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Welcome to the first edition of *Trust eSpeaking* for 2014. We hope you find the articles in this e-newsletter both interesting and useful.

If you would like to talk further about any of the material in *Trust eSpeaking*, or about trusts in general, please don't hesitate to contact us – our details are above.

INSIDE:

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The next issue of Trust eSpeaking *will be published in September 2014.*

NZLAW

AN ASSOCIATION OF INDEPENDENT LEGAL PRACTICES

Risks for Trustees

Health and safety, and other laws, can affect trustees

The Pike River Mine tragedy has changed the way in which health and safety is thought about. This, and other legislative changes, are likely to have major effects for trustees in the future. If your trust owns any type of business or a farm, the trustees need to start thinking more about their responsibilities.

Following the Pike River disaster a Royal Commission under Justice Pankhurst looked at what went wrong and what we can learn from this tragedy for the future. As a result, the authorities are now taking occupational health and safety much more seriously. In the future the laws are likely to be re-written to require a lot more of employers. Regulations that might once have been dismissed as 'nanny state' will now need much more attention paid to them.

This might not seem important to trustees as few trusts own a coal mine. But the new regime will go much further and wider than that. The forestry industry is one which has already been targeted. Any trust which owns any type of business will need to be concerned about health and safety requirements. Trustees can be liable for very substantial damages and fines if the trust fails to meet its obligations.

Other obligations

There are other laws which may affect trustees where a business is operated through the trust. Employment laws can give rise to liabilities and environmental damage can create liability under the Resource Management Act 1991. This is particularly important for trusts which operate a farm. The owners of the farm may be liable for injury to contractors and others working on the farm or visiting the farm – and in the case of a trust, that means the trustees may be liable.

You may remember reading the case a few years ago of the farm owners who were held liable for the loss of life caused by the collapse of a private bridge on their property, even though they had not built the bridge themselves. If you ask workers or contractors onto your premises or property, you are responsible for their safety.

One solution, in the case of farms, is often to have the trust own the land but the trustees lease it back to the settlor who runs the farm. This does not, however, relieve trustees from all potential liability because they will still be owners of the land. Another possibility is to operate the business through a company. You then have the question, however, of who is to be the director of the company. Directors can be exposed to the same types of liabilities as those outlined above in the case of trustees.

Personal liability

It's also important to remember that trustees can be held personally liable. If the trust doesn't have enough money, the trustees may have to put their hands into their own pocket. When trustees sign loan documents or other contracts, they can insist on a clause saying they are not personally liable and only have to pay out of the trust fund. But if you are sued for negligence or failure to comply with regulations – or you are fined – then your liability is personal and not limited to trust assets.

None of this is intended as suggesting that trustees should not hold businesses as trust assets. Where trustees own or operate a business or a business premises, they need to ask themselves some questions:

- Are they aware of all of their responsibilities under health and safety, resource management and other similar laws?
- Have they taken all reasonable steps to comply with the legislation?
- Have they taken out adequate insurance to cover all the risks involved?

If you need some guidance on your responsibilities as a trustee in terms of owning and/or operating a business, please don't hesitate to contact us. ■

When a Trustee Loses Capacity

Removing and replacing incapacitated trustees

With New Zealand's ageing population, more and more people are losing mental capacity as they grow older. When this happens to a trustee of a trust, it can make trust administration difficult or, in some cases, almost impossible.

Complications to trust administration

The majority of New Zealand's trust deeds require trustees to act unanimously when exercising their trustee discretions. There are good reasons for this; this, however, becomes impossible when one trustee has lost mental capacity and is not capable of being involved in decision-making. Decisions cannot be made unanimously if one trustee is not capable of making a decision. In practice, this means that the trust is in limbo until the incapacitated person is removed as trustee.

How can an incapacitated trustee be removed?

Many trust deeds provide for a named person, most often the settlor of the trust, to have the power of appointment and removal of trustees. If the deed is silent as to who has the power of appointment and removal of trustees or the person with the power to remove and appoint trustees is the incapacitated trustee, then s43 of the Trustee Act 1956 provides for the continuing trustees to have the power to replace the incapacitated trustee on the basis that they are unfit or incapable of acting. If the person with that power is not the incapacitated trustee, then that person with the power can remove and, if necessary, replace the incapacitated trustee with a new trustee. This is usually done by deed.

Under s51 of the Act, the High Court also has the power to remove and replace an incapacitated trustee if it's inexpedient, difficult or impractical to do so without the court's assistance. Old age and infirmity have been held sufficient grounds for the court to make an order.

Sections 43 and 51 only apply, however, when you are replacing the incapacitated trustee with a new trustee. These sections cannot be used to remove an incapacitated trustee who is not being replaced. In this situation an application to the High Court will need to be made.

Removal or replacement of the trustee is, however, only the first step, and there can be lingering issues. The incapacitated trustee's name will have to be taken off the title to the trust's assets. Being incapacitated, the trustee cannot sign any documents, transferring the trust's property to the new trustees.

Where the incapacitated trustee has an attorney appointed under an enduring power of attorney, that attorney can complete documents and make decisions about the incapacitated trustee's personal property. This does not extend, however, to the property the incapacitated trustee owns as trustee of a trust as trust assets are not the personal property of the trustee.

Land Information New Zealand (LINZ) which administers our land title system takes the view that an attorney for an incapacitated trustee cannot sign documents relating to trust assets on behalf of the incapacitated trustee.

Vesting orders

The only satisfactory way to rectify the title to the trust's property is to make an application to the High Court for a vesting order under s52 of the Act. Under s52, the court has the power to vest the trust's assets in the names of the new trustees.

Looking ahead

Applications to the High Court are expensive and slow. It's not satisfactory that a problem such as this cannot be resolved by a quick and inexpensive process. This problem has been raised in the Law Commission's recent report on the Law of Trusts and also on previous occasions. Reform is urgently needed and has been recommended to the Law Commission. Hopefully changes will be made soon; otherwise many ordinary trusts will have to meet the cost and experience unnecessary delays. ■

« BACK

Looking into the Election Crystal Ball

A change in government may have implications for your trust

With an election coming up this year we thought it would be interesting to turn our minds to what impact this election, or the next, may have on how you operate and what you place in your family trust.

The Labour Party is promising a capital gains tax (CGT) of 15% with an exemption for your family home. Also promised is an increase in the top tax rate for high earners (over $150,000 and indexed)[1]. You can never second guess what future legislation will look like but it's probably time that you started to think about changes you may need to make in the future.

Capital gains tax

New Zealand is believed to be the only country in the OECD that has no form of CGT; so it's likely that this will be adopted here sooner or later. The country nearest to us with a CGT regime is Australia. In the interests of aligning tax laws we are making the assumption any future New Zealand government will adopt legislation that's similar to the Australian laws. Some points of interest:

Pre-commencement date exemption: Generally capital gains and capital losses from pre-CGT assets are exempt. The Labour Party has confirmed that if it becomes the government, this will occur. Will we see a flurry of purchases just before any future CGT legislation?

Family home exemption: In Australia this is referred to as the 'main residence exemption'. Labour's finance spokesman, David Parker, has confirmed the exemption will apply regardless of the entity holding the family home (sole name, joint names, trust or company). Only one property, however, will be exempt. This is great news for those holding their family home in a trust as in Australia the main residence exemption is not available for a home held by a family company or a trust.

Capital gains made by trusts: If you receive a distribution from a trust under the Australian legislation, you may have CGT consequences. Some types of distribution from trusts are relevant for CGT purposes:

» Distributions of the trust's net income for tax purposes that includes a net capital gain

» Distributions or other entitlements described as being referable to a specific capital gain or gains, or

» Distributions of non-assessable amounts.

Be prepared for a new set of complicated rules.

Proposed change to the top tax rate

At the time of writing, Labour's policy announced in its 2011 manifesto of putting the top tax rate back to 39% for income earners over $150,000, remains in place. When Dr Cullen increased personal tax rates from 33 cents to 39 cents there was a huge growth in trusts and Messrs Penny and Hooper[2] (use of a company with a trust as shareholder to reduce personal income tax, which was ruled to be tax avoidance) type structures.

If the personal tax rate returns to 39 cents the Inland Revenue is likely to pay more attention to your trust structure. In that case, the administration of your trust and good record keeping are likely to become more important – this is something you can start on now.

It will be important you work with all your professional advisers to ensure your trust documentation is sound and cannot be attacked in light of the Penny and Hooper and Krukziener[3] (Inland Revenue reconstructing as income over $5 million of current account advances from a trust as income) decisions.

There are likely to be considerable impacts for trustees and beneficiaries if there is a change in government. In anticipation of possible changes, perhaps it's time to contact us to perform a health check on your trust and trust structures? ■

1 Labour Party Policy Platform and 2011 Labour Manifesto
2 *Penny and Hooper v CIR* [2011]NZSC95
3 *Krukziener v CIR* [2010]24NZTC24.563

« BACK