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# The Legitimate Bounds of a Trustee's Discretion

**Abstract**
From the earliest times, judges have reiterated the notion that a trustee's exercise of discretion is considered an almost sacrosanct power examinable only upon evidence of mala fides. The contention of this article is that, in the modern commercial environment, there should be a limited tightening of the bounds and controls placed upon trustees in the exercise of their discretion so as to increase trustees' accountability. The upshot of this is that greater fairness could be accorded to beneficiaries.

**Keywords**
trustee discretion, trust law, trustee accountability

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ARTICLES

# THE LEGITIMATE BOUNDS OF A TRUSTEE'S DISCRETION

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## Introduction

From the earliest times, judges have reiterated the notion that a trustee's exercise of discretion is considered an almost sacrosanct power examinable only upon evidence of *mala fides*. The contention of this article is that, in the modern commercial environment, there should be a limited tightening of the bounds and controls placed upon trustees in the exercise of their discretion so as to increase trustees' accountability. The upshot of this is that greater fairness could be accorded to beneficiaries.

The observations of Young J in the recent case of *Maciejewski v Telstra Super Pty Ltd*[1] will be used as a springboard for this discussion. In *Maciejewski*, an employee of Telstra, Miss Maciejewski, made an application to the trustee of the Telstra Superannuation Scheme for a benefit on the basis that she was totally and permanently incapacitated. The board of the trustee (Telstra Super Pty Ltd), some three and a half years after the application, recommended that Miss Maciejewski's claim be denied. In considering the application, the board had before it a document forwarded by the Manager of Death and Invalidity Benefits ('the manager') entitled 'Invalidity Benefit Claim – Appeal File Summary and Recommendations'. The document set out extracts from medical reports (submitted both by Miss Maiejewski and the employer) which were prepared some five to six years earlier and related specifically to the issue of workers' compensation liability. The manager invited Miss Maciejewski to forward further information, but this invitation was not taken up. The board accepted the Manager's conclusion that the reports were adequate to fairly assess Miss Maciejewski's claim.

The primary issue for consideration was whether:

> In the opinion of the Trustee, after consideration of all relevant information, evidence and advice, is the member unlikely ever to engage

* The author would like to acknowledge the valuable assistance of Mr Gino Dal Pont (Senior Lecturer, University of Tasmania) for his comments on draft versions of this paper.

1 *Maciejewski v Telstra Super Pty Ltd* (1998) 44 NSWLR 601.

> in any gainful work for which s/he is, for the time being, reasonably qualified by education, training or experience?[2]

The board concluded that Miss Maciejewski's claim for the Total and Permanent Invalidity Benefit be denied. No reasons were recorded except to state that Miss Maciejewski did not satisfy the criteria. Miss Maciejewski applied to the Supreme Court of New South Wales alleging breach of trust and seeking an order requiring the Trustee to reconsider the Invalidity Benefit Claim. Young J held the Trustee had failed to adequately and fairly assess Miss Maciejewski's claim.[3] The matter was remitted to the Trustee for reconsideration.

His Honour's judgment raises two distinct aspects of the exercise of a trustee's discretion: *first*, how the judicial examination of the exercise of a trustee's discretion can potentially conflict with a trustee's right not to give reasons; and *secondly*, whether or not principles of procedural fairness ought apply in the trusts area so as to restrict the exercise of a trustee's discretion. These aspects are considered in Parts Two and Three respectively.

## Examination of Trustees' Exercise of Discretion

The circumstances and judgment of the *Maciejewski* case highlight an apparent tension within trust law. This tension, particularly apparent in commercial situations, relates to the conflict between on one hand, a trustee's right not to give reasons for the exercise of a discretion and, on the other, the subsequent judicial examination of the exercise of discretion. It is a well established trust law principle that trustees are not required to give reasons for the exercise of discretion.[4] In *Maciejewski* counsel for defendant relied upon this principle to argue that the exercise of the trustee's discretion was not reviewable. Young J correctly rejected this argument. The discretionary nature of a trustee's power, or the fact that reasons are not required to be given, do not dictate that a trustee's discretion is absolute. Traditionally, a trustee's discretion cannot be exercised irresponsibly, capriciously or wantonly.[5] Stated in positive terms, the discretion must be exercised *bona fide*, having regard to the purpose for which it was given, and upon real and genuine consideration. Issues of this kind can therefore be examined by the court.[6]

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2 Ibid at 603.

3 Ibid at 606.

4 *Re Londonderry's Settlement* [1965] Ch 918; *Hartigan Nominees Pty Ltd v Rydge* (1992) 29 NSWLR 405 at 434 per Mahoney JA, at 444-445 per Sheller JA.

5 *Pilkington v Inland Revenue Commissioners* [1964] AC 612 at 641 per Viscount Radcliffe; *Gartside v Inland Revenue Commissioners* [1968] AC 553 at 617–618 per Lord Wilberforce; *Lutheran Church of Australia South Australia District Incorporated v Farmers Co-operative Executors and Trustees Ltd* (1970) 121 CLR 628 at 639 per Barwick CJ; *Karger v Paul* [1984] VR 161 at 164-166 per McGarvie J.

6 *Karger v Paul* [1984] VR 161 at 164 per McGarvie J.

The rejection of the defendant's argument by Young J emphasises how a court's examination of a trustee's discretion can impinge on the trustee's right not to give reasons for the exercise of that discretion. His Honour, without referring to any Australian authority, but citing the words of Robert Walker J in *Scott v National Trust for Places of Historic Interest of Natural Beauty*[7] opined that although trustees are not required to give reasons:

> if a decision taken by trustees is directly attacked in legal proceedings, the trustees may be compelled either legally (through discovery or subpoena) or practically in order to avoid adverse inferences being drawn) to disclose the substance for their decision…Indeed whilst trustees do not have to give reasons in a case where a plaintiff puts forward a prima facie case that the trustee's discretion has miscarried, the absence of reasons and the absence of any evidence before the Court as to what happened, will tend to make that prima facie case a virtual certainty.[8]

In other words, whilst as a matter of legal principle trustees are not required to express reasons for their discretionary decisions, practically they may be compelled to do so. When a trustee discloses reasons as a matter of litigious necessity some legal protection is afforded in that the beneficiaries are precluded from relying upon that evidence to examine and review the trustee's exercise of discretion.[9] The latter is said to provide protection from a policy that would otherwise undermine a trustee's right not to give reasons.

However, the issue of concern is that, in establishing whether or not a trustee has acted in good faith, the court determines whether or not the trustee has given real and genuine consideration and has not acted with an ulterior purpose. In the determination of these issues it is very difficult to appreciate how an assessment of a trustee's reasons cannot be made. For instance, to establish whether or not a trustee has acted with an ulterior motive, or given real and genuine consideration, one must necessarily examine the trustee's decision in question. If this is the practical reality of the situation, then there is a very fine line, if any line at all, between the two concepts. It would seem that although principle dictates that the essence of trustee decisions are not examinable, practice and reality dictate that the review of trustees decisions are necessary to avoid the inference of *mala fides*.

It is submitted that a solution to the apparent tension is the limited abolition of a trustee's right not to give reasons. By *limited* it is suggested that the solution be restricted to superannuation trusts. The rationale for this restriction lies in the essential differences between a traditional family trust, from which the principles discussed above have germinated, and a superannuation trust. *First*, it can be argued that, unlike traditional family trusts, the rationale underlying the right not

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7 *Scott v National Trust for Places of Historic Interest or Natural Beauty* [1998] 2 All ER 705.

8 *Maciejewski v Telstra Super Pty Ltd* , see above n 1 at 604.

9 *Karger v Paul* [1984] VR 161 at 166 per McGarvie J.

to give reasons principle is arguably redundant in terms of superannuation trusts. If the rationale is no longer relevant, a rule that expresses that rationale logically must suffer the same fate. This is discussed below at Redundant Rationale. *Secondly*, the contractual and commercial origins of a beneficiary's interest in a superannuation fund, as distinct from the volunteer status of the traditional trust beneficiary, arguably dictates that the trustee ought be subject to a greater level of accountability. This is discussed below at Contractual and Commercial Origins.

## Redundant Rationale

In the well known case of *Re Londonderry's Settlement*[10] Salmon LJ gave three justifications for trustees not being required to give reasons for their discretionary decisions. *First*, the giving of reasons is inconsistent with the principle that trustees' decisions cannot be challenged where the discretion is exercised *bona fide* and without improper motive. *Secondly*, to require the giving of reasons would be likely to embitter family feelings, and the relationship between the trustees and members of the family. *Finally*, such a requirement adds to trustees' already onerous obligations. Each of these are discussed below.

At a superficial level, the giving of reasons does conflict with the principle that discretion will not be examined except upon evidence of *mala fides*. However, it is submitted that the comments by Young J cited earlier demonstrate that the giving of reasons practically aids the court in its examination of a trustee's discretion. Where reasons are not detailed this may lead to an adverse inference being drawn. If the principle that trustees are not required to give reasons instead supports the *mala fides* doctrine, it is difficult to appreciate how an adverse inference could in fact be drawn. Hence, if the disclosure of trustees' reasons are practically required in order to assess good faith and lack of ulterior motive this necessarily implies that that at a practical level the disclosure of reasons does not conflict with the *mala fides* principle, but to the contrary, supports it.

Lord Justice Salmon's second justification, namely the concern for the relationship between family members and trustees, is particularly valid when the issue resolves around a traditional family trust. However, when one moves into the commercial sphere, particularly superannuation, this justification loses much, if not all, of its force. The relationship *between beneficiaries* of superannuation funds is generally one of common employment, a relationship one or more steps removed (especially in the context of larger organisations) from a familial one. The relationship between the beneficiaries *and trustees* is of a professional, not a familial, nature. Also, the issue of maintaining secret a settlor's intention, or not disclosing a settlor's dislike or favouritism of particular beneficiaries, is not a relevant consideration in the superannuation context. The sole purpose of superannuation funds is statutorily prescribed as being the provision of

10 *Re Londonderry's Settlement* [1965] Ch 918 at 936.

superannuation and like benefits.[11] For a trustee of a superannuation fund to entertain a settlor's secret intention or notions of favouritism in the exercise of its discretion would be to entertain an irrelevant consideration thereby constituting a breach a trust. Whilst it may be preferable for beneficiaries and trustees to be on good terms it is not necessarily required for the successful operation of a superannuation fund.

Regarding Lord Justice Salmon's third justification, though it is true to state that trustees are subject to onerous duties, unlike trustees of traditional family trusts, trustees of superannuation trusts are invariably (and generously) remunerated for their services. The issue of adding an additional obligation is therefore a remunerative and cost issue, not one which alone can dictate that trustees need not provide reasons.

## Contractual and Commercial Origins

The differing natures of traditional family trusts and superannuation trusts can also be seen as justifying separate treatment in this regard. It has been judicially recognised that 'pension schemes are of quite a different nature to traditional trusts'.[12] The essential difference is that beneficiaries of a superannuation trust are not volunteers; unlike beneficiaries of a traditional trust, their rights have contractual and commercial origins. Though the nature of a superannuation beneficiary's interest is that of a mere expectancy the beneficiary has given valuable consideration for that interest. In return for the provision of services employees receive a wage or salary and the provision of superannuation benefits.[13] Therefore, in the event that an employee is deprived of a superannuation benefit (or other associated benefits) it is reasonable, given the provision of consideration, that beneficiaries, *as a matter of fairness*, be entitled to reasons for the trustees' decisions.

Countering this argument is the single instance English decision of Rattee J in *Wilson v Law Debenture Trust Corp plc*.[14] This case involved a part sale of a company resulting in its employees being transferred to the purchaser's superannuation scheme. The trustee of the original scheme transferred an amount in respect of the employees to the purchaser's scheme, but a surplus remained in the original scheme. The beneficiaries (the former employees) sought, *inter alia*, access to trust documents that outlined reasons for the trustee's decision not to transfer the surplus. Counsel for the plaintiff argued

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11 *Superannuation Industry (Supervision) Act* 1993 (Cth), s 62.

12 *Imperial Group Pension Trust Ltd v Imperial Tobacco Ltd* [1991] 2 All ER 597 at 605 per Browne-Wilkinson VC; *Mettoy Pension Trustee Ltd v Evans* [1991] 2 All ER 513 at 537 per Warner J.

13 The contractual nexus is strengthened in the Australian context by the statutory prescribed Superannuation Guarantee Scheme whereby employers are required to contribute a prescribed minimum level of superannuation support for each employee. Employers who fail to do so are liable to pay a superannuation guarantee charge equivalent to the amount of the shortfall and an interest component: see generally *Superannuation Guarantee Charge Act* 1992 (Cth); *Superannuation Guarantee (Administration) Act* 1992 (Cth).

14 *Wilson v Law Debenture Trust Corp plc* [1995] 2 All ER 337.

that, as the plaintiffs were not volunteers, they were entitled to see that the fund was properly administered and this could only be achieved by reference to the trustee's reasons.[15] In short, Rattee J held that although a pension scheme is significantly different from a private trust this did not negate the application of long-established principles of trust law as to the exercise by trustees of discretions conferred on them by the relevant trust deed. Rather, his Honour considered that the relevant issue focused on the nature of the interest purchased, the resolution of which turned on the application of principles of trust law to the relevant terms of the trust deed. To this end, Rattee J noted that, although a beneficiary of a superannuation fund provides consideration, the interest purchased remains a mere expectancy, meaning that the rights which flow therefrom are limited to those consistent with the nature of the interest held.

This argument is, on its face, quite compelling. However, though it is legally correct to state that a beneficiary of a superannuation fund holds a mere expectancy, albeit a purchased expectancy, to then conclude that established trusts principles must necessarily apply is no foregone conclusion. If it can be demonstrated that the rationale underlying the development and application of the relevant principle does not hold true in the case of superannuation trusts the fact that those principles are long established principle*s* is irrelevant. This point was not argued before Rattee J, and, as such, was not addressed in his Honour's judgment. Therefore, although general principles of trust law may apply equally to superannuation trusts, arguably Rattee J did not given full consideration to the specific issue of whether trustees of superannuation funds should be compelled to gives reasons for their decisions.

### Summary

In summary, it is accepted that the difference in nature of superannuation funds from the traditional family trust is insufficient to remove the established trust law principle that trustees are not required to give reasons for their decision. However, when the differences in nature are combined with evidence that the rationale underlying the principle is redundant in terms of superannuation funds, it is open to conclude that trustees of superannuation funds ought be required to disclose reasons for their decisions. Such a conclusion carries with it the further benefit of resolving, at least in the superannuation context, an apparent conflict between, one the one hand, a trustee's right not to give reasons, and on the other, the subsequent judicial examination of the exercise of a trustee's discretion.

## Natural Justice and its Applicability to Trust Law

### Natural Justice and its Applicability to Trusts

The second issue raised by the *Maciejewski* case is the application of principles of procedural fairness in the trusts arena. The application of these principles to

15 Ibid at 345 per Rattee J.

the discretionary decision making process conferred on trustees has received little attention by the Australian and New Zealand judiciary, and those of its members who have considered the issue have held that they do not apply to trusts.[16] The reason for this conclusion has been that:

> Questions relating to bias are covered by the trustees' recognised duties of impartiality and avoidance of personal profit. Questions of hearing conflicting contentions are covered, to the necessary degree, by the traditional duty of diligence, which in appropriate cases can encompass a duty to make inquiries.[17]

Hence, the reasoning underlying the non-applicability of administrative law notions of procedural fairness to the exercise of trustees' discretion does *not* flow from the proposition that they are irrelevant in the trust context, but rather that they are already encapsulated within trustee duties. So it can be argued that in the situation where a principle of procedural fairness is not otherwise encapsulated within a trustee duty and that principle does not conflict with any other principle of trust law, such a principle may, and, it is submitted, should, apply to the exercise of a trustee's discretion.

In the *Maciejewski* case Young J, without examining any authorities, gave an indication that principles of procedural fairness should have some relevance to trust law. Quoting from *Scott v National Trust for Places of Historic Interest or Natural Beauty,* his Honour expressed full agreement with the proposition that trustees:

> are not under any general duty to give a hearing to both sides…Nevertheless, if (for instance) trustees (whether of a charity, or a pension fund, or a private family trust) have for the last ten years paid £1,000 per quarter to an elderly impoverished beneficiary of the trust it seems at least arguable that no reasonable body of trustees would discontinue the payment, without warning, and without giving the beneficiary the opportunity of trying to persuade the trustees to continue the payment, at least temporarily. The beneficiary has no legal or equitable right to continued payment, but he or she has an expectation. So I am inclined to think that legitimate expectation may have some part to play in trust law as well as in judicial review cases.[18]

*Prima facie* this obiter dicta statement is contrary to established precedent. However, if the relevant situation in which it is advantageous to a beneficiary for the principles of procedural fairness to apply is, *first*, not covered by an already existing trustee duty, and *secondly*, does not conflict with any other principle of trust law, there are few grounds for finding a legal impedient to its application.

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16 *Karger v Paul* [1984] VR 161 at 166 per McGarvie J; *Dominik v Eutrope* [1984] VR 636 at 638 per Natham J; *Stuart v Armourguard Security Ltd* [1996] 1 NZLR 484 at 506 per McGechan J.

17 *Stuart v Armourguard Security Ltd* [1996] 1 NZLR 484 at 506 per McGechan J.

18 *Scott v National Trust for Places of Historic Interest or Natural Beauty* [1998] 2 All ER 705 at 718 per Robert Walker J in *Maciejewski v Telstra Super Pty Ltd*, see above n 1 at 605 per Young J.

Taking the lead from Young J, the remainder of this paper is devoted to a discussion of whether the principles of procedural fairness ought to apply in the trust context so as to curb trustees' discretion. This issue will be examined at two levels: *first*, at a general level, the issue of whether or not a trustee should be compelled to formally allow all beneficiaries who could be adversely affected by the exercise of his or her discretion to have an opportunity to be heard (discussed at Natural Justice and its Applicability to Trusts); and *secondly*, considering the specific example quoted by Young J (discussed at Generally – An Opportunity to be Heard?). At this point it is noted that the concept of granting an opportunity to be heard is restricted in this paper to the making of representations to the trustee.

**Generally - An Opportunity to be Heard?**

At a general level the issue raised by the *Maciejewski* case is whether or not beneficiaries who could be adversely affected by the exercise of a trustee's discretion should be able to avail themselves of the principles of procedural fairness to compel a trustee to confer on them an opportunity to be heard. Conceivably, in the general discretionary trust scenario, beneficiaries *adversely affected* may encompass any beneficiary who has not been favoured with a distribution from the trustee in respect of each exercise of the trustee's discretion.

At a superficial level, there would appear to be no legal impedient for the application of principles of procedural fairness in the proposed manner. *First*, the proposed application of principles of procedural fairness is not covered by an existing trust law duty or principle. As a matter of trust law, there is no implied obligation requiring a trustee to confer on those adversely affected by the exercise of discretionary power an opportunity to make representations or to be heard.[19]

*Secondly*, although principles of procedural fairness are commonly thought to apply only to the judicial review the administrative decisions, there is established precedent for their application in the private law sphere. Procedural fairness has been applied in respect of disciplinary action by trade unions, professional bodies, trade associations, clubs, societies and other domestic bodies.[20] Moreover, Aronson and Dyer argue that the effect of enactment of *Industrial Relations Act* 1988 (Cth) s 170DC is to impose a duty to hear where an employer terminates employment for conduct or performance related

19 *Karger v Paul* [1984] VR 161 at 166 per McGarvie J.

20 See Aronson M & Dyer B, *Judicial Review of Administrative Action*, LBC (1996), 493-494. The application of principles of procedural fairness to domestic bodies has not been without difficulty. However, it is submitted that these difficulties do not detract from the notion that the application of principles of natural justice has been extended into the private law arena: Aronson & Dyer, ibid at 494 ; and Griggs L & Snell R, 'Natural Justice – An Alternative Ground for Intervention in Corporate Decision Making?' (1994) 10 *QUTLJ* 22 at 32-33.

reasons.[21] This, it is said, has the effect of taking 'natural justice deep into the heartland of the 'private sector''.[22]

*Finally*, from the perspective of beneficiaries, the principle of fairness which underlies both notions of procedural fairness and trustees' duties would be most effectively satisfied by requiring trustees to formally allow representations by beneficiaries whose interests *could be* adversely affected by the exercise of discretionary power. Moreover, the exercise of discretion by a trustee is very similar in nature to the decision making power of persons having the power to make administrative decisions. In that the major difference between the two is that one is in the public law setting whilst the other is in the private, it is legally inconsistent that different rights and principles should have application to one and not the other. Consequently, where trusts principles do not already encapsulate principles of procedural fairness, the remaining principles of procedural fairness should, for reasons of fairness and consistency, apply in the trusts arena.

Whilst the foregoing provides a general rationale for the introduction of principles of procedural fairness so as to compel an opportunity for discretionary beneficiaries to be heard, there are three compelling reasons for *not* extending the proposed application to discretionary trusts. First, the nature of the interest held by discretionary beneficiaries is contrary to the bestowal of such a right. Secondly, it is practically ineffective to apply such principles. Finally, given the nature of the interest held, it is unlikely that satisfaction of the administrative law duty to act fairly would compel trustees to grant all potentially adversely affected beneficiaries an opportunity to be heard. These are discussed in turn below.

### *Nature of the Beneficial Interest*

A discretionary beneficiary's interest in a discretionary trust is a mere expectancy.[23] The beneficiary has a right to be considered by the trustee as a potential recipient of trust property, a right in the nature of an equitable chose in action. This is not, however, a proprietary right, for a 'beneficiary of a [discretionary trust] does not have a proprietary interest in any particular asset of the trust fund or in the trust fund as a whole'.[24] Phrased another way, the beneficiary's interest in not an interest *in possession*.[25] A beneficiary who has an interest in possession is able to presently claim the subject of the interest.[26] These general trust law principles are often supplemented by provision in trust

21 Aronson & Dyer, see above n 20 at 494.

22 Ibid.

23 *Gartside v Inland Revenue Commissioners* [1968] AC 550 at 607 per Lord Reid, at 615 per Lord Wilberforce; *Re Coram* (1992) ALR 353 at 356-357 per O'Loughlin J.

24 *Gartside v Inland Revenue Commissioners* [1968] AC 553 at 607 per Lord Reid, at 617 per Lord Wilberforce; *R & I Bank of WA Ltd v Anchorage Investments Pty Ltd* (1992) 10 WAR 59 at 79 per Owen J.

25 *Gartside v Inland Revenue Commissioners* [1968] AC 553 at 607 per Lord Reid.

26 Ibid.

deeds that a discretionary beneficiary has no interest until such time as the trustee exercises the discretion in his or her favour.[27] Discretionary beneficiaries do, however, possess a right enforceable in equity to ensure that the trust is properly administered.[28] The right of due administration entails having standing to challenge improper exercises of the trustee's discretion and a right to inspect trust accounts and documents.

In this context it must be determined whether the implication of principles of procedural fairness, which would require a trustee to give beneficiaries who may be disadvantaged by the exercise of his or her discretion an opportunity to make representations, accords with the nature of a discretionary beneficiary's interest. There are three reasons as to why the implication of such principles is contrary to the nature of the interest conferred by discretionary trusts. *First*, the application of such a right implies that the discretionary beneficiary has a right to claim a portion of the trust property. The nature of the interest held is merely a right to be considered as a potential recipient, not an interest in possession. To quote Lord Reid: 'If the trustees do decide to pay you something, you do not get it by reason of having the right to have your case considered, you get it only because the trustees have decided to give it to you.'[29]

Conversely, it could be argued that the right to make representations in respect of a trustee's exercise of discretion falls within a discretionary beneficiary's right to due administration of the trust. To this end, one may say that to properly administer the trust and correctly exercise a discretion a trustee should be fully informed of all the circumstances, allowing potential recipients to make representations being a vehicle through which these circumstances may be determined. However, such an argument does not accord with the very nature of a discretionary trust. A trustee of a discretionary trust is not required to be fully informed of all the circumstances of the potential recipients.[30] The trustee must exercise his or her discretion *bona fide* for the purpose for which the power was granted, that is, not irresponsibly, capriciously or wantonly. This does not require that a trustee be fully informed and to seek out all possible options.[31]

*Secondly*, the certainty of object requirement for the creation of a valid discretionary trust is less strict than for a fixed trusts. A list of beneficiaries is not required. Rather, the certainty requirements are fulfilled if a trustee can determine whether or not a specified person falls within or outside the criterion stated within the deed.[32] In some circumstances, particularly where a wide class

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27 Dal Pont G, Chalmers D & Maxton J, *Equity and Trusts: Commentary and Materials*, LBC (1997), 494.

28 *Commissioner of Stamp Duties (Qld) v Livingston* [1965] AC 694; *Re Goldsworthy* [1969] VR 843 at 847-849 per Smith J; *R&I Bank of Western Australia Ltd v Anchorage Investments Pty Ltd* (1992) 10 WAR 59 at 63 per Rowland J, at 79 per Owen J.

29 *Gartside v Inland Revenue Commissioners* [1968] AC 553 at 607 per Lord Reid.

30 *Karger v Paul* [1984] VR 161 at 166 per McGarvie J.

31 Evans M, *Outline of Equity and Trusts*, Butterworths (1993), 341.

32 *McPhail v Doulton* [1971] AC 424 at 448-449 per Lord Wilberforce (with whom Lord Reid and Viscount Dilhorne agreed); *Re Baden's Deed Trusts (No 2)* [1973] Ch 9 at 24 per Megaw LJ. See also *Horan v*

of beneficiaries is specified, the trustee is not required to make as vigorous a survey as in the case of small group.[33] In view of this, it would be unusual to require that trustees inform all beneficiaries who could potentially recipients an opportunity to be heard. The circumstances may in fact preclude this as the trustee may not, and is not required to, have knowledge of all potential recipients. In such a case, it is difficult to argue that the trustee ought be penalised for the failure to grant an opportunity to be heard.

*Finally*, a necessary corollary to requiring trustees to allow those adversely effected by an exercise of discretion to make representations in respect of that exercise of discretion would be to require trustees to gives reasons. It is a very small step from allowing an opportunity to be heard to the disclosure of reasons. Such a step is contrary to established trust principles.[34]

### *Practicality*

Practically speaking it would be difficult and inefficient for a trustee of a discretionary trust to call for representations each time the trustee proposed to exercise his or her discretion in manner which may adversely effect some beneficiaries. This is particularly so where the discretionary pool of beneficiaries is large. One can imagine the untenable situation where a trustee required to exercise a discretion to distribute income annually would be required each year to call for submissions, consider each on its merits and then finally exercise the discretion conferred by the trust deed. Such an exercise would be extremely time consuming and add to trustees' already onerous obligations.[35]

### *General Administrative Law*

The concluding argument in respect of the general consideration is that it is doubtful that the administrative law duty to act fairly would compel a trustee to give discretionary beneficiaries an opportunity to be heard. Traditionally, the determination of whether an administrative decision-maker was required to apply the principles of procedural fairness was determined by application of the circumstances of the case to the formula derived from *Durayappah v Fernando*.[36] The *Durayappah* formula consists of three factors which guide the court in determining whether principles of natural justice apply, namely the

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*James* [1982] 2 NSWLR 376 per Mahoney and Glass JJA; *Herdegen v Federal Commissioner of Taxation* (1988) 84 ALR 271 at 277 per Gummow J; *Re Beckbessinger* [1993] 2 NZLR 362 at 369 per Tipping J.

33 Davies D, 'The Variety of Express Trusts' (1986) 9 U Tas LR 209 at 211.

34 *Re Londonderry's Settlement* [1965] Ch 918; *Tierney v King* [1983] 2 Qd R 580 at 583 per Matthews, Kelly and Macrossan JJ; *Hartigan Nominees Pty Ltd v Rydge* (1992) 29 NSW 405 at 434 per Mahoney JA, at 444-445 per Sheller JA.

35 The courts are slow to add to trustees' already onerous obligation. This is demonstrated by the courts' reasoning on the refusal to require trustees' to give reasons for their discretionary decisions: *Re Londonderry's Settlement* [1965] Ch 918; *Tierney v King* [1983] 2 Qd R 580 at 583 per Matthews, Kelly and Macrossan JJ; *Hartigan Nominees Pty Ltd v Rydge* (1992) 29 NSWLR 405 at 434 per Mahoney JA, at 444-445 per Sheller JA.

36 *Durayappah v Fernando* [1967] 2 AC 337.

nature of the interest held, the consequences of the decision, and the breadth of the discretion conferred on the decision maker. A fourth factor was later added to the *Durayappah* formula, namely, the nature of the tribunal exercising the decision making power…[37] If the circumstances of the case did not accord with the requirements of the *Durayappah* formula, the principles of procedural fairness were not relevant. In 1985, however, the High Court in *Kioa v Minister for Immigration and Ethnic Affairs*[38] significantly relaxed the implication test,[39] so much so that arguably there can now be said to be a common law duty on administrative decision-makers to observe the principles of procedural fairness. Mason J stated:

> The law has now developed to a point where it may be accepted that there is a common law duty to act fairly, in the sense of according procedural fairness, in the making of administrative decision which affect rights, interests and legitimate expectations, subject only to the clear manifestation of a contrary statutory intention.[40]

The concept of an implication test has not been completely abandoned, however, as the common duty to act fairly will be presumed to apply where an administrative decision satisfies the very broad threshold test of *rights, interests and legitimate expectations* of an individual citizen in a direct and immediate way.[41] It is important to emphasise that the threshold test is broad and general. *Kioa*, coupled with subsequent High Court decisions, dictates that if the common duty to act fairly is not rebutted by clear statutory intention, and the circumstances of the case fall within the very broad *rights interests and legitimate expectations* test, the substantive issue remaining to be determined is the *content* of the duty.[42] It is in this respect that the factors making up the *Durayapaph* formula are now utilised. The factors, whilst not relevant for the implication of the duty to accord procedural fairness, are used to determine how

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37 *Salemi v MacKellar (No 2)* (1977) 137 CLR 396 at 420 per Gibbs J. See Sykes E, Lanham D, Tracey R & Esser K, *General Principles of Administrative Law,* Butterworths (1997), pp 197-200; Hotop S, *Principles of Administrative Law,* LBC (1985) 175-190.

38 *Kioa v Minister for Immigration and Ethnic Affairs* (1985) 159 CLR 550.

39 See Allars M, *Introduction to Australian Administrative Law,* Butterworths (1990), 240, 242-243.

40 *Kioa v Minister for Immigration and Ethnic Affairs* (1985) 159 CLR 550 at 584 per Mason J. His Honour's remark has been argued to represent a new beginning in the law relating to natural justice: Griggs and Snell, see above n 20 at 25.

41 *Kioa v Minister for Immigration and Ethnic Affairs* (1985) 159 CLR 550 at 584 per Mason J. See also, Aronson & Dyer, see above n 20 at 400.

42 'The critical question in most cases is not whether the principles of natural justice apply. It is, what does the duty to act fairly require in the circumstances of the particular case? It will be convenient to consider at the outset whether the statue displaces the duty when the state contains a specific provision to that effect, for then it will be pointless to inquire what the duty requires in the circumstances of the case, unless there are circumstances not contemplated by the statutory provision that may give rise to a legitimate expectation.': *Kioa v Minister for Immigration and Ethnic Affairs* (1985) 159 CLR 550 at 585 per Mason J. The approach of Mason J has been accepted by the following subsequent decisions: *Ainsworth v Criminal Justice Commission* (1992) 175 CLR 564; *Johns v Australian Securities Commission* (1993) 178 CLR 408; *Annetts v McCann* (1990) 170 CLR 596 at 598 per Mason CJ, Deane & McHugh JJ; and *Commissioner for Australian Capital Territory Revenue v Alphaone Pty Ltd* (1994) 127 ALR 699 at 713 per Northrop, Miles and French JJ. For a comprehensive analysis of the development of this approach see Aronson & Dyer, see above n 20 at 395-407.

that duty is to be fulfilled.[43] Griggs and Snell argue that this approach is 'like a minimal compliance approach. A decision maker or Court must always work on the basis that a person is entitled to natural justice, unless there is a clear statutory exemption, and then establish whether that person has received at leat the minimal level of procedural fairness necessary in the light of the circumstances of that particular case.'[44]

Regarding the application of principles of procedural fairness in the proposed manner, it is submitted that the duty to act fairly is activated by satisfaction of the broad threshold test. The type of *rights* and *interests* that are sufficient to activate the duty to act fairly includes proprietary and financial interests, reputation, preservation of livelihood and liberty.[45] In *Kioa* Brennan J went even further arguing that *interest* refers to any interest which gives standing at common law to seek a public law remedy.[46] If his Honour's approach is accepted the private law analogy would be an interest which is sufficient to grant standing to seek a private law remedy. A discretionary beneficiary's equitable chose in action clearly falls within this category as a discretionary beneficiary has standing to enforce due administration of the trust. Failing this, arguably an equitable chose in action constitutes an *interest.*

However, it is submitted that whilst the duty to act fairly may be activated, the content of the duty would not extend to requiring adversely affected beneficiaries an opportunity to be heard. As noted above, the *Durayappah* formula guides the court in the determination of the content of the duty to act fairly. The following examination of the *Durayappah* factors arguably leads to the conclusion that the duty to act fairly requires only that trustees consider the right of discretionary beneficiaries to receive a portion of the trust fund.[47]

*Nature of the Interest Held.* As discussed earlier, the nature of a discretionary beneficiary's interest is mere equitable chose in action. The argument presented at 3.2.1 in respect of the beneficiaries interest has application here also. In summary, the interest is not an interest in possession, but rather only a right to ensure that a trustee exercises his or her discretion bona fide for the purposes of the trust. A trustee acting bona fide is not required to make comprehensive inquiries of all beneficiaries.

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43 Griggs & Snell, see above n 20 at 25.

44 Ibid.

45 *Kioa v Minister for Immigration and Ethnic Affairs* (1985) 159 CLR 550 at 582 per Mason J, at 616-19 per Brennan J, at 632 per Deane J. See also Aronson & Dyer, see above n 20 at 408-413; and Allars, see above n 39 at 242-243.

46 *Kioa v Minister for Immigration and Ethnic Affairs* (1985) 159 CLR 550 at 621-622 per Brennan J.

47 The fourth *Durayappah* factor will not be considered at this point. It is acknowledged that as a trustee is not a judicial body this factor will tend against the application of procedural fairness. However, it is submitted that this is not fatal as 'what must be remembered is that natural justice has been applied to non-commercial organisations in non-judicial, or at best, quasi-judicial circumstances, and with the increasing interventionist approach of the judiciary in the administrative law area, this factor does not carry great weight': Griggs and Snell, see above n 20 at 29.

*Consequences of Decision.* Aronson and Dyer argue that the seriousness of the consequence of the decision and the content of the duty to act fairly are directly related.[48] That is, the content of duty will increase as the seriousness of the consequences involved increase. Where a trustee is required to annually exercise his or her discretion as to distribution, it cannot be said that a decision *not* to distribute to a particular beneficiary impacts seriously, or in any way, on that beneficiary's rights. A discretionary beneficiary has a right to be considered as a potential recipient. Consequently, even in the situation where a discretionary beneficiary is not favoured with a distribution, the right to be considered remains. When the time comes for a trustee to again exercise the discretionary power, the beneficiary will again be considered.

*Breadth of Discretion*. The breadth of discretion and the content of the duty to act fairly are inversely related. 'The more circumscribed the discretion, the more likely is it that natural justice will be required to be observed'.[49] Generally, trustees are conferred with very broad discretionary powers. A duty to distribute is often couched in terms of *absolute discretion*. So, in respect of the content of the duty to act fairly, a very broad power implies a less stringent duty to act fairly.

The nature of the interest held by discretionary beneficiaries, the general breadth of discretion conferred on trustees, and the fact that a trustee's failure to exercise his or her discretion in favour of a particular beneficiary does not alter that beneficiary's legal rights, tend towards the general conclusion that the duty of fairness is satisfied by trustees' bona fide exercise of discretion. This does not require a formal procedure whereby trustees give notice and accept submissions in respect of the exercise of their discretion.

In summary, the introduction of principles of procedural fairness into trust law so as to compel a trustee to afford an opportunity to be heard to those adversely affected by his or her exercise of discretion does not sit comfortably with the nature of beneficiaries' interests conferred under a discretionary trust, the practical workings of the proposed procedure, and current administrative law principles. At most, the duty to act fairly requires a trustee to exercise his or her discretion in good faith, with real and genuine consideration and without ulterior motive. If this is correct, a further consequence is that general trust law precludes the application of principles of administrative law, as the duty to act fairly is already encapsulated by trustees' duty to exercise discretion *bona fide* without improper motive.

## Specific Application – An Opportunity to be Heard?

Whilst the foregoing arguments tend to the conclusion that principles of procedural fairness should not compel trustees to give potentially adversely

48 Aronson & Dyer, see above n 20 at 510.
49 Hotop, see above n 37 at 184.

affected discretionary beneficiaries an opportunity to be heard, it is submitted that such principles not precluded from applying to the specific situation outlined by Young J in the *Maciejewski* case. His Honour suggested that, if trustees for the past ten years have distributed a pension quarterly to an elderly impoverished beneficiary, legitimate expectations may have a part to play in requiring the trustee to give the beneficiary the opportunity of trying to persuade the trustees to continue the payment.[50]

Generally – An Opportunity to be Heard? above outlined three reasons for rejecting the proposed general application procedural fairness to trust law. It is contended in this section that whilst the first reason continues to apply in this specific context, the second and third do not. Notwithstanding the applicability of the first rationale, it is submitted that trustees should be compelled in the specific situation at hand to allow relevant beneficiaries an opportunity to be heard. A discussion of each rationale follows.

***Nature of the Beneficial Interest***

The arguments in respect of this first reason centred on the nature of the interest conferred on a discretionary beneficiary. Although a discretionary beneficiary, on being favoured with a distribution, has an equitable proprietary interest in the trust fund equivalent to the amount of the distribution,[51] his or her remaining interest in the trust fund is only a mere expectancy. Where a trustee exercises his or her discretion quarterly as to distribution of trust income, despite any previous distributions, the beneficiary will again only be entitled to be considered as a potential recipient. Consequently, although the specific situation outlined Young J involves a previous distribution, this circumstance has no effect on the arguments presented in respect of the nature of a discretionary beneficiary's interest conflicting with the application of principles of procedural fairness. However, it is contended that this is not fatal to the argument that the principles of procedural fairness ought to apply in the specific situation at hand. Rather, it is argued that the issues of practicality (below at Practicality), and the operation of administrative law (particularly the duty to act fairly: below at 3.3.3), outweigh these arguments.

***Practicality***

The practicality and efficiency of giving notice and calling for representations (or a hearing) is not in issue. Generally, beneficiaries who have been favoured with a distribution are a smaller subset than the pool of beneficiaries from whom a trustee can choose. As a consequence, the time and resources required to allow

50 *Maciejewski v Telstra Super Pty Ltd*, see above n 1 at 605.

51 *Re Vestey's Settlement* [1951] 1 Ch 209 at 220 per Evershed MR, at 222-223 per Jenkins LJ; *Queensland Trustees Ltd v Commissioner of Stamp Duties (Qld)* (1952) 88 CLR 54 at 64 per Dixon CJ, McTiernan, Webb and Kitto JJ.

the previously favoured beneficiaries to make representations is of little significance.

***General Administrative Law***

Regarding the administrative law duty to act fairly, it is submitted that a greater level of procedural fairness is required in the specific situation under discussion than that which is required in the general situation outlined at Generally – An Opportunity to be Heard? The following represents an application of the specific situation outlined by Young J to the administrative law principles, namely, the threshold test and the content of the duty to act fairly.

*Threshold Test.* The threshold test which activates the duty to act fairly is satisfied in the general scenario, and is therefore satisfied in consideration of the specific scenario. If it is held that that an equitable chose in action is not sufficient to activate the duty to act fairly, reliance may be placed on the concept of legitimate expectations. In accord with the High Court's present emphasis on the content of the duty to act fairly (rather than the implication thereof), the concept of legitimate expectations will be further developed in that context.

*Content of Duty to Act Fairly.* The application of the *Durayappah* factors to the situation at hand indicates that the duty to act fairly will be satisfied by something greater than the due exercise of discretion. *First,* a beneficiary who is in receipt of a distribution has a proprietary interest in the fund. Proprietary interests are the strongest type of interest protected by the principles of procedural fairness, and accordingly the content of the duty to act fairly must increase. A significant counter argument to this proposition was raised at Nature of the Beneficial Interest, namely that though a discretionary beneficiary may be in receipt of a distribution, the proprietary interest that flows from this is limited to the amount of the distribution.

A stronger argument for increasing the content of the duty to act fairly is that the relevant beneficiary, in this case an impoverished beneficiary who has been in receipt of quarterly distributions from the trustee for the past ten years, has a legitimate expectation that the distribution will be renewed. Though the concept of a legitimate expectation has not been precisely defined by the courts, it has been described as denoting expectations that go beyond enforceable legal rights provided that they have some reasonable basis.[52] As the concept has been used for a number of different purposes within administrative law,[53] its application to the current situation is most effectively illustrated by analogy. The decision by a trustee not to renew a pension which has been paid for the past 10 years is

52 *Attorney-General (NSW) v Quin* (1990) 170 CLR 1 at 20 per Mason CJ. See also *Salemi v MacKellar [No 2]* (1977) 137 CLR 396; *Reg v MacKellar; Ex parte Ratu* (1977) 137 CLR 461; *Heatley v Tasmanian Racing and Gaming Commission* (1977) 137 CLR 487; *FAI Insurances Ltd v Winneke* (1982) 151 CLR 342.

53 For an outline of the different purposes for which the concept of legitimate expectations is used see Aronson & Dyer, see above n 20 at 414-416.

analogous to the application for the renewal of a licence in circumstances where renewal is expected. In *FAI Insurances* Mason J cited with approval a statement by Scarman LJ in *Re Hook*[54] that:

> it may therefore be right to imply a duty to hear before a decision not to renew when there is a legitimate expectation of renewal, even though no such duty is implied in the making of the original decision to grant or refuse the licence.[55]

The circumstances which may give rise to a legitimate expectation in this sense include: (1) the practice of the authority of automatically renewing licences; (2) where there has been no adverse change in the licence holder's circumstances since the last renewal; or (3) where the licence holder in reliance upon the renewal has expended considerable monies and has been given no indication that the renewal would not be forthcoming.[56] These factors are similarly present in discretionary trust situation under discussion. To renew a pension quarterly for ten years leads to a reasonable and legitimate expectation that it will again be renewed by the trustee. Further, given the practice has been maintained for such a period, the beneficiary could be said to have reasonably relied on the distribution. The behaviour of the trustee and reasonable reliance placed on the distribution by the beneficiary is, it is submitted, sufficient to lead to a legitimate expectation that the distribution will be renewed.

The second *Durayappah* factor relates to the consequences of the decision. In the situation at hand the consequences of an adverse decision are far more serious than in the general situation of a discretionary beneficiary having a mere expectancy of receiving a distribution. In the specific situation at hand, the consequences are the non-receipt of a quarterly pension by an impoverished beneficiary who has relied upon this payment for the past ten years.

The argument in relation to the final *Durrayppah* factor, breadth of discretion, is the same in this context as that discussed above at General Administrative Law. There is no reason to assume that in the specific context the trustee's breath of discretion will more circumscribed than argued above.

Notwithstanding the trustee's apparent breadth of discretion (as in the general situation), the legitimate expectation that the distribution will be renewed created by the trustee's practice of renewing a quarterly pension for 10 years (ie renewal thereby occurring 40 times) and the subsequent reasonable reliance upon that distribution combined with the serious consequences if the distribution is not renewed, is sufficient to require the trustee to confer on the relevant beneficiary an opportunity to be heard.

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54 *R v Barnsley Metropolitan Borough Council; Ex parte Hook* {1976] 1 WLR 1052 at 1058 per Scarman LJ.

55 *FAI Insurances Ltd v Winneke*, (1982) 151 CLR 342 at 361 per Mason J.

56 Hotop, see above n 37 at 182.

In summary, it is concluded that though the nature a discretionary beneficiary's interest tends against the conclusion that principles of procedural fairness should apply, in the specific situation, the fairness considerations which underlie the duty to act fairly outweigh these arguments. Where the behaviour of a trustee in effect creates a representation that is reasonably relied upon fairness to the beneficiary dictates that a greater level of procedural fairness should be accorded to the beneficiary. The behaviour of the trustee should be seen as outweighing the nature of the interest held. As argued by Young J, principles of procedural fairness do have some part, albeit a limited part, to play in trust law.

**Suggestion**

The foregoing identifies that there is a legally justifiable position for the application of the principles of procedural fairness to trust law, albeit only on a limited basis. The remaining issue to be considered is whether or not the principles of fairness dictated by the duty to act fairly are most effectively utilised by the application of the principles of procedural fairness to trust law. In this regard it is submitted that to apply these principles adds an unnecessary layer of complexity to trust law. The wholesale importation of a separate body of law constitutes a very large solution for a limited problem. This is not, however, to suggest that the complexity rationale should of itself operate to defeat the application of the underlying principles of fairness. Instead it is submitted that these principles could be developed within the trust law context. By using the administrative duty to act fairly as an analogy, trust law could be developed so that specific situations (such as the situation identified above) which demand fair procedural treatment are accorded such treatment. This could be effectively achieved by an extension of the trustee's duty to give real and genuine consideration to the exercise of his or her discretionary power.

Part 2 of this paper examined a trustee's duty in respect of the exercise discretionary power. Briefly, a trustee must exercise a discretionary power *bona fide* for the purpose of the trust giving real and genuine consideration.[57] Arguably there is ample room within this doctrine to incorporate a concept analogous to the duty to act fairly where its implication and content is determined by the existence of a legitimate expectation. For instance, where the behaviour of a trustee effectively represents that a distribution will be renewed and the beneficiary reasonably relies upon such representation, fairness requires that, for the trustee to give *real and genuine consideration* to the exercise of his or her discretionary power, the reliant beneficiary is granted an opportunity to make representations to the trustee in respect of the exercise of that power. To go further, the representation and reliance, also having undertones of estoppel, effectively create an equity in the beneficiary, which would be satisfied by conferring an opportunity to be heard.

57 *Karger v Paul*, [1984] VR 161 at 164 per McGarvie J.

## Conclusion

This article has sought to examine the legitimate bounds of a trustee's discretion. Its main conclusion is that a trustee's discretion should be circumscribed in two distinct ways. *First*, in the limited field of superannuation, trustees should be required to disclose to beneficiaries the reasons for their decisions. Not only does this accord greater fairness to beneficiaries but it has the added advantage that an apparent conflict between the two established principles of trust law namely the right not to give reasons, and the curial examination of the exercise of a trustee's discretion, is dissolved. *Secondly*, the principle that trustees are required to give real and genuine consideration to the exercise of their discretion should be further developed so that beneficiaries who have reasonably relied on an expectation created by a trustee's behaviour and actions should have a right to make representations to the trustee is respect of the exercise of his or her discretionary power. The development of this principle could be most effectively achieved by consideration of the rationale underlying the concept of legitimate expectations and its involvement in determining the content of the administrative law duty to act fairly. The primary objective of limiting trustees' discretion in the proposed ways is to increase the accountability of trustees, and so according greater fairness to beneficiaries of discretionary trusts.