fairness and justice,"[374] nor is the discretion based on the principles of equal sharing under the Act[375] or a "surrogate mechanism for dividing what, but for the trust, would have been relationship property."[376] The Court of Appeal has stated that s 182 is not a "trust busting route"[377] into the PRA.

Recently the Supreme Court considered the way in which the jurisdiction under s 182 should be exercised and in *Ward v Ward* held:[378]

> Based on the foregoing discussion we consider the proper way to address whether an order should be made under s 182 is to identify all relevant expectations which the parties, and in particular the applicant party, had of the settlement at the time it was made. Those expectations which the parties, and in particular the applicant party, have of the settlement in the changed circumstances brought about by the dissolution. The court's task is to assess how best in the changed circumstances the reasonable expectations the applicant had of the settlement should now be fulfilled.

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372 See the discussion at Chapter 5 paragraph D.

373 Family Proceedings Act 1980 s 182.

374 *W v W* [2009] 3 NZLR 336 at [49] (CA).

375 Fisher on Matrimonial and Relationship Property, Loose-leaf, para [6.14].

376 *Ward v Ward* [2009] 2 NZLR 31 (SCNZ) at [49].

377 *X v X* [2009] NZFLR 956 at [44]–[45].

378 *Ward v Ward* above n 376 at [25].

> If the dissolution has not affected the implementation of the applicant's previous expectations, there will be no call for an order.

Further s 182(3) provides that the comparison of changes in circumstances needs to be made at the time of the settlement and at the time of dissolution of the marriage or civil union.

Whilst the position with post-nuptial settlements presupposes an entitlement to apply for a variation of the trust, the position with ante-nuptial settlements is different. In *Kidd v van den Brink*[379] the High Court held that there had to be a "degree of connection or proximity between the settlement (not the settled property) and the particular marriage"[380] and that nuptial character will not exist if the future spouse is only one of a class of possible beneficiaries. The applicant then sought leave to appeal to the Court of Appeal[381] and whilst leave was granted on other grounds William Young P said that leave would not be granted on the ante-nuptial settlement argument because the Supreme Court in *Ward v Ward* [382] applied s 182 in line with established English authority that a nuptial settlement requires a particular marriage in mind.

The ground that the Court of Appeal did grant leave was whether "dispositions to the trust made during the currency of the marriage engage s 182 as post-nuptial settlements."[383] The Court of Appeal then indicated that it may follow the reasoning of Kiefel J in *Kennon v Spry*[384] that:[385]

> There appears to be no reason why each disposition of property to the trust, from the time of the parties' marriage, cannot be viewed as a separate trust created at that time, albeit on the terms of the trust.

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379 *Kidd v ven den Brink & Anor* HC Auckland, 21 December 2009, CIV Harrison and Winkelmann JJ.

380 At [18].

381 *Kidd v ven den Brink* [2010] NZCA 169 (CA).

382 *Ward v Ward* above n 376.

383 *Kidd v ven den Brink* above n 381 at [10].

384 *Kennon v Spry* (2008) 251 ALR 257 (HCA).

385 At [209] Kiefel J.

However, the case has now settled[386] and this is an issue, of considerable significance, which will need to be considered by the Court of Appeal on another occasion because on current High Court authority the 'multi trust' theory has been rejected.

E Judicial Responses in Other Cases

In cases which do not engage either the PRA or the Family Proceedings Act, the courts have considered discretionary trusts where a party has effective 'control' of the administration and disposition of trust assets. The validity of these trusts has been challenged on the basis that the trust is a sham or the *alter ego* of the settlor. The concept of *alter ego* trusts has also been applied in some constructive trust cases. All of these judicial responses require examination.

1 Shams and alter ego trusts

Whether trust assets are within the grasp of the court's jurisdiction has been the subject of intense scrutiny not only in family law but also by creditors. There have been lively debates about the possibility that many discretionary trusts with wide dispositive powers should be declared invalid as being a sham.[387] The Australian concept of the *alter ego* trust has been pulled into the debate as a means of disregarding the trust[388] or as part of the grounds to establish a constructive trust.

However, the Court of Appeal in *Official Assignee v Wilson & Anor*[389] largely extinguished these possibilities when it found that a trust 'controlled' by a person who was neither a trustee nor beneficiary was not a sham. The court adopted the traditional view[390] that both settlor and trustees have to have a common intention, at the time of inception, not to create the legal rights and obligations of a trust relationship. This creates a very high evidential threshold for a third party claimant. The Court of Appeal also rejected the concept of an 'emerging sham' on the basis that once a valid trust was

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386 Law Commission Issues Paper above n 3 at [3.37].

387 *Begum v Ali* FC Auckland, 10/12/04, FP004/128/00 Judge O'Donovan and was upheld on appeal in *A v B* HC Auckland, 1/6/05, CIV-2005-404-496 Rodney Hansen J.

388 *C v C (No 2)* [2006] NZFLR 908 (FC).

389 *Official Assignee v Wilson & Anor* [2008] 3 NZLR 45 (CA) ("Wilson's case").

390 *Snook v London & West Riding Investments Ltd* [1967] 1 All ER 518 at 528.

created it could not be undone "unless the later appearance of a sham can be traced back to the creation of the trust, the trust remains valid."[391]

Correspondingly the enthusiasm for the development of an alternative cause of action being the *alter ego* trust was dampened in *Wilson's* case when the Court of Appeal held that it was not an alternative doctrine that could be applied to 'bust' trusts. Robertson and O'Regan JJ rejected the concept by concluding:[392]

> [t]he assumption of factual control by someone other than a trustee … or by someone without legal right to exercise such power cannot of itself invalidate a trust … Actual control alone .. cannot be sufficient to extinguish the rights of the beneficiaries …

Yet, the position with *alter ego* trusts in relationship property cases remains unclear because Glazebrook J[393] left open the possibility that an *alter ego* trust which is not a sham

> …can be treated as the property of the individual involved for the purposes, for example, of a relationship property division.

And then went on to say:[394]

> I agree that the trust could not be looked through and that the trust assets themselves would not be available for division. It may be, however, that the trust property could nevertheless be treated as an asset of the individual involved and the other party awarded a larger share of the other available assets. Whether this approach is contrary to the legislative intent as manifested in the Property (Relationships) Act 1976, as suggested by Peart … would, however need to be considered. Section 182 of the Family Proceedings Act 1980 may also be relevant.

This is an indication from the Court of Appeal that some interests in discretionary trusts may be given property status in proceedings under the PRA. As the development of the principles of *alter ego* trusts in family law largely originates from Australia, the courts

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391 *Wilson's case* above n 387 at [57].

392 At [69]–[70] Robertson and O'Regan JJ.

393 At [128] Glazebrook J.

394 At [129].

are likely to derive assistance from the Australian cases culminating in *Spry.*[395] It is also an indication that the courts are increasingly looking at an expansive meaning of property which runs across orthodox trust principles. That does not mean the trust would collapse because the courts do not have access to the trust capital but they would still be able to order the 'controller' to pay a sum to satisfy the disadvantaged spouse or partner's relationship property claims.

The concept of *alter ego* trusts will not be available as a general cause of action in other jurisdictions such as claims by third party creditors and this is a further indication that the meaning of property under the PRA is being developed in a way that marks the special nature of this social legislation.

Under the PRA concepts such as *alter ego* trusts and the doctrine of the 'bundle of rights' then become almost interchangeable because both rest on the principle that property interests can be declared to exist in those discretionary trusts which are effectively 'controlled' by a spouse or partner. The courts can take into consideration wealth that has been generated during the relationship, exclude wealth from third party or pre-relationship sources and fashion orders that are capable of enforcement or at least provide 'judicious encouragement' to trustees to comply with the courts view of the justice of the case.[396]

2 Constructive trust claims

This discussion would not be complete without briefly considering the position of a de facto partner at the end of the relationship when the PRA does not apply.[397] This group of claimants cannot seek a variation of the trust under s 182 as there are no nuptial settlements.[398]

Prior to *Wilson's* case the High Court adapted the *alter ego* trust principle in constructive trust claims. The constructive trust is imposed upon property owned by an express trust on the principles of *Lankow v Rose.*[399] An applicant needs to show direct or indirect

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395 *Kennon v Spry* above n 162.

396 See chapter 5 – valuation of interests in discretionary trusts and enforcement at pages 72-77.

397 Either because the de facto relationship ended before 1st February 2002, or there were no dispositions of property which could fall with s 44 and s 44C.

398 See pages 85-86 above and the discussion on variation and resettlement of trusts.

399 *Lankow v Rose* [1995] 1 NZLR 277 (CA) and adopting the approach of Tipping J at 294.

contributions to the property in question, a reasonable expectation of an interest in the property and the defendants should then reasonably yield the claimant an interest in that property. The *alter ego* principles are then applied to the parties' reasonable expectations of the applicant's interest in the trust assets. In *Prime v Hardie*[400] Salmon J explained the position in this way:[401]

> I accept that the plaintiff did have an expectation of an interest in the family home and, that despite the fact that it is owned by a trust, that expectation was a reasonable one. It was reasonable because the home was treated as though it was owned by the first defendant … I consider the trust can reasonably expect to yield the claimant an interest in the family home.

In that case the de facto partner did have an interest in the family home but not the rental properties.[402] In *Glass v Hughey*[403] a de facto partner established a constructive trust against business assets owned by a trust but on the basis that she had made contributions both direct and indirect to the business. Priestley J found that the husband retained effective control over the trust's shareholding in the company and held that:[404]

> [t]he trust for all intents and purposes [has] been disregarded by the husband so far as his operation of International is concerned and, so far as the wife's claim is concerned should be regarded as a sham or more particularly the husband's alter ego.

Since *Wilson's* case the concept of an *alter ego* in a potential constructive trust claim was raised in *F v W*[405] when Gendall J dismissed the possibility of a sham but said that "the trust was the *alter ego* of Mr F."[406] Consequently Gendall J held that if the disadvantaged partner cannot establish that certain items are relationship property then a constructive trust claims based on the approach in *Prime v Hardie*[407] or *O v S*[408]is still available.

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400 *Prime v Hardie* [2003] NZFLR 481 (HC) Salmon J.

401 At [33].

402 At [34].

403 *Glass v Hughey* [2003] NZFLR 865 (HC) Priestley J.

404 At [89].

405 *F v W* 3 August 2009, HC Wellington, 3 August 2009, CIV-2009-485-531, Gendall J.

406 At [37].

407 *Prime v Hardie* above n 400.

408 *O v S* (2006) 26 FRNZ 440 (FC) Judge O'Dwyer.

VII Evaluation and Criticisms of the 'Bundle of Rights' Theory

For reasons discussed in chapters 4 and 5 the doctrinal basis for concepts such as *alter ego* trusts and more recently the 'bundle of rights' remains highly controversial on both sides of the Tasman.

Whilst the High Court of Australia has settled on an expansive meaning of property under the FLA it has been at the expense of settled principles in trust and fiduciary law. The outcome of decisions such as *Spry*[409] has been to declare discretionary trusts ineffective against third party spousal claims in circumstances where the trustee's power of selection is controlled either by a spouse who is a beneficiary or an appointor. The entire trust fund can then be declared to be the property of the spouse. It would be trite to say that there is considerable disquiet as to whether discretionary trusts can or should be looked through in this way.

In New Zealand, the debate is more recent and also sits in a different family property and statutory regime. The 2001 amendments to the PRA do not allow the courts to walk through trusts and re-distribute its assets to a disadvantaged spouse or partner. The Supreme Court[410] also confirmed the view that Parliament's purpose is to protect trust capital over relationship property rights.

Although it may appear a fine line, it is the writer's view that the way the Court of Appeal applied the concept of a 'bundle of rights' to the valuation of a debt owed to the parties in *Walker*[411] did no damage to the integrity of the trust. Instead, it built on the valuation principles in *Z v Z (No 2)* but in a different context. Similarly the occupation order cases[412] referred to in chapter 5 do not look through the trust or affect the trust fund.

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409 *Kennon v Spry* above n 162.

410 *Ward v Ward* above n 376 but this case involved an interpretation of s 182 Family Proceedings Act 1980.

411 *Walker v Walker* above n 225.

412 *R v R* above n 275 and *M v M* above n 290.

A Lack of Jurisprudential Debate and Explanation

In New Zealand a major criticism of the concept of a 'bundle of rights' is that it has emerged with a "lack of jurisprudential debate and explanation."[413] Undoubtedly such criticisms are justified because the term was first discussed by the Court of Appeal in 1997 in the context of the valuation of a spouse's interest in a law partnership[414] but it was no until 2006[415] that the concept arose in the context of trusts and then applied by the Court of Appeal in 2007[416] but with limited explanation.

No statutory guidance has been given to explain how and why the definition of property under the Act had been expanded to include these 'rights' as property. No explanation has been given as to why the law of powers and fiduciary obligations appear to have been disregarded. Further, there appears to be no other overseas jurisdiction which has relied upon a concept of a 'bundle of rights' in this context. The closest analogy that can be made is to the Australian *alter ego* principles which have developed since the early 1980s but only after considerable debate and full arguments before their highest courts.

There is also confusion as to the boundaries of the 'bundle of rights' principles particularly in light of the Court of Appeal's reiteration of the long held view that discretionary beneficiaries have no right to any trust property until an appointment of property is made in their favour.[417] In practical terms the 'bundle of rights' doctrine appears to carve out an exception to the general rule but the line between a mere hope or expectancy and a property interest is uncertain.

Recently the Law Commission commented[418] that the *Walker* decision is unclear as to what is the property in question. Is it the trustee/spouse's rights as a director, shareholder, power to "hire and fire" trustees and directors as well as the parties' discretionary interests considered on an individual basis? Or is it the 'combined package" of all these rights and interests? Or is it the 'control' that the accumulation of the assets gives that is the relevant property? It is the writer's view that the Court of

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413 Anthony Grant "Cradle to Grave: The interface between property and family law" 2010 www.anthony.grant.com.

414 *Z v Z (No.2)* above n 300.

415 *M v B* [2006] 3 NZLR 660 at 112, Robertson J.

416 *Walker v Walker* above n 225.

417 *Gartside v Inland Revenue Commissioners* above n 221, *Hunt v Muollo* above n 201 and *Nation v Nation* above n 204.

418 Law Commission Issues paper above n 3 at [4.39].

Appeal focussed on the 'control' that arises with the "package" of rights and interests but it is accepted that this is only one interpretation.

Another issue is whether the 'bundle of rights' cases are only applicable in a valuation exercise under the PRA[419] or does the principle apply generally in relationship property cases? With the likely abolition of gift duty in October 2011 this could be crucial because debt-backs may be forgiven at the time of settlement of the trust and for existing trusts within 24 hours of gift duty being abolished! If there are no debts to value then the utility of this line of case authority may be lost in applications to determine the extent of property available for division.[420] If the 'bundle of rights' doctrine operates independently to a valuation of a debt then there could be wide ranging possibilities as to its application in family law.

There is also the difficult issue of valuation of a spouse or partner's 'bundle of rights.' On one view once the element of 'control' has been established then the court could take the value of the trust fund as the property to be divided.[421] If that approach was inappropriate then the court could consider the factors discussed in chapter 5 and adapt a methodology for valuing the 'controller's' interest in the trust fund by drawing on the contingent valuation methods in partnership and superannuation cases.[422]

Before, during or after the valuation stage the courts will need to develop principles surrounding the disposition of assets into the trust from mixed sources such as inheritance or pre-relationship property. For instance, the courts may adopt the view of Kiefel J in *Spry*[423] that each disposition of property to the trust creates a separate trust but on the terms of the original trust deed. The 'multi-trust' approach would also give the courts flexibility to differentiate between separate and relationship property.

All of these important questions need to be answered if the doctrine of the 'bundle of rights' is to be understood and consistently applied in the context of relationship property claims. At the moment uncertainty fuels speculation that the doctrine is unprincipled and is a form of law by 'abracadabra' and consequently should not be respected. Yet it is the writer's view that the principles are perfectly well grounded and draw upon a vast body

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419 See the comments made in chapter 5 at pages 72-75.

420 The 'bundle of rights' principles could still be applied in the occupation order line of authority.

421 This was the outcome of *Walker v Walker.*

422 *Z v Z (No 2)* above n 300 and *Haldane v Haldane* above n 301.

423 *Kennon v Spry* above n 162 at [209].

of Australian case law that has slowly developed the meaning of family property in the context of discretionary trusts.

B 'Effective' Control of Discretionary Trusts

In New Zealand the problem of 'settlor control' and the increasing tendency to create *alter ego* or settlor responsive trusts is well known but at least for the last ten years the judicial response, under the PRA, has been muddled as practitioners and judges try to mould solutions out of concepts such as 'shams' which has its origins in commercial contract law or attempting to establish the *alter ego* trust as a separate cause of action available in all trust/third party claim cases or bending the boundaries around the provisions to vary or resettle trust assets[424] by injecting concepts such as equal sharing.

Even practitioners who remain critical of the concept of a 'bundle of rights' have raised concerns that the modern discretionary trust often gives the possessor of powers effective control over the trusts' assets and therefore the 'bundle of rights' concept "… may be another way of explaining that many family trusts are 'insincere' and in effect the settlor or possessor of powers has effective control over the trust's assets and can do with them as he or she likes. Where this is correct, the doctrine deserves respect." [425]

Alternatively, some commentators have expressed concern that judges are being persuaded by family lawyers to 'underplay or to acquiesce'[426] to notions of effective control by disregarding trust principles. That courts should disregard submissions on 'settlor' control rendering a trust ineffective and one commentator suggested that "[i]t is misconduct for counsel to mount a baseless argument."[427] There is no doubt that debate is heated because the doctrine of the 'bundle of rights' raises immensely important issues between the interface of family and trust law.

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424 Family Proceedings Act, 1980 s 182.

425 Anthony Grant "The Bundle of Rights doctrine: Is it good law? (Part 2)" NZ Lawyer 11 December 2009 p 13.

426 J Palmer and S Weil "Beneficiaries rights – the more you get the less you have?" (paper presented to the New Zealand Law Society Trusts Conference, 2009).

427 T Molloy QC "Still more on settler control: the 18th September 2008 reserved decision of New Zealand High Court in *Harrison v Harrison* CIV2008-404-001270" *Trusts & Trustees* Vol 16, No 2, 2 March 2010.

The problems associated with 'control' are seeping into cases in all jurisdictions. For instance in *Isolare Investments v Fetherston*[428] Williams J voiced concerns when he said[429]:

> As mentioned, Mr Langdon said that his and other practitioners, commonplace form of discretionary family trusts now gives trustees very much greater control over trust assets than hitherto. At least as far as the Fetherston Family Trust is concerned, the form of the deed may well be seen as raising the expectations of discretionary beneficiaries, particularly when there is identity between the primary beneficiaries and trustees. Whether, following detailed scrutiny of such changes, the traditional view of beneficiaries' lack of interest in discretionary trust assets will survive remains to be seen. It was not in issue in *Johns* or *Hunt.*

In *RWR v AJR,*[430] a relationship property case, Andrews J rejected a submission, based on orthodox trust principles, that the husband was no better off than his wife as a discretionary beneficiary because:[431]

> … the trust deed gave RWR, as settlor, the power to appoint a new trustee. The trustee appointed by him was a company of which he is the sole director and sole shareholder. The combined effect of those two facts is that RWR has control over the trust.

In Australia and other common law jurisdictions there have been judicial concerns that trusts which are under the effective 'control' of an appointor are not trusts at all.[432] Although these cases arise in different statutory settings the point remains the same that when the evidence establishes that a settlor and/or an appointor treats the assets in the trust as their own then there is a strong argument that trust property may be included in the property of the 'controller'.

There are three aspects of control which need to be considered in the interface between family and trust law. Namely, whether the laws of powers and fiduciary obligations

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428 *Isolare Investments Ltd v Fetherston* HC Auckland, 15/9/06, CIV 2002-404-1791,Williams J.

429 At [51].

430 *RWR v AJR [Trusts]* [2010] NZFLR 82.

431 At [31].

432 A Grant and N Peart "The case for the Spouse or Partner" (a paper presented to the New Zealand Law Society Trusts Conference, June 2009) at 139 and the cases referred to including *Rahman v Chase Trust Company (CI) Ltd & Ors, Re Stephen Moor* (1991) JLR 103, *In the Marriage of Ashton .. In the Marriage of Stein … In the Marriage of Goodwin …*

regulate these types of discretionary trusts? Whether these trusts offend the principle of certainty of intention to create a trust and therefore are not trusts at all? How to ascertain this characteristic of 'control'? All these issues are inter-linked so it is necessary to go back to basics and consider the core values that protect the trust from third party claims.

As discussed in chapter 3 the essential characteristic of a trust rests on the fiduciary relationship between trustee and beneficiary and the rules that regulate the trustee's duty to perform the trusts honestly and in good faith.[433] As Waters explains:[434]

> .. it is also common knowledge that historically Equity courts aimed to enforce the subjective intention of the creator of the express trust. Intent was the foremost judicial concern … Trust law therefore become for the most part – and remains so – an assembly of rules that operate in the absence of intention. It is because this is so that we have the present problem. Default rules suggest to some that there are no limits to otherwise desired express powers. And into the bargain what are the few mandatory rules in trust law is itself arguable.

The common law does permit settlors to reserve certain rights and powers[435] but the problem lies in the boundaries between what is or is not permissible. The modern New Zealand discretionary family trust often provides that the settlor has the power to 'hire and fire'[436] trustees and appoint the settlor as a trustee. This can be done without the need to give reasons and is a powerful way of controlling or at least influencing the trustees in making their decisions. As Waters says there is a perception that discretionary trusts are a more settlor responsive device and consequently[437]:

> My concern is the ambiguity that these powers create in their lessening of the fiduciary obligation of the trustee towards the beneficiary, and of a meaningful beneficiary right to a trustee accounting.

Nevertheless the author concludes that:[438]

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433 *Armitage v Nurse* [1998] Ch 241 at 253-4.

434 Donovan Waters QC "Settlor control – what kind of a problem is it?" *Trusts & Trustees*, Vol 15, 1 March 2009 at p 12 ["Settlor control"].

435 "Settlor control" at p 13 and also referring to The 1985 Hague Trusts Convention, Article 2.

436 At p 13.

437 At p 14.

438 At p 16.

> Sham appears to be the only effective way in which to respond to settlor or third party trust control. But when that cannot be argued, because the instrument confers settlor or third party powers without a trace of settlor dissembling in so doing, trust law is content with fairly general statements about the possible fiduciary nature of the power conferred.

That neatly encapsulates the tension between trust and family law. As a consequence of *Wilson's* case a party has a very high threshold to satisfy before a trust could be declared a sham and effective 'control' is not a ground to invalidate a trust.

Most of the criticisms[439] around using terminology such as effective 'control' of discretionary trusts are that it obfuscates the central tenet that trustees are accountable to their beneficiaries and therefore cannot have 'control' of the trust. If the trustee or appointee breaches their fiduciary obligations the appropriate remedy is to challenge the validity of the disposition as fraud on a power. This is the reason that equity has developed stringent rules restraining the self-interest of trustees and keeps them within the ambit of their power. However, this becomes a circular argument because a trust that is effectively 'controlled' is likely to be one where a fiduciary has wide powers to benefit themselves as well as deny others such as an estranged partner or spouse. Obligations owed to other discretionary beneficiaries are eroded as the trust deed may permit the distribution of the entire trust fund to the 'controller'.

In a family property claim, orthodox accountability depends upon a disadvantaged spouse or partner asking the court to intervene to enforce the trustees' fiduciary obligations when or if the 'controlling' party has misused their trustee office. It presumes that the disadvantaged party will have ongoing access to knowledge surrounding the administration of the trust and the disposition of its assets, after the qualifying relationship has ended. This is extremely unlikely.

It also offends other relationship property principles that recognise the importance that when relationships end and property questions arise under the PRA they should be dealt with inexpensively, simply and speedily as is consistent with justice.[440] This is a further reason why reliance on fiduciary obligations, as a means of protecting the purity of the

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439 W M Patterson "Fog, Resettlements and Fraud on a Power" (paper presented to the New Zealand Law Society Trusts Conference, 2009), A Grant "Effective control sand sham trusts" *NZ Lawyer* (7 August 2009).

440 Property (Relationships) Act 1976, s 1N(c).

trust structure, is unrealistic. It also illustrates that there are different policy reasons to support an expansive meaning of property under the PRA as opposed to other statutes.

Whilst it is possible for a discretionary beneficiary to have access to the Trust Deed and some financial information it is only possible as part of the court's inherent supervisory jurisdiction over trusts[441] or as a consequence of an application for relationship property orders.[442] In the former a discretionary beneficiary may struggle to persuade the court to grant access.[443]

> In many cases the court may have no difficulty in concluding that an applicant with no more than a theoretical possibility of benefit ought not to be granted relief.

Where there are allegations of breach of trust or fiduciary obligations then it has been pointed out that:[444]

> … in situations where the trustee has not observed his core obligations and has indeed acted dishonestly or capriciously, his decision is a breach of trust for which remedies can lie against him. Yet it is near impossible to prove such a breach without accessing the trustee's reasons and trustees are unlikely to accede freely to requests for access for such reasons.

A disadvantaged spouse or partner can apply to the Family Court for disclosure of the Trust Deed and some other documents but that provision is also restricted because it only applies to dispositions of relationship property to a trust and the type of information necessary to establish a party has acted dishonestly or capriciously is completely different and is supervised by the High Court. Consequently, the inability to access trustees' resolutions is a further impediment on holding a reluctant party to account.

As discussed in chapter 3 whilst a breach of trust can be sanctioned by the court and the trustee can be held responsible[445] the threshold required to establish a fraud on a power is

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441 *Schmidt v Rosewood Trust Ltd* [2003] 2 AC 709; adopted in New Zealand in *Foreman v Kingstone* [2004] 1 NZLR 841.

442 Property (Relationships) Act 1976 s 44B.

443 J Palmer & S Weil "Beneficiaries rights – the more you get the less you have?" (a paper presented to the NZLS/CLE Trusts Conference 2009) at p 88 quoting from Lord Walker in *Schmidt v Rosewood Trust Ltd* at [67] above n 439.

444 At p 89.

445 At 89 referring to *Wong v Burt* [2005] 1 NZLR 91 (CA).

not straight forward particularly in situations where there is a mixed purpose and there is evidence of 'appointor control.'

As Grant and Peart[446] have explained the Supreme Court in *Kain v Hutton*[447] appear to sanction 'appointor control' when Blanchard J said that the settlor had "complete ongoing control of the trust" and that control gave her - " … the ability to take the benefit herself or, if she saw fit, to pass all or some of it to her daughters or other family members." In these circumstances a disadvantaged spouse or partner will have difficulty, on orthodox principles, in establishing a fraud on a power. Post separation a disadvantaged party may find the wealth that has accumulated during their relationship is re-settled on to a trust in which not only they are not a beneficiary but also includes new beneficiaries.

Without repeating the discussion in chapter 3, it can be seen that the shield provided to trusts, by the laws on powers and fiduciary obligations, is seriously eroded where a party has effective 'control.' If accountability in these types of discretionary trusts is illusory then that devalues the power of the right of trust law to claim the orthodox view is immune from other competing claims. An expansive meaning of property under the PRA acknowledges society's expectation that wealth created during a qualifying relationship should be available for division between the parties of that relationship. These values are more important and are likely to give 'trumping' power to property claims in family law over trust orthodoxy.

This line of reasoning does not apply to general third party claimants because the core values claimed by discretionary trusts are different to the competing interests of third parties such as creditors. In these circumstances, traditional property rights protect the discretionary trust and have presumptive power over other third party claimants.

C Certainty of Intention

Maybe the real issue with 'control' rests on whether these trust structures fall foul of the elementary proposition that a valid trust in equity requires certainty of intention to separate legal and beneficial ownership from the property in question. As Palmer and Weil observe:[448]

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446 "The case for the spouse or partner" above n 432 at p 138.

447 *Kain v Hutton* above n 64 and see chapter 3 above and discussion on Fraud on a Power.

448 "Beneficiaries rights – the more you get the less you have?" above n 443 at page 80.

> The legal owner of the property cannot then act in relation to the property for his own or for a third party's benefit, but rather only for the benefit of the beneficiaries in whom equitable title to the property rests.

The Law Commission also suggests[449] that the courts could focus on this analysis and invalidate trusts where the settlor "continued to exercise personal dominion over the so-called trust property."[450] Certainly this could be an avenue for the courts to consider but like the 'sham' cases they will depend on their own facts and there will be difficulties in establishing a lack of intention. At present there appear to be no case authorities in New Zealand and for that reason it is difficult to evaluate in the context of family law. However, it is the writer's view that this line of reasoning is on all fours with the Australian *alter ego* principles that beneficiary control creates 'effective' or 'de facto' ownership of the trust's assets and 'effective' ownership is a form of beneficial ownership.

D 'Control' – The Reality Test?

The proposition that a party can 'control' a discretionary trust also exposes the different perspectives taken in trust and family law.

In trust law the presumption that an appointor will exercise a power in good faith and for the end designed is the starting point. Wide dispositive powers in a trust deed cannot point to a situation of 'control' unless or until there is specific evidence that trustees have succumbed to the controller without considering their fiduciary duties. In the absence of such proof courts should not assume the necessary level of 'control' exists.

However in family law, courts are often faced with wide ranging enquiries to discover the extent of relationship property as well as understand the parties' present and future circumstances. The perspective taken by family law is to look at the reality of the parties' circumstances and courts are more inclined to view the trust deed in light of its likely use. Australian case authority developed from the presumption that social reality was the touchstone and not the presumptions afforded by equity.

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449 Law Commission Issues Paper above n 3 at [5.32 to 5.33].

450 At 5.32.

This reality approach may appear to confuse 'control' with the discretions given to trustees. However, equitable presumptions will not sit easily in a Family Court when it is apparent, on the evidence, that a spouse or partner is likely to make self-serving distributions and unlikely to be held to account. It is also instructive to reflect on the events in *Spry* after the High Court of Australia determined the meaning of property. As previously explained Dr Spry refused to comply with the judgment and he then removed approximately $A4.4 million in cash from his daughters' trusts and threatened to burn the money and if necessary go to jail rather than pay his former wife the sums ordered by the court. The daughters and Mrs Spry intervened and retrieved the cash. As the Full Court of the Family Court of Australia said "It does not suggest someone who has much regard to 'equitable orthodoxy'."[451] The original Family Court assessment, that Dr Spry had complete control and was capable of using his powers to distribute the trust's assets in a way that suited his needs, was vindicated.

In New Zealand, it is the writer's view that the enquiry as to whether a party has 'control' over the trust will develop from a social reality perspective and in the ways discussed in *Walker* and *R v R [Occupation Order]* [452] which involves an assessment of the trust deed, whether a party has effective control of the trust, the trustee decisions made during the qualifying relationship together with the likely use of the trust's assets.

E Australian Meaning of Property – Is it Relevant in New Zealand?

There appears to be a view that the Australian approach to both the meaning of property and the *alter ego* trust should not be followed because it sits in an entirely different statutory property regime.[453] It is accepted that there are certain aspects of the *alter ego* line of authorities and the effectiveness of the trust which need to be approached with caution.

However, the one area which is instructive is the interface between the meaning of property and the presumptive power afforded to trust orthodoxy that there cannot be property interests in discretionary trusts. The Australian judicial response has been to give 'trumping' power to the family law claims that *alter ego* trusts create property interests.

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451 *Stephens v Stephens and Anor* (2009) 42 Fam LR 423 at [134] May, Boland and O'Ryan JJ.

452 *R v R [Occupation Order]* above n 275 at [61].

453 "Equity and the Property (Relationships) Act 1976" above n 96 at [41.2.2].

The FLA always gave the courts the option of considering effective 'control' as a financial resource[454] of one of the parties to the marriage. In terms of the structure of the FLA there was no need to expand the meaning of property. However, the inability to make orders affecting a party's financial resources coupled with the injustice of an insufficient property pool led the courts to expand the meaning of property. If the conventional view was to be given presumptive power then the judicial response should have been contained around the treatment of financial resources. The courts may have adopted the United Kingdom approach that fashions orders to give 'judicious encouragement'[455] to trustees to make distributions to satisfy the court's judgment. However the *alter ego* doctrine adopted a different pathway by expanding the meaning of property at the expense of traditional trust principles.

It is for these reasons that Australian case authority is relevant to New Zealand and illustrates the way that an operative conception of property acknowledges that whilst property claims involve conflict and change it is the importance of the underlying social values that matter most.

F Other Options?

Another criticism of the 'bundle of rights' doctrine, in the occupation order line of cases, is that such orders are not necessary and more principled grounds could have been used to reach the same result. For instance, where there are conflicts between trustees, as in the case of *R v R [Occupation Order]*[456] the proper course of action is to apply to the High Court to remove and replace the trustees.[457] However, even if summary judgment is available it is unlikely that replacement trustees could be found quickly and be willing and able to resolve a dispute regarding occupation of the family's principal residence. In the interim the family would be paralysed, the animosity likely to increase and consequently this is likely to be to the detriment of the children of the relationship and probably encourage parties to attempt 'self-help' remedies. Commonly, at the time of separation, issues such as these need to be resolved promptly for the sake of all involved and the Family Court is in the best position to make the assessment as to who is to live in

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454 See discussion at Chapter 4 page.

455 See discussion at Chapter 5 page.

456 *R v R* above n 275.

457 A Grant "The bundle of rights turns trusts to dust" *NZ Lawyer* (5 February 2010).

the home. From a policy perspective it is difficult to argue that these types of situations should be outside the jurisdiction of the court.

Another criticism is that it was not necessary for the Family Court to consider the 'bundle of rights' doctrine on the facts of *R v R* because the trustees' resolution granting the parties a right to occupy the home was likely to be property interest.[458] However, the counter view was argued in *Mv M*[459] that a resolution passed by a trustee does not create a legal or beneficial interest in the land as it is a bare licence to occupy and can be revoked at any time. Whilst courts may be sympathetic to the idea that trusts should not preclude the courts from resolving disputes between parties in a qualifying relationship "the boundaries of the law have to be respected.[460] These observations rest on the premise that until Parliament legislates to reform the Act it is not for the courts to create solutions.

Whilst these lines of reasoning are valid in other statutory contexts they fail to recognise that the PRA is intended to be a code which displaces the rules and presumptions of the common law and equity to property transactions between spouses and partners.[461] Once it is accepted that the property in question is the wealth that has been created during the parties' qualifying relationship then the justifications for reliance on the trust orthodoxy fall away.

G Other Policy Reasons

Another reason that it is unreasonable to extend the meaning of property in family law is that it gives priorty to those in qualifying relationships over other discretionary beneficiaries. In many modern discretionary trusts it is usual for the children of the relationship, or an earlier relationship together with other dependants to also be beneficiaries. Giving priority to the position of the spouse or partner who is a 'controller' may result in a situation where the trust fund is exhausted to repay a debt based on the *Walker* 'bundle of rights' principles. However, depending on the facts, other discretionary beneficiaries may always be in a position of having no more than a mere *spes*. In *Spry* the High Court of Australia preferred the view that where the trust assets

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458 "Relationship Property and Trusts" above n 46 at p 13.

459 *M v M* above n 290 at [42].

460 "Relationship Property and Trusts" above n 46 at p 23.

461 Property (Relationships) Act 1976, s 4(1)(a).

represent wealth that has accumulated during the marriage then the children's interests should be deferred.

It is likely that this reasoning will apply in New Zealand because it is consistent with the approach taken by courts to applications for Orders settling property for the benefit of children of the relationship[462] that they should be confined to limited circumstances.[463] The policy reason is that children will be best provided for by ensuring that the property division between the parties is implemented in accordance with the principles and purposes of the PRA.

H Leave it to Parliament?

In the space of this dissertation it is not possible to consider the wide body of literature which has been developed around judicial constraints in the making of judge law. Despite the court's deference to Parliament it is widely accepted that Judges do make law in the decision making process. The question this disseration asks is whether the 'bundle of rights' doctrine crosses the boundaries of the court's decision making power with Parliament's legislative prerogative.

Arguably principles of trust law that have been developed over hundreds of years should be given priority over a conflicting meaning of property in family law. Further, when the 2001 reforms were enacted Parliament was aware of the problems that trusts created in relationship property claims but decided not to give the courts authority to access trust capital. The "bundle of rights" theory does indirectly affect both the disposition and administration of trust assets.

The doctrine of precedent provides the law with legitimacy and certainty but as Thomas observes:[464]

> But the precedent should be re-evaluated where it no longer appears to serve the interests of justice or is no longer adequate to meet the contemporary needs and expectations of the community. The coercive element in the doctrine of precedent

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462 Property (Relationships) Act 1976 s 26.

463 *Fisher on Matrimonial and Relationship Property* above n 100 at [18.83].

464 E W Thomas *The Judicial Process: Realism, Pragmatism, Practical Reasoning and Principles* (Cambridge University Press Cambridge, September 15 2005) at p 251.

> would not longer prevail over the twin objectives of justice and relevance. Precedents would be like signposts pointing to the possilbe law or finding in the instant case, rather than rules directing the law or finding.

Whether the development of the law, in the context of a particular case, rests with Parliament or the judiciary is of itself a prinicple of law to be determined by the courts. Where to draw the line depends upon whether the courts can appropriately shape the law more effectively than Parliament. Thomas suggests that where the areas of the law have historically been the subject of case law such as contract, tort and trusts then they can be developed by a judge and should be "advanced to meet the community's needs and expectations without the necessity of the occasional statutory boost. Such areas of the law lend themselves to an incremental approach in accordance with legal principles."[465]

The development of the "bundle of rights' theory is an incremental approach to expand the meaning of property in an area of the law which should not have to wait for a further statutory boost. It is also a reflection of changes to the social, moral and economic fabric of New Zealand society. The use of discretionary trusts in 2011 is vastly different to the trust principles that evolved over 200 years ago. Even if the need for reform of the PRA has been a source of judical and academic comment, it does not mean that the courts should wait for Parliament to respond unless the suggested reform is before the legislature and that is not the situation here.

Whilst the courts can take into consideration the current Law Commission's review of the law of trusts it does not follow that courts should then show deference to the outcome of such a review as Thomas says "Regrettably, law reform reports may be found gathering dust and cobwebs in the basements of legislatures around the world.":[466] Finally, the courts should not ignore the consequences of a decision if it creates injustice because:[467]

> .. the courts should be slow to reject a sound submission requiring a development in the law because it is thought that the change should be left to Parliament. Faced with the injustice or hardship, the court should think again. … Judges cannot turn their back on the unfortunate consequences of their decision and, by leaving the law change to Parliament, assume that they have discharged themselves from responsibility for those consequences.

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465 At p 262.

466 At p 262.

467 At p 263.

In the context of family property law it is the writer's view that it is within the decision-making mandate of the court to adopt an expansive meaning of property. The concept that effective 'control' of a discretionary trust creates a property interest in proceedings under the PRA does not mean it is applicable in general law. Considerations of property interests in laws that govern the relationships of strangers are very different to those in marriage, civil union or de facto relationships. Waiting for Parliament to reform the Act should not be a reason for the courts to give priority to orthodox trust principles.

VIII Conclusion

The 'bundle of rights' doctrine is a development of the law which has created property interests in the context of the PRA. Although its application has been criticised because it offends orthodox trust principles much of the debate has lost sight of its stautory context. The PRA is social legislation which creates different sets of rights and obligations for those in qualifying relationships from laws that deal with the property of strangers. The *Walker v Walker*[468]case authority is an incremental development of the meaning of family property in the context of valuation cases and it is not an attempt to unravel trust law.

For the reasons discussed in chapter 2, competing claims to property rights depend upon the importance of the underlying values associated with those rights. The trust orthodoxy relies upon fiduciary obligations to regulate the trust relationship, to ensure that trustees exercise their discretions honestly and in good faith for the purposes of the trust. Trusts which enable a spouse or partner to effectively control the trust undermine these codes of regulations.

The claim that property rights are created when a party has control over a discretionary trust reflects the social reality that these types of trusts are an illusion of separate ownership in the context of family property law. The core values reflected in the PRA are that the wealth generated during the qualifying relationship should be equally divided, that at the end of the relationship questions arising as to the division of property should be dealt with simply, speedily and inexpensively and the need to ensure that a just division takes into account the economic advantages and disadvantages to the parties at the end of the relationship. These values are more important in family law than the competing values of the trust orthodoxy.

This dissertation does not suggest that the 'bundle of rights' doctrine can be applied in the general law. Claims involving third party creditors or other claimants raise different core values and policy considerations. The Court of Appeal in *Wilson's* case was clear that the concept of the *alter ego* trust is not a separate cause of action in general trust cases. The possibility of an *alter ego* trust creating property interests under the PRA involves quite different considerations which prompted Glazebrook J[469] to comment on its possible application in relationship property claims.

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468 *Walker v Walker* above n 225.

469 *Wilson's case* above n 389 at [128]–[129].

Whilst trust lawyers may express alarm and concern that the trust orthodoxy is being unravelled in a way that has no precedent in law it needs to be emphasised that it is not the traditional law of trust that has created these property interests. Rather it is the development of the modern trust which gives effective control to a settlor or appointor that has attacked the purity of the trust coupled with legislation that recognises quite different rights and obligations for those in qualifying relationships.

The traditional trust which separates legal and beneficial ownership, places restraints on the ability of settlors or trustees to benefit from the income and capital of the trust and can be regulated by the laws of powers and fiduciary obligations are outside the 'bundle of rights' doctrine. This may create a further sub-set of trust situations which remain outside the ambit of the PRA or s 182 Family Proceedings Act 1980. These types of cases will need to await Parliamentary reform.

There will also be situations where the "bundle of rights" doctrine will have to address situations where there is little property outside the trust. For the reasons discussed in chapters 6 the PRA does not provide jurisdiction to the Family Court to access the trust's capital but depending upon the facts the use of judicious encouragement may assist the reluctant spouse and his or her co-trustees to use their powers to distribute sufficient trust capital to satisfy relationship property claims.

This is not to suggest that in time New Zealand Courts could not deliver a decision similar to the High Court of Australia's approach in *Kennon v Spry*[470] but in the meantime it is more likely that the law will develop in an incremental way. For the reasons already discussed the PRA invokes a fluid concept of property and changing social values will continue to throw out challenges to the courts to consider conflicting claims that some rights or interests should be given a property status over others.

Running parallel with the "bundle of rights" doctrine is the development of the law regarding the setting aside of dispositions to trusts. For the reasons discussed in chapter 6 the recent decisions of *Regal Castings*[471] and *Ryan and Unkovich*[472] have opened the door to the possibility that wealth generated during the relationship can be returned to the pool of relationship property. The case law will become increasingly important when gift

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470 *Kennon v Spry* above n162.

471 *Regal Castings* above n 336.

472 *Ryan v Unkovich* above n 338.

duty is abolished later this year because currently the "bundle of rights" doctrine rests on the valuation of debts owed by the trust to the parties. If s44 is applied in a restricted way then the challenge will be to see if the courts are prepared to extend the "bundle of rights" doctrine outside the valuation of debts or in the occupation order cases.

This an exciting and challenging time for both trust and family lawyers as they navigate through largely uncharted waters. No doubt the debate will be heated. Trust and family lawyers often develop their analytical skills in very different social environments. Those that are steeped in the trust orthodoxy will struggle to understand how trusts can be exposed to claims by spouses or partners. Yet many have voiced concerns that a growing number of trusts are insincere and open to attack. Family lawyers are often deeply suspicious of discretionary trusts as they perceive them to be a way to avoid obligations under the PRA and yet many family practitioners will readily see the benefits of trusts as they can shelter wealth that is not created by the relationship, such as inheritances.

The picture is complex and the underlying principles deserve a rigorous debate. The outcome will enrich our understanding of the meaning of property in family law, how property rights and interests evolve over time and why there can be different meanings of property in different statutory settings.

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