Allens
Deutsche Bank Place
Corner Hunter & Phillip Streets
Sydney NSW 2000 Australia
T +61 2 9230 4000
F +61 2 9230 5333
www.allens.com.au

GPO Box 50
Sydney NSW 2001 Australia

ABN 47 702 595 758

Allens › ‹ Linklaters

14 July 2017

Ms Erin Gough
New South Wales Law Reform Commission
GPO Box 331
Sydney NSW 2000

By Email

Dear Ms Gough

Review of laws relating to beneficiaries of trusts

Submission

Thank you for the opportunity to make this submission.

We are a law firm involved in advising on trusts in many areas of our practice, reflecting the wide use of trusts in Australian corporate and commercial life. The areas include funds management, superannuation, banking and finance, debt capital markets, securitisation, infrastructure development, real estate, mergers and acquisitions, insolvency and reconstruction, litigation and tax. We act for investors and beneficiaries, trustees and responsible entities, investment managers, insolvency practitioners, and lenders and other creditors and counterparties, but we are not making the submission on anyone else's behalf or instructions. The views are our own and reflect the experiences of partners and senior lawyers with expertise in the area.

We would welcome the clarification of a number of aspects of the law relating to the liability of beneficiaries in relation to activities of the trustee. In particular we often find ourselves advising foreign investors and counterparties unfamiliar with Australian commercial concepts and law as to these issues.

In our experience, there is at least some fuzziness in the following areas:

(a) The extent to which beneficiaries are personally liable to indemnify trustees. In most trust instruments that we see this is clarified (one way or the other, by exclusions or by express indemnities), but there may be some questions as to the extent to which exclusions may apply or be read down.

(b) The extent to which creditors and counterparties may be subrogated to that right of indemnity, gaining an indirect right to make a claim against the beneficiaries, in the same way as they are subrogated to the trustees' proprietary rights of exoneration out of trust assets and have indirect access to the assets.

(c) The extent to which beneficiaries may be directly liable to third parties as a result of activities of the trustee.

There are of course various generally applicable heads of accessory liability under which a party can be liable for the fault of another, under equity, tort or statute (eg *Barnes v Addy* constructive trusts, the tort of inducing a breach of contract, and liability under ss 236, 237, 239, 246 and 248 of the *Australian Consumer Law* adopted by the *Fair Trading Act 1987* (NSW), for those 'involved' in a contravention). While any review should take account of accessory liability we do not think any special treatment should be given to beneficiaries under those heads.

The other significant possibility is that the trustee is acting as agent for the beneficiary as principal. In relation to contracts, that would make the beneficiary a party and liable in place of the trustee — the trustee would not be liable in the absence of particular contractual provisions or the operation of the principle of undisclosed agency. In other areas, such as tort or statutory liability, the beneficiary as principal may be liable (in addition to the trustee) for the acts of the trustee within its actual or ostensible authority.

These are just instances of a wider problem, and that is that trusts are used as commercial and investment structures when trust law was not designed for that purpose. Trust law needs to take account of that use and provide the certainty craved by parties involved. Issues include:

- the absence in current case law of any right of direct access or recourse for trust creditors to trust assets; and
- the lack of a specific insolvency regime for trusts (and the uncertainties under current law so far as it applies to 'insolvent' trust estates).

In our experience, those two issues are of much greater concern in practice (examples of significant difficulties include the application of the 'clear accounts rule' under which unrelated trust breaches prejudice the rights of unsecured creditors, and innocent creditors are in a sense subordinated to beneficiaries, and the negotiation and application of limitation of liability clauses in contracts with trustees).

We suggest that at least the questions of beneficiaries' liabilities and creditor's access to trust assets should be considered together – they are inextricably connected – and that the Commission's terms of reference should be expanded accordingly. That would enable it to suggest a comprehensive regime covering recourse for creditors to trust assets and beneficiaries and addressing the interests of both beneficiaries and creditors.

Any review addressing beneficiaries' liability would need to address the direct liability of beneficiaries to trust creditors, and other third parties, for trustee activities. That may entail considering recommending statutory provisions clarifying when that liability does or does not arise and imposing such a liability. If the Review were to suggest such provisions but not cover trust creditors' access to trust assets, it would only be addressing part of the issue. The provisions would risk distorting creditors' attention and recovery actions towards the beneficiaries and away from the trustees and trust assets. In particular, in some situations, if the law does provide for direct recourse to beneficiaries it may be appropriate to provide that creditors must first seek recovery from trust assets (or to clarify that they need not do so).

Similarly, if beneficiaries are to be made liable in any circumstances in the 'insolvency' of a trust, it may be appropriate (subject to constitutional limitations) to look at other possible rules for reopening transactions in insolvency, or insolvency generally.

At this stage, we are not making any submission on oppression.

We would be happy to expand on the above or to discuss them. If you wish us to do so please contact Diccon Loxton [redacted], Derek Heath [redacted] Penny Nikoloudis [redacted] or Mark Kemp [redacted].

Yours faithfully