Russell McVeagh | Private Client Year in Review 2024

It is now almost four years since the Trusts Act 2019 came into force, and it continues to generate a steady stream of interesting decisions from all levels of the court system.

While the Supreme Court's much-anticipated determinations on *Legler v Formannoij* [2022] NZCA 607 and *Cooper v Pinney* [2023] NZCA 62 have not yet been released, the appeal against *D v A* [2022] NZCA 430 was handed down in late November.

We expect 2025 to be another year full of important developments in the private client space.

A, B and C v D and E Limited [2024] NZSC 161

The shocking facts of this case will now be well known to many. Ms A, Mr B and Mr C are the three living adult children of Mr Z. All three were seriously abused by their father during their childhood, and suffered "incalculable damage", extending into their adulthood, as a result.[1] Prior to his death, their father transferred the majority of his assets into a trust, of which his children were not beneficiaries, preventing them from having any claim to the assets via his estate.

The children brought proceedings seeking to unwind the transfer of assets. As the case evolved on appeal, the primary claim focused on the children's assertion that their father owed them a fiduciary duty that he had breached when he transferred his assets into the trust for the purpose of avoiding his obligations to them. The children argued that the trustees were therefore holding the gifted assets as constructive trustees for the executors of the estate. The fiduciary duty was said to arise as a consequence of the father's abuse, which was the direct cause of the children's vulnerability, including economically, in their adulthood. In the High Court, the children's claim was successful. In the Court of Appeal, the decision was reversed.

The Supreme Court agreed a fiduciary relationship existed between a parent and their children during childhood, and that the father had breached his fiduciary duties through his abuse. However, the Court did not consider the fiduciary relationship extended into their adulthood, or that there was a basis for asserting it had "revived" at the time he transferred his assets into the trust. It is a characteristic of the fiduciary relationship that the beneficiary is "peculiarly vulnerable to", or at the mercy of, "the fiduciary holding the discretion or power".[2] But the vulnerability does not create the relationship – the relationship creates the vulnerability: "[a] fiduciary relationship cannot be reverse engineered into a situation to provide the Court with a remedial response".[3] The Court concluded that, whatever moral claims the children had to their father's assets, he did not hold them as a fiduciary for them. The Court observed that the children could have brought claims against their father in relation to the abuse at the time, whether as tortious actions or acts in breach of fiduciary duty in their childhood, but had elected not to do so (albeit for understandable reasons).[4]

An alternative pathway by which the children's claims could be met, raised by counsel assisting the Court, was the possibility that the beneficial ownership of the assets had in fact never been transferred to the trust. This would be on the basis that:

1. the father had remained a trustee and beneficiary of the trust, and continued to live in the house and enjoy many of the normal incidents of ownership;
2. the evidence established that part of his motivation for the transfer was to defeat any claim his children might bring after his death; and
3. the trust had accordingly been used to avoid the reach of Family Protection Act claims.

The Court should therefore treat the assets as remaining part of the estate, "effectively creating an anti-avoidance remedy at common law in respect of claims under the Family Protection Act."[5] The Court was unable to make findings in this regard as it was not pleaded by the parties, and had not been the subject of evidence or argument in the courts below. It did, however, observe that the proceeding illustrated a case for including an anti-avoidance provision in the replacement for the Family Protection Act, in the event Parliament decides to retain the regime.

The Court concluded that the developments sought by the children would "require a reworking of the fundamental concepts of fiduciary relationships which is disconnected from their doctrinal underpinnings and would be incautious, creating great uncertainty in the law."[6] The appeal was dismissed.

To date, some commentary has criticised the Supreme Court's decision not to extend the principles of fiduciary duty or trust law to accommodate the extreme fact scenario here, noting the obvious harm caused by the father and the unfairness of preventing the children from claiming against his estate. Others, however, have concluded that this outcome was unavoidable without wide-ranging, and highly uncertain, change to fiduciary law in Aotearoa New Zealand.

Power of review under s 126/127

This year has seen the first decisions under sections 126 and 127 of the Trusts Act 2019, which enable a beneficiary to apply to the court to review an "act, omission or decision" of a trustee on the grounds that it was not reasonable in the circumstances. In June we published an article on two of the first cases to apply the provisions: *Paton v Acropolis Holdings Limited* [2024] NZHC 43 and *Sherwin v JKA Holdings Limited* [2024] NZHC 920, available here.

On the decisions to date, it is clear that applications for review are being determined on the facts of each case rather than by reference to decisions under the previous s 68 of the Trustee Act 1956, or determinations abroad. The courts appear unlikely to override a trustee decision if it falls somewhere on the (quite broad) "reasonable" spectrum, and was the result of (reasonably) careful consideration. Trustees are being given room to flex their discretionary muscles without the fear of having their decisions set aside. However, there has not yet been any appellate consideration of the provisions, and there remains considerable scope for broader intervention by the courts in appropriate cases.

Queenin v Queenin [2024] NZHC 1035

A further recent case to address the procedure under sections 126 and 127 is *Queenin v Queenin*. The case has sparked debate amongst trust practitioners, highlighting tension between the purist legal approach and those who favour a more pragmatic view in the context of the ubiquitous "discretionary family trust".

The settlors had established a trust to hold their home and other rental properties. Both were trustees, together with their son. The beneficiaries were the settlors, their children, grandchildren, related trusts and appointed persons or charities.

Following the introduction of the Trusts Act 2019, the settlors decided they no longer required a trust and that the trustees should distribute the assets to them and terminate the trust. When the son disagreed, they took steps to have him removed as a trustee and replaced by a trustee company, controlled by their accountant.

The son, in his capacity as a beneficiary, applied under s 95(1) of the Act for an order reviewing the exercise of the power. The Court applied the review procedure set out in sections 126 and 127. The son also sought the appointment of a trustee corporation as sole trustee.

The High Court had sympathy for the settlors. The "context" of a family trust played a pivotal role in the decision. The Judge found that the settlors had contributed all the capital to the trust fund and had appointed their son as trustee to assist them in the management of the trust's assets. In that context, the Court considered it would be unfair and inequitable to remove the settlors from control of the trust assets and to replace them with a professional trustee. The settlors argued that the power to remove all other beneficiaries provided the Judge with "further support that the trust's purpose was to protect their assets for their own enjoyment, despite not being listed as 'primary beneficiaries'."[7] The Court found that the settlors appropriately exercised the power to remove the son as a trustee as they could no longer expect him to support them to benefit from the trust without interference.[8]

Those in support of the decision quote the sections of the Act requiring judges and trustees to give proper consideration to the intentions of the settlors at the time the trust was established (ss 4(a); 121; 126(b); 27; 45(h); 59(1)(a); 94; 124(4)(c) and 125(3)(c)).

Those who question the decision are concerned that it overlooks long established principles of trust law and the mandatory duties in the Act. A fundamental aspect of trust law is that the settlor disposes of (at least some) beneficial interest of the property by setting up a trust. If this does not occur, then there is no trust. Trustees must balance the interests of the beneficiaries against the wishes of the settlor.

If a settlor wishes to retain a high-but-permissible level of control of the trust fund, careful drafting is required (e.g., by including a definition of "primary beneficiaries" and a protector who has the power to make or veto specific decisions). This requires bespoke drafting to avoid excessive settlor control potentially defeating a trust.

Uncertainty under s 182 of the Family Proceedings Act 1980

The Supreme Court has recently granted leave to appeal *Zhou v Lassnig* [2024] NZCA 177, which considered how a trust should be varied on dissolution of a marriage pursuant to the powerful mechanism in s 182 of the Family Proceedings Act 1980, which gives a wide discretion to Courts to vary trusts (or "nuptial settlements") on divorce.

So far, each court asked to determine the case has reached a different conclusion. The Family Court decided that the trust equity should be shared equally between the former spouses. The High Court held that the trust equity should be divided 60:40 in favour of the wife. The Court of Appeal increased the wife's share to 80%.

The relationship at issue lasted only three years. The couple were trustees and primary beneficiaries, and lived in one of the three trust-owned properties. Ms Zhou had contributed 81% of the equity and Mr Lassnig the remaining 19%. There was a considerable amount of debt.

The Supreme Court previously established a three-step process, known as the "Preston test" for determination of s 182 applications: [9]

1. Determine whether there is a "nuptial settlement" (trust).
2. Assess whether there is a difference between the position of the spouse under the trust on dissolution of the marriage (**position B**) and what the position would have been had the marriage continued (**position C**) (**position A** being the position at the time the trust was settled).
3. If there is a difference between position B and position C, the court must determine how the discretion should be exercised in the particular case.

In *Zhou* the parties agreed that there had been a nuptial settlement when the trust was established.

The Court of Appeal held that Mr Lassnig had no reasonable expectation of a mortgage-free home or to share in trust income and distributions given that (1) no such payments had been made during the relationship; and (2) the likelihood of such payments was remote, given the extent of the trust's debt and repayment obligations. The Court also held that the parties' reasonable expectation must have been that any gains in property value would be shared on a pro-rata basis, in proportion to their advances, rather than equally.

Overall, the Court found the gap between Mr Lassnig's "position B" and "position C" was negligible once he received a refund of his contribution and a pro rata share of the equity.

In exercising its discretion under step 3, the Court held that the shorter the duration of a relationship, the more weight may be given to the disparity of financial contributions. It found that Mr Lassnig's non-financial contributions would have had to outweigh Ms Zhou's by a considerable margin for the court to focus on them, and that the evidence did not support such a finding.

Finally, the parties' relationship had ended following a physical altercation that resulted in Mr Lassnig being served with a police safety order. Ms Zhou also claimed that, prior to this incident, she had been psychologically abused. Counsel for Ms Zhou claimed that the impact of family violence is a consideration that should be relevant to the court's exercise of discretion under step 3 of the *Preston* test. The Court acknowledged the potential in the argument that, in respect of s 182 applications, a party should not expect to be placed in the same position that would have applied had their marriage continued if it was their abusive behaviour that had destroyed the premise of a continuing marriage. However, the Court found that, on the evidence, this was not the appropriate case for such argument.

Whatever the result of the appeal, the variety of outcomes between the courts show just how unpredictable the *Preston* test can be in practice. To avoid this uncertainty, parties that settle nuptial trusts should be careful to make provisions for distribution of trust assets in the event of separation either by way of careful drafting in the trust deed, memorandum of wishes or a s 21 agreement under the Property (Relationships) Act ratified by the trustees.

ADR under the Trusts Act

Section 145 of the Trusts Act 2019, which empowers the court to order parties to a trust dispute[10] to participate in an alternative dispute resolution (**ADR**) process, has seen increasing use this year, as advisors become more familiar with the scope and utility of the power.

Previous case law under the provision[11] established that, even where an application meets the jurisdictional requirements of s 145, the court retains discretion to decline an application, taking into account factors such as cost, confidentiality, speed, the seriousness and complexity of the matter, the wishes of the parties, the wishes of the settlor (if known), finality, and enforcement. Where the orders would clearly be futile (for example, where parties have made clear they will not constructively engage in the ADR process) they will not be appropriate.[12] Given the s 145 power remains in its infancy, each case determined under the provision adds further clarification and colour to the matters the court will take into account when exercising it.

Wiggins v Wiggins [2024] NZHC 863

After their parents' deaths, Jennifer and Ian Wiggins became the sole trustees of their parents' trust. Each asserted that the other had failed to engage with their responsibilities as trustee and not communicated or cooperated with the other on critical trust functions. In 2023, Jennifer filed an application in the High Court seeking (amongst other things), that Ian be removed as trustee and replaced by an independent corporate trustee. Jennifer then sought orders referring the matter to mediation under s 145.

In the High Court, Justice Churchman refused to order mediation. First, because, in the context of this particular dispute, mediation would be futile. A nominee company which provided the trust with income would not be a party, and the mediation outcome therefore not be enforceable against it. The mediation could accordingly not be said to be final, and the costs in conducting it would potentially be wasted.[13] Second, in this case, there was no urgency which justified mediation.[14] The application was dismissed.

Gatfield v Hinton [2024] NZHC 1712

After the death of Ken and Jacqueline Gatfield, a dispute arose between their four surviving daughters and a granddaughter in relation to ownership of the family bach, which was held, in part, in trusts created under Ken and Jacqueline's wills.

In the High Court, after proceedings were initiated in relation to one daughter's conduct as trustee, she applied for orders under s 145 that the proceeding be referred to mediation. Orders were also sought that, in the event mediation was unsuccessful, the dispute then be referred to arbitration.

One of the bases for opposing the application was that it had been brought by way of interlocutory application and not via the procedure set out in part 18 of the High Court Rules 2016 (by way of statement of claim). In the High Court, Associate Judge Lester reiterated prior confirmations from the court that, where a proceeding is underway, an application for referral to ADR may be made by interlocutory application.[15] Determination of whether a matter should be referred to ADR did not require discovery, interrogatories, or a full opposed proceeding, and doing so would "undermine one of the key advantages of ADR being it is a quicker (and cheaper) process than conventional litigation."[16]

The Associate Judge considered the factors in favour of ADR to include the desirability of family matters being dealt with confidentially, the ability to explore non-monetary outcomes (that is, the ability for ADR to address the parties' interests and not solely their strict legal rights[17]), that a wide range of issues could be addressed, and that, even if all that was ultimately achieved at a mediation was a narrowing of the issues, that would still be of value to the parties. The Associate Judge was satisfied it was appropriate in this case to order the parties to attend mediation and took the further step of providing a deadline by which it was required to be completed. Finally, in what we believe to be the first instance of such orders being made under s 145, the Associate Judge ordered the appointment of an arbitrator to conduct an arbitration between the parties in the event the matter was not fully resolved at mediation.

Trustee costs

The use of trust funds to meet a trustee's defence costs in litigation continues to be a vexing subject. While a trustee's right of indemnity is fundamental, it will only apply to costs and expenses that have been "properly incurred". In the absence of a *Beddoe* order (being court orders obtained by the trustee at the outset of proceedings confirming their right to indemnification), trustees are exposing themselves to the risk of being required to meet or repay those costs personally.

The High Court's costs decision in *Martin v Martin* provides a recent example.[18] In that case, separated spouses were also the two remaining trustees of a trust. As a dispute began to brew in relation to the categorisation and division of their property, the wife applied to have them both removed as trustees and replaced by independents. The husband opposed that application, filed relationship property proceedings, and made a cross-application under s 137 of the Trusts Act, seeking that the wife represent the trustees in those proceedings. In the High Court, the wife's applications were granted, and the husband's dismissed.[19]

In the subsequent costs decision, Justice Grau confirmed that, where an application to remove trustees is made on appropriate grounds, the costs of the application will usually be paid from the trust. In this case, the Judge considered that the wife's application to have herself and her husband replaced with independent trustees was clearly in the interests of the trust's beneficiaries, and an entirely reasonable action to have taken in the circumstances. She was entitled to have her costs paid from trust funds. By contrast, the Judge was satisfied that the husband's actions were not in the interests of the beneficiaries (and noted in this regard the previous Judge's comments that the order he had sought would almost certainly be both unworkable and costly[20]). His costs could not be considered "properly" incurred, and he was accordingly not entitled to be indemnified from trust funds.

In addition, the Judge found that, by his opposition and counter-application, the husband had contributed unnecessarily to the time and expense of the proceeding. It was unreasonable for him to have opposed the appointment of independent trustees given his acknowledgement that the relationship had broken down, and that he had failed to consult with his wife on trust matters. The wife was entitled to an uplift of 20% on standard scale costs. Her Honour considered that the increased costs order was further supported by the fact that counsel had "inappropriately and unfairly discussed the substance of settlement discussions between the parties" as part of the costs submissions.[21]

The decision further confirms the value of seeking *Beddoe* orders if there is any doubt as to whether the trustee may be entitled to indemnification in a particular case. While the jurisdiction remains imperfect, and may create cost and delay, it remains far better than the alternative.

Immigration

While 2024 has been quiet on the immigration law front, significant reform is foreshadowed through 2025. The Minister of Immigration, Hon Erica Stanford, has indicated that she is focussed on building an immigration system that attracts highly skilled and high net worth non-New Zealanders, and that this, along with other factors, will be key in delivering an immigration system that follows through on the Government's commitments. The Government has also recognised that immigration settings are just one aspect to attracting talent and investment to New Zealand, but that the role of the immigration system in this space is to ensure that settings do not present barriers, perceived or practical, for highly skilled individuals or investors that choose New Zealand. We are aware that substantive policy work is underway in this area, and we anticipate that there will be future announcements in this space in the near future and reform through the balance of the Parliamentary term.

Increased trustee tax rate and tax avoidance arrangements:

Legislation was enacted in March 2024 to increase the trustee tax rate from 33% to 39% and therefore align that rate with the top personal tax rate of 39%. The change applied from the 2024–25 income year, which commenced on 1 April 2024 for most taxpayers.

The practical effect of this law change is that a trust with beneficiaries on the 39% personal tax rate cannot circumvent the 39% rate by having the trustees retain current year trust income rather than making distributions to beneficiaries. Such retained income was previously taxed at 33%.

The tax rate change meant that there was a lot of private client activity in relation to trusts in the first quarter of 2024 with many taxpayers seeking advice regarding their investment structures involving trusts. Many sought to have income taxed at the previous trustee tax rate of 33%, particularly where trusts owned companies with material amounts of retained earnings. Such earnings could be distributed to trustee shareholders by way of a dividend pre-1 April 2024 and taxed at 33%.

In response to the increased scale of activity and questions from taxpayers, Inland Revenue published guidance regarding the increase in trustee tax rate and certain transactions and structural changes being proposed by taxpayers. The published guidance sought to assist taxpayers with examples of when tax avoidance issues might arise in relation to various factual situations, including shifting income-earning assets from trusts to companies. It will be interesting to see the Inland Revenue approach to such transactions in 2025 and whether further guidance is provided regarding acceptable transactional matters.

Any questions? Talk to one of our experts


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1 *A v D* [2021] NZHC 2297 at [92].
2. At [24], referring to the characteristics of relationships concerning which fiduciary obligations have been imposed, as articulated by the Supreme Court of Canada in *Frame v Smith* [1987] 2 SCR 99.
3. At [76].
4. At [83].
5. At [79].
6. At [83].
7. At [71].
8. At [73].
9 *Preston v Preston* [2021] NZSC 154.
10. Specifically, a matter to which the parties are (1) a trustee and one or more beneficiaries, or (2) a trustee and one or more other trustees of the trust.
11. *Including S v N* [2021] NZHC 2860.
12. *Terry v Terry* [2023] NZHC 884.
13. At [23].
14. At [24].
15. *Being S v N [2021] NHCZ 2860* [2021] NZFLR 756 ad [14]; and *Wright v Pitfield* [2022] NZHC 385 at [14].
16. At [38].
17. At [64].
18. *Martin v Martin* [2024] NZHC 658.
19. *Martin v Martin* [2024] NZHC 147.
20. *Martin v Martin* [2024] NZHC 147 at [35]
21. At [24].