CONFLICTS IN COMMERCIAL TRUSTS

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Introduction

1 Sir Owen Dixon once remarked that "*[t]he daily relations of man and man are governed by common law, tempered but slightly with equity, and disfigured but little by statute*".[1] The winds of time and circumstance have truly given rise to an extensive and uniquely Australian tendency to employ trust relationships in all manner of commercial relations.

2 Although it is never advisable to commence a lecture with statistics, some figures from the ATO may assist in putting that tendency into perspective.[2] The data for the 2014-2015 financial year accounts for income tax returns for some 802,645 trusts. That figure includes 31,027 trusts classified as involved in the Agriculture, Forestry and Fishing industry, 68,642 in the Construction industry, 108,728 in the Financial and Insurance Services industry, 16,480 in the Manufacturing industry and 134,081 in the Rental, Hiring and Real Estate Services industry. As these numbers highlight, and today's conference

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[1] Sir Owen Dixon, *Jesting Pilate and Other Papers and Addresses* (Law Book Company Ltd, 1965) 13.

[2] Australian Tax Office, 'Taxation Statistics', accessible at <http://data.gov.au/dataset/25e81c18-2083-4abe-81b6-0f530053c63f/resource/64ac0184-a9b9-47ed-87c1-efb55e2a497f/download/taxstats2014trust3selecteditemsbyindustry.xlsx>.

recognises, trusts are undeniably an integral part of the Australian commercial environment.

3 The commercial embrace of the trust relationship in Australia has been received by commentators in different ways. In an essay in Paul Finn's collection, *Equity and Commercial Relations*, Kennedy J remarked that "*[p]erhaps the belated adoption of the judicature system in New South Wales has led to a greater awareness in this country of the equitable resources waiting to be exploited*".[3] That is one way of looking at things – an almost utilitarian conception of equity as a substrate for commercial innovation. Of course, there are consequences that flow from the adoption of particular equitable relationships. In this regard, the view was long held that "*equity had no place in the world of commerce*" – that world demanding speed, certainty and "*the kind of bright line rules…which equity abhors*".[4] The experience of commercial lawyers in this country over recent decades, and indeed, today's seminars, should remind us all that although some of the consequences and uncertainties engendered by use of the trust relationship in commerce can be avoided or modified, some of them cannot.

4 As I will seek to explore below, there is an evident and continuing tension between the so-called "contractualisation" of equity and trust law, and the notion that there are certain fundamental principles of equity that cannot be opted out of, notwithstanding deft legal drafting and the demands of commercial expectations. The duties of corporate trustees and their directors throw these issues into stark relief. In this regard, I will explore first, the fiduciary no-conflict rule, and the scope for its modification or exclusion in the context of commercial trustees, and second, the duties that apply to the directors of corporate trustees.

[3] P D Finn (ed), *Equity and Commercial Relationships* (Law Book Company Ltd, 1987) 2.

[4] P J Millett, 'Equity's place in the law of commerce' (1998) 114 *Law Quarterly Review* 214.

Conflicts and commercial trustees

5 Historically, the law of fiduciary duties emerged, principally during the 19th century, through a process of broadening the obligations of conscience that equity applied to trustees and agents.[5] However, at least from the time of Lord Nottingham,[6] obligations of conscience were applied to trustees which now appear harsh compared with modern fiduciary standards. Those trust-specific obligations have survived in a group of miscellaneous rules that go beyond the more general fiduciary standards of the modern law.[7] While a full exposition of conflicts of interest and duty for commercial trustees would potentially include treatment of the special rules, most of the commercial conflicts that arise for trustees in modern times involve the application of the general fiduciary standards developed in the more modern case law.

6 It is uncontroversial that a trustee, whether corporate or individual, has a fiduciary duty of undivided loyalty to trust beneficiaries. In *Meinhard v Salmon* 164 NE 545 (1928) Cardozo CJ, in the Court of Appeals of New York, explained:

> Many forms of conduct permissible in a workaday world for those acting at arm's length, are forbidden to those bound by fiduciary ties. A trustee is held to something stricter than the morals of the market place. Not honesty alone, but the punctilio of an honour the most sensitive, is then the standard of behaviour. As to this there has developed a tradition that is unbending and inveterate.[8]

[5] The development of the fiduciary idea is succinctly described by PD Finn, *Fiduciary Obligations* (Law Book Company Ltd, 1977), Ch 1.

[6] Lord Nottingham, often described as the "father of modern equity", was appointed Lord Chancellor in 1675. Lord Nottingham was instrumental in the development of the law of trusts and is recognised for having systemised the principles of equity.

[7] Some of the particular rules are: the rule that a trustee is generally not entitled to remuneration (JD Heydon and MJ Leeming, *Jacobs' Law of Trusts in Australia* (LexisNexis Butterworths, 8th ed, 2016), at [17-39]); the rule that a trustee must not purchase the trust property either directly or from a co-trustee, even if the purchase is by public auction and the terms are fair and even generous (*Jacobs*, at [17-43]); the rule that if a trustee purchases the equitable interest of a beneficiary, the onus is on the trustee to show that full value was given, full information was supplied, the beneficiary had the benefit of the trustee's judgment, and the transaction was at arm' s length (*Jacobs*, at [17-47]). The latter two rules are considered later in this paper.

[8] *Meinhard v Salmon* 164 NE 545, 546 (1928).

7 By the latter half of the 20th century, "*[e]quity had established and formalised a new and coherent head of law*" under the fiduciary rubric.[9] As will be explained, the core fiduciary duty of undivided loyalty has been propounded in cases about conflict between interest and duty, conflict between duty and extraneous duty, and profit-taking by reason of or in the course of the fiduciary's office. It should be noted, however, that even outside the special trust-specific rules already mentioned in passing, there are other special, stricter standards that apply in defined circumstances to a wider class of fiduciaries.[10]

8 The core fiduciary duty is one of undivided loyalty and manifests itself in Australia as a proscriptive principle. As Gaudron and McHugh JJ explained in *Breen v Williams* (1996) 186 CLR 71:

> In this country, fiduciary obligations arise because a person has come under an obligation to act in another's interests. As a result, equity imposes on the fiduciary proscriptive obligations - not to obtain any unauthorised benefit from the relationship and not to be in a position of conflict.[11]

Duty-interest conflicts & duty-duty conflicts

9 The latter obligation not to be in a position of conflict is most well-developed in relation to conflicts between interest and duty. In what is perhaps the seminal exposition, Lord Herschell in *Bray v Ford* [1896] AC 44 described the "*inflexible rule of a Court of Equity that a person in a fiduciary position…is not allowed to put himself in a position where his interest and duty conflict*".[12] In his influential judgment in *Hospital Products Ltd v United States Surgical*

[9] Finn, above n 5, 2.

[10] Thus, the rule in *Keech v Sandford* (1726) Sel Cas t King 61; 25 ER 223 creates a presumption of law that certain fiduciaries (including, but not limited to, trustees) cannot retain the benefit of renewal of a lease, while for other fiduciaries there is only a presumption of fact requiring the fiduciary to account for the benefit of the renewed lease: *Chan v Zacharia* (1984) 154 CLR 178; *Jacobs*, at [13-12]. The rule in *Keech v Sandford* is not further explored in this paper.

[11] *Breen v Williams* (1996) 186 CLR 71, 113.

[12] *Bray v Ford* [1896] AC 44, 51.

Corporation (1984) 156 CLR 41, linking the profit principle and the no-conflict rule, Mason J referred to the fiduciary's obligation "*not to promote his personal interest by making or pursuing a gain in circumstances in which there is a conflict or a real or substantial possibility of a conflict between his personal interests and those of the persons whom he is bound to protect*".[13] In the very same year, in C*han v Zacharia* (1984) 154 CLR 178, Deane J's formulation was that "*a person who is under a fiduciary obligation must account… for any benefit or gain… which has been obtained or received in circumstances where a conflict or significant possibility of conflict existed between his fiduciary duty and his personal interest in the pursuit*".[14] In *Pilmer v Duke Group Limited (in liq)* (2001) 207 CLR 165, it was Mason J's formulation that was invoked.[15]

10 The rule that fiduciaries are not allowed to put themselves in a position in which they owe conflicting duties is the less well developed emanation of the no-conflict rule. In *Commonwealth Bank of Australia v Smith* (1991) 42 FCR 390 the Full Court of the Federal Court observed that:

> Not only must the fiduciary avoid, without informed consent, placing himself in a position of conflict between duty and personal interest, but he must eschew conflicting engagements. The reason is that by reason of the multiple engagements, the fiduciary may be unable to discharge adequately the one without conflicting with his obligation in the other.[16]

11 Likewise, in *Bristol & West Building Society v Mothew* [1998] Ch 1, Millett LJ indicated that "*[a] fiduciary who acts for two principals with potentially conflicting interests without the informed consent of both is in breach of the obligation of undivided loyalty*" and that a "*fiduciary must take care not to find himself in a position where there is an actual conflict of duty so that he cannot*

[13] *Hospital Products Ltd v United States Surgical Corporation* (1984) 156 CLR 41, 103.

[14] C*han v Zacharia* (1984) 154 CLR 178, 199.

[15] *Pilmer v Duke Group Limited (in liq)* (2001) 207 CLR 165 at [78].

[16] *Commonwealth Bank of Australia v Smith* (1991) 42 FCR 390, 392.

fulfil his obligations to one principal without failing in his obligations to the other".[17] Adopting language earlier adopted by Gummow J,[18] the New South Wales Court of Appeal in *Beach Petroleum NL v Kennedy* (1999) 48 NSWLR 1 identified the impetus for the conflict of duty and duty rule as being that "*the fiduciary may be unable to discharge adequately the one obligation without conflicting with the requirement for the observance of the other obligation*".[19]

12 These represent but a few of the many subtly and not so subtly different formulations of the no-conflict rule. For today's purposes, I propose to focus on specific applications of the no-conflict rules and the scope for modification and exclusion, rather than attempting a parsing of the various verbal formulations.

13 In considering the extent to which the no-conflict rule can be modified or excluded, it is helpful at the outset to distinguish three categories of techniques employed in the drafting of modern trust deeds. First, questions of *ultra vires* are sought to be addressed by the express conferral of wide powers on trustees. Second, questions of breach of duty are sought to be avoided by narrowing the duties owed by trustees. Third, the consequences of breach are sought to be limited by the use of exemption from liability clauses.

Fiduciary duty as a constraint on the exercise of powers

14 It is common practice in modern trust deeds to incorporate a clause purporting to confer upon the trustee absolute or plenary power in relation to the trust estate.[20] It is important to distinguish two distinct issues in this regard – questions as to the power of a trustee to perform a particular act or action, and questions as to the manner of exercising the powers conferred. Absolute

[17] *Bristol & West Building Society v Mothew* [1998] Ch 1, 18.

[18] *Breen v Williams* (1996) 186 CLR 71, 135.

[19] *Beach Petroleum NL v Kennedy* (1999) 48 NSWLR 1, 47 [201].

[20] Nuncio D'Angelo, *Commercial Trusts* (LexisNexis Butterworths, 2014) 160ff.

or plenary power clauses address questions of the former kind – questions of power. There is clear authority that the conferral of absolute or plenary power does not mean that there are no equitable constraints on the manner in which a trustee may exercise that power.

15 *Wilson v Metro Goldwyn Mayer* (1980) 18 NSWLR 730 concerned a staff pension fund established by trust deed. Under cl 12 of the deed, there was a power to amend the deed exercisable by the trustee *and* the company. Relevantly, cl 12 provided, *inter alia,* that the trusts declared by the deed could "*be altered or amended by a deed executed by the Company and the Trustees in any respect which would in the opinion of the Company not prejudice any benefits secured by contributions made on behalf of any member prior to the date of such alteration or amendment*". A dispute arose as to whether there was power to make a particular amendment.

16 Kearney J rejected the company's argument that its power under cl 12 was absolute and unfettered. Kearney J observed that "*the company must reach its opinion on the basis of a correct understanding of the question to be considered and, hence, must act upon a correct construction in forming its opinion*".[21] Kearney J went on to observe, in *obiter,* that he was "*inclined to regard such a power as falling within the category of powers referred to in Metropolitan Gas Co case inherent in which are fiduciary obligations precluding the company from using such power so as to benefit itself*".[22]

17 The decision referred to, *Metropolitan Gas Company v Federal Commissioner of Taxation* (1932) 47 CLR 621, also concerned a staff pension fund established by trust deed. The particular point in question was whether the company was entitled to certain deductions in its income tax assessment. That question depended on the construction of the trust deed. The

[21] *Wilson v Metro Goldwyn Mayer* (1980) 18 NSWLR 730, 735.

[22] Ibid 736.

Commissioner of Taxation had placed particular emphasis on certain powers in the trust deed being exercisable by the trustees in conjunction with the Company, stressing that the trustees were the director and secretary of the Company. In this regard, Gavan Duffy CJ and Starke J expressed the view that "*[t]he trustees are, of course, in a fiduciary position under the trust instrument, and must exercise their powers honestly and reasonably in the interest of the contributors*".[23]

Informed consent to particular circumstances of breach

18 That immediately raises the question – to what extent and in what circumstances can trustees' proscriptive fiduciary duties be modified, mollified or excluded?

19 The beneficiaries of a trust can authorise particular transactions or instances of conduct that would otherwise constitute a breach of fiduciary duty on the part of the trustee. Consider, for example, the most straightforward application of the no-conflict rule – the self-dealing principle. The modern rule against self-dealing evolved out of the stricter rule which still exists for trustees, as noted at [5] above, which prohibits the purchase of trust property by trustees. In 1856, in *Denton v Donner* (1856) 53 ER 112*,* Sir John Romilly MR opined that "*[n]o doubt where a person is a trustee for sale, and he sells the estate to himself, the transaction is absolutely and ipso facto void*".[24]

(a) family companies & family businesses

20 The use of trusts in the management of family and company property, and as a vehicle for family businesses, raises particular issues in this regard. In *Re Douglas* (1928) 29 SR (NSW) 48, for example, Harvey CJ in Eq considered the question of the sale of trust property to the wife of a trustee. Although

[23] *Metropolitan Gas Company v Federal Commissioner of Taxation* (1932) 47 CLR 621, 633.

[24] *Denton v Donner* (1856) 53 ER 112, 114.

declining to adopt an absolute prohibition, his Honour indicated that a "*Court of Equity would presume [such a] contract was for the benefit of the trustee, and evidence would be required to displace this presumption*".[25] Likewise, in requiring a trustee and his son to account after sale of trust property to the son and subsequent profitable on-sale, Chapman J observed in *Henderson v Woodroofe* [1921] NZLR 411 that "*[t]here is no doubt that the Court has always regarded with extreme disfavour a sale by a trustee of trust property to a near relative*".[26] In this regard, the concerns sought to be addressed by modern statutory provisions directed at related party transactions also draw equity's gaze.

21 It appears that, except where the trustee itself purchases the trust property, the application of the self-dealing rule can be avoided by informed consent. Lord Eldon LC in *Ex parte Lacey* (1802) 31 ER 1228 envisaged the permissibility of such conduct on the condition of "*universal consent*". Additionally, in *Sargeant v National Westminster Bank plc* (1990) 61 P & CR 518, it was held that the no-conflict rule was no bar to trustee purchase of trust property in circumstances where such purchase was expressly authorised by the trust instrument.

22 In relation to the fair-dealing rule, and a trustee's purchase of beneficiaries' interests under the trust, the touchstone is informed consent and punctilious honesty. In *Coles v Trecothick* (1804) 32 ER 592 for example, Lord Eldon LC observed that:

> …the cestui que trust may deal with his trustee, so that the trustee may become the purchaser of the estate. But, though permitted, it is a transaction of great delicacy, and which the Court will watch with the utmost diligence: so much, that it is very hazardous for a trustee to engage in such a transaction.[27]

[25] *Re Douglas* (1928) 29 SR (NSW) 48, 50; see also *Tanti v Carlson* [1948] VLR 401.

[26] *Henderson v Woodroofe*[1921] NZLR 411,418.

[27] *Coles v Trecothick* (1804) 32 ER 592, 597.

23 His Lordship went on to observe that what is required is that "*there is no fraud, no concealment, no advantage taken, by the trustee of information, acquired by him in the character of trustee*".[28] More recently, in *Trinkler v Beale* (2009) 72 NSWLR 365, Macfarlan JA cited the following proposition put by Megarry VC in *Tito v Waddell (No 2)* [1977] 1 Ch 106 that:

> …if a trustee purchases his beneficiary's beneficial interest, the beneficiary may have the sale set aside unless the trustee can establish the propriety of the transaction, showing that he had taken no advantage of his position and that the beneficiary was fully informed and received full value.[29]

(b) trust contracts

24 Another context in which the no-conflict rule raises particular concerns is in relation to trust contracts. The use of trusts in property investment schemes, and indeed, commercial ventures more generally, will often involve commercial links between scheme promoters, corporate trustees and external contractors and service providers. Although the traditional approach of the law of trusts was that a trustee could not delegate their duties or powers and had to act personally, the modern reality is that the administration of a commercial trust will necessarily entail a range of delegations and service contracts with external advisers and agents.

25 *Williams v Barton* [1927] 2 Ch 9 provides an example of how a trustee may run afoul of the no-conflict rule by contracting with a service provider in which they are interested. Burton was a trustee, but he was also employed in a stockbroking firm on terms under which his salary consisted of half of any commission earned by the firm on business introduced by him. On Burton's recommendation, the firm was employed to provide valuations of certain securities held by the trust. Russell J had no hesitation in concluding that the case was within the:

[28] Ibid.

[29] *Tito v Waddell (No 2)* [1977] 1 Ch 106, 225 cited in *Trinkler v Beale* (2009) 72 NSWLR 365 at [21].

> … mischief which is sought to be prevented by the rule. The case is clearly one where his duty as trustee and his interest in an increased remuneration are in direct conflict. As a trustee it is his duty to give the estate the benefit of his unfettered advice in choosing the stockbrokers to act for the estate; as the recipient of half the fees to be earned by George Burnand & Co. on work introduced by him his obvious interest is to choose or recommend them for the job.[30]

26 It may be that, as a result of the analysis of Deane J in *Chan v Zacharia* (1984) 154 CLR 178*,* such cases are more appropriately conceptualised as involving a misuse of position and profit from fiduciary office, rather than a duty-interest conflict.[31] I raise such circumstances here, not in order to delve into the vexed question of whether the profit principle is an emanation of the no-conflict rule, but as a note of caution and to highlight, again, the importance of informed consent.

Efficacy of general authorisation clauses and exclusion of no-conflict rule

27 This brief survey of the authorities should suffice to demonstrate that the fiduciary no-conflict rule can be modified, excluded or avoided, at least in relation to particular circumstances or transactions, on the basis of fully informed consent and utmost honesty. That's the easy part. The more difficult, and more interesting, question is the efficacy of a general waiver or conflict authorisation clause in a trust deed.

28 Dr D'Angelo, in his book *Commercial Trusts,* provides examples of clauses "*attenuating the fiduciary burden*" and which purport to expressly authorise or permit trustees and trustee associates to engage in particular kinds of conduct and transactions.[32] As Dr D'Angelo frankly, and I think rightly, warns:

> …there is a real question about the outer limits of efficacy of a generic waiver clause in a commercial trust instrument, particularly as against investors who acquire their interest without any specific information about activities or intended activities of the

[30] *Williams v Barton* [1927] 2 Ch 9, 12.

[31] *Chan v Zacharia* (1984) 154 CLR 178, 198ff.

[32] D'Angelo, above n 20, 348ff.

> trustee that may be in conflict; for them, the extent of the disclosure is limited to the contents of the clause itself.[33]

29 The efficacy of such clauses can be approached from two different perspectives. With respect to what I will call a "general authorisation clause", the question will be whether the clause is effective as a prospective authorisation of the trustee acting in ways that would otherwise constitute a breach of the no-conflict rule. With respect to what I will call a "general exclusion clause", the question is not prospective authorisation of conduct that would otherwise constitute breach, but rather the exclusion or circumscribing of the trustee's fiduciary duties such that a breach cannot arise. I would suggest these different perspectives reflect a distinction between the *scope* of the trustee's obligations and the *source* of the trustee's obligations. However, the two inevitably run into each other – an authorisation clause seeking to permit trustee conflict as a matter of absolute generality is really seeking to dam the scope of the fiduciary stream at its source.

30 In relation to what I have called general authorisation clauses, it would seem that efficacy will be treated as turning on the question of "fully informed consent". We know from *Maguire v Makaronis* (1997) 188 CLR 449 that "*[w]hat is required for a fully informed consent is a question of fact in all the circumstances of each case and there is no precise formula which will determine in all cases if fully informed consent has been given*".[34] I think it is by no means certain that a broadly worded general authorisation clause encompassing circumstances that were never objectively in the settlor's contemplation will constitute "fully informed consent". I suspect the courts would approach such "consent" with all the more caution where the trust scheme has been promoted or established by a related company of the trustee and the beneficiaries are investors who acquired their interests without

[33] D'Angelo, above n 20, 164-165.

[34] *Maguire v Makaronis* (1997) 188 CLR 449, 466.

the benefit of any specific disclosures as to the contemplated circumstances of conflict.

31 In relation to what I have called general exclusion clauses, it might be thought that the efficacy of such a clause is affirmed by *Hospital Products Ltd v United States Surgical Corporation* (1984) 156 CLR 41. It is true that, in that case, Mason J observed that:

> The fiduciary relationship, if it is to exist at all, must accommodate itself to the terms of the contract so that it is consistent with, and conforms to, them. The fiduciary relationship cannot be superimposed upon the contract in such a way as to alter the operation which the contract was intended to have according to its true construction.[35]

32 However, those remarks were prefaced with this observation:

> That contractual and fiduciary relationships may co-exist between the same parties has never been doubted. Indeed, the existence of a basic contractual relationship has in many situations provided a foundation for the erection of a fiduciary relationship. **In these situations** it is the contractual foundation which is all important because it is the contract that regulates the basic rights and liabilities of the parties.[36] (emphasis added)

33 It is by no means clear that the proscriptive fiduciary obligations owed by the trustee of an express trust can be excluded by the terms of the trust deed. Ad hoc fiduciary relationships arising from particular contractual circumstances, as was the concern in *Hospital Products*, are not necessarily co-equal with the fiduciary relationship traditionally recognised as obtaining between the trustee and beneficiaries of an express trust. Paul Finn states that the question is whether "*it should be possible to contract out of fiduciary responsibilities which* ***inhere in and are characteristic of****, a function to be performed by a party to a relationship with another*".[37]

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[35] *Hospital Products Ltd v United States Surgical Corporation* (1984) 156 CLR 41, 97.

[36] Ibid.

[37] Paul Finn, 'Fiduciary Reflections' (2014) 88 *Australian Law Journal* 127, 141.

34 This question goes to the very heart of the law of trusts and equity jurisprudence in this country – to what extent can the concept of an express trust be emptied of content whilst maintaining its jurisprudential identity? What are the "things" that our law so associates with express trusts that their absence will destroy the character of a trust relationship as such?

35 These questions of jurisprudential identity have given rise to the notion of the "irreducible core of trusteeship". That notion is most well developed in relation to the permissible scope of exemption from liability clauses. In that regard, in considering the validity of a clause purporting to exempt liability for want of skill and care, Millett LJ observed in *Armitage v Nurse* [1998] Ch 241 that:

> The duty of the trustees to perform the trusts honestly and in good faith for the benefit of the beneficiaries is the minimum necessary to give substance to the trusts, but in my opinion it is sufficient.[38]

36 The exclusion or curtailing of duties, such that liability never arises, is the other side of the coin to the questions raised by exemption from liability. Both categories of drafting technique must confront the point identified by Millett LJ in *Armitage v Nurse* that "*[i]f the beneficiaries have no rights enforceable against the trustees there are no trusts*".[39]

37 In the end, the extent to which a trustee's duties can be excluded without impinging on the irreducible core of trusteeship is, fundamentally, a question of policy. In his book, Dr D'Angelo remarks that "*it is unreasonable to expect an arm's length remunerated professional trustee to dedicate itself exclusively to the trust and to do nothing else*".[40] Also in favour of the broad excludability of a trustee's fiduciary duties is the approach of Jacobson J in *ASIC v Citigroup Global Markets Australia Pty Ltd (No 4)* (2007) 160 FCR 35, and the strong American tradition of contractarianism. Perhaps the most convincing

[38] *Armitage v Nurse* [1998] Ch 241, 253-254.

[39] Ibid 252.

[40] D'Angelo, above n 20,165.

argument in this regard is that the settlor is the master of their bounty, and there is no wrong in the beneficiaries taking their entitlements as they find them.

38 On the other side of the ledger, however, lies the storied history of the express trust as the archetype of a fiduciary and the keystone of equity jurisprudence. As Finn expressed his view, "*the courts should be slow indeed to give their blessing to a blanket denial of fiduciary responsibility in a relationship which manifestly would otherwise be fiduciary".*[41] In line with the notion of the irreducible core, and the idea that there are some things that necessarily inhere in trusteeship, Leeming JA has observed extra-judicially:

> Equity, through the principles it has developed about fiduciary duty, protects interests which differ from those protected by the law of contract and tort, and protects those interests from a standpoint which is peculiar to those principles… Nor does equity *invariably* follow the law in determining the extent of rights and obligations.[42]

39 The issues at stake have been aptly summarised in the following way:

> It is tempting to think that those who use the "commercial trust" may yet find that by shying away from the personal duties and liabilities making up the trust relationship they are giving up more than they expected. Equity might yet take issue with the cherry-picking exercise designed to enable the "beneficiaries" to obtain the coveted proprietary interest stripped of all personal relationship of trust and confidence. What property rights equity grants it grants on the basis of special personal relationships and protects by personal remedies; what case is there for giving such rights and remedies to parties who by their own agreement insist that they are not in a relationship which alone would support those? There is little reason to think that were a breach of trust to be asserted by a beneficiary of the Citibank type trust the courts would not set out to give effect to the commercial agreement on distribution of risks and liabilities that the parties have made for themselves. However, the way this would be done matters greatly. If equity is not to become a valet to commerce, the parties should be held to the terms of their commercial bargain and only given such relief as their commercial relations justify. There should be no equitable remedy for breach of trust where there is no trust in the first place.[43]

[41] Paul Finn, 'Fiduciary Reflections' (2014) 88 *Australian Law Journal* 127, 143.

[42] Mark Leeming, 'The scope of fiduciary obligations: How contract informs, but does not determine, the scope of fiduciary obligations' (2009) 3 *Journal of Equity* 1, 4.

[43] Alexander Trukhtanov, 'The irreducible core of trust obligations' (2007) 123 *Law Quarterly Review* 342, 346.

40 I do not seek to answer the policy question in either direction today. What I do stress is that it is by no means certain that broad general authorisation and general exclusion clauses, purporting to exclude an express trustee's fiduciary duties, will be efficacious. For now, as Dr D'Angelo suggests in his book, the wisest course will often be to seek transaction and circumstance specific waivers.[44]

Statutory modification

41 It is to be noted that in certain statutory contexts, particularly where there are consumer protection imperatives at play, the legislature has answered these policy questions for us.

42 In relation to managed investment schemes, and the overlay of Chapter 5C of the *Corporations Act 2001* (Cth) on the law of trusts, a responsible entity is subject to a non-excludable duty to "act in the best interests of the members and, if there is a conflict between the members' interests and its own interests, give priority to the members' interests".[45] That said, there is still scope for member approval for the giving financial benefits from scheme property to the responsible entity or related entities.[46]

43 In relation to superannuation funds, the *Superannuation Industry (Supervision) Act 1993* (Cth) deems certain covenants into the governing rules of a registrable superannuation entity.[47] This deeming includes covenants to give priority to the duties to and interests of the beneficiaries

[44] D'Angelo, above n 20,165.

[45] *Corporations Act 2001* (Cth), s 601FC(1)(c).

[46] Ibid ss 601LA-601LE.

[47] *Superannuation Industry (Supervision) Act 1993* (Cth), s 52(1).

over the duties to and interests of other person and to ensure that the interests of the beneficiaries are not adversely affected by the conflict.[48]

Conflicts and the directors of corporate trustees

44 What then of the directors of corporate trustees? That directors owe fiduciary duties to their company principal is well established.[49] In general, the directors of a company do not owe fiduciary duties to individual shareholders,[50] and the like view has been taken with respect to directors of a corporate trustee and the beneficiaries of the relevant trust.[51] The discussion which follows does not dwell on the fiduciary relationships that might apply to directors as a consequence of particular factual circumstances.[52]

Trustee duties as giving shape and direction to directors' duties

45 That is not to say that the trust relationship, and the status of the corporate principal as trustee, is of no relevance to the duties of directors of corporate trustees. Company directors owe an array of duties to their corporate principal, both by force of statute and at general law. The status of a company as a trustee being a relevant factual circumstance, it should really come as no surprise that that fact may bear on the determination of whether, for example, a director has exercised the powers and duties of a director with care and

[48] Ibid s 52(2)(c)-(d).

[49] *Mills v Mills* (1938) 60 CLR 150, 185 (Dixon J).

[50] *Percival v Wright* [1902] 2 Ch 421, 425; *Multinational Gas and Petrochemical Co* v *Multinational Gas and Petrochemical Services Ltd* [1983] Ch. 258, 288.

[51] *Cope v Butcher* (1996) 20 ACSR 37, 38; *Hurley v BGH Nominees Pty Ltd* (1982) 6 ACLR 791, 796, 800; *Canberra Residential Developments Pty Ltd v Brendas (No 5)* (2009) 69 ACSR 435, 450-452.

[52] See however *Brunninghausen v Glavanics* (1999) 46 NSWLR 538; *Crawley v Short* (2009) 262 ALR 254.

diligence, or whether they have done so in good faith in the best interests of the corporation and for a proper purpose.[53]

46 There is a long line of authority recognising as much. Although decided in the context of particular Tasmanian superannuation legislation, the decision of the High Court in *Fouche v The Superannuation Fund Board* (1951) 88 CLR 609 provides an important touchstone for analysis. The statute in question established a superannuation fund, and established the Superannuation Fund Board as a body corporate having the management and control of the fund. In holding that the members of the board were liable for loss sustained by the fund as a result of loans to Mr Fouche, the High Court, constituted of Dixon, McTiernan and Fullagar JJ, noted that there was "*no escape from the view that the individual members of the board owed a duty to the corporation which they constituted and whose property and affairs they controlled and managed*".[54] Their Honours ultimately reached the view that "*all four defendants were guilty of gross negligence in assenting to the investment… and that all are liable to make good any loss resulting therefrom*".[55] That is, the imprudent investment of trust funds founded a breach of the directors' duties to the corporate trustee.

47 Some 30 years later, in considering a derivative action by company shareholders, Walters J in *Hurley v BGH Nominees Pty Ltd (No 2)* (1984) 37 SASR 499 was faced with the argument that the directors of a corporate trustee could not be under any fiduciary duty to the company in respect of assets and income held by the company as trustee. His Honour ultimately

[53] There is an analogy between the decided cases concerning the relevance of breach of trust by a corporate trustee to the assessment of whether the directors of the trustee breached their duty of care and diligence, and cases which consider whether a breach of the law by the company is a "stepping stone" to the establishment of a breach of the duty of care and diligence by the company's directors. The "stepping stone" theory of director liability was recently reviewed by Edelman J in *Australian Securities & Investments Commission v Cassimatis (No 8)* [2016] FCA 1023.

[54] *Fouche v The Superannuation Fund Board* (1951) 88 CLR 609, 640.

[55] Ibid 641.

concluded that the directors' fiduciary obligations to the company were sufficient to support the derivative action. In reaching this view, his Honour remarked that "*a director must not disregard the interests of members of his company, or the interests of beneficiaries who are not shareholders but who are entitled to receive a benefit from the company's activities as a trustee of the relevant trust*".[56]

48 Some of Walters J's observations appear to countenance directors owing a fiduciary responsibility directly to the beneficiaries of the trust of which their company is trustee. Insofar as his Honour recognised that "*the extent of that responsibility must depend upon the facts of the particular case*",[57] I do not demur. Certainly particular circumstances could arise such as to give rise to a fiduciary relationship between the directors of a corporate trustee and the beneficiaries of the relevant trust.

49 However, the preferable view is that there is no special duty to consider the interests of beneficiaries. Rather, the relevance of the trust relationship and the interests of beneficiaries lies in informing the duties owed by directors to the corporate trustee in their capacity as directors. This approach was lucidly expounded by Finn J in *Australian Securities Commission v AS Nominees Ltd* (1995) 62 FCR 504. In those proceedings, the Commission brought applications on the just and equitable ground for the winding up of certain companies which were trustees and managers of various superannuation trusts and unit trusts. In support of the applications, the Commission contended that the companies had been run at the direction of, and in the interest of, one Mr Windsor, and that the directors of the various corporations had demonstrated little appreciation of their own duties as directors and the duties of their corporations as trustees.

[56] *Hurley v BGH Nominees Pty Ltd (No 2)* (1984) 37 SASR 499, 510.

[57] Ibid 640.

50 In examining the duty of a trustee to exercise the same care as an ordinary, prudent business man, Finn J gave consideration to the exposure and potential liability of directors of a corporate trustee. His Honour observed that "*the requirements of care and caution are in no way diminished*" in respect of a corporate trustee, and that those requirements have "*a* ***flow-on effect*** *into the duties and liabilities of the directors of such a company*".[58] Continuing, Finn J observed "***the duties of trusteeship of the company can give form and direction to the common law and statutory duties of care and diligence imposed on directors****, where the directors themselves have caused their company's breach of trust*".[59] His Honour left open the question of whether the directors of a corporate trustee owe a duty of care directly to the beneficiaries of the trust.[60]

51 In *Westpac Banking Corporation v The Bell Group Ltd (in liq)* [2012] WASCA 157, Lee AJA discerned the following propositions in relation to the duty of care and diligence owed by directors in equity:

> [G]iven that the conduct of directors may effect a breach of trust by a corporate trustee, the trust duties of that corporate trustee may give 'form and direction' to the duty of a director in equity to apply care and diligence to the management of that corporation. But that duty of care and diligence of a director of a corporate trustee is the same duty as that imposed on a director of a non-trustee corporation.[61] (citations omitted)

52 Similar views have been expressed in the Victorian Court of Appeal in relation to the obligation of company directors to act in good faith in the best interests of the company. As Garde AJA observed in *Australasian Annuities Pty Ltd (in liq) v Rowley Super Fund Pty Ltd* (2015) 318 ALR 302 "*a director acting in the best interests of the company as a whole must act in good faith to ensure that the company administers the trust in accordance with the trust deed having*

[58] *Australian Securities Commission v AS Nominees Ltd* (1995) 62 FCR 504, 517.

[59] Ibid.

[60] Ibid 518.

[61] *Westpac Banking Corporation v The Bell Group Ltd (in liq)* [2012] WASCA 157 at [854].

regard to the rights and interests of the beneficiaries of the trust".[62] His Honour continued "*[i]t is not in the best interests of the company for it to act in breach of its duties of a trustee*",[63] and remarked that directors "*should act in good faith to ensure that there is no cause for legitimate complaint by a beneficiary about the administration of a trust for which the company is responsible*".[64]

53 This sort of indirect relevance also arises as a matter of statute in relation to the trustees of self-managed superannuation funds (SMSFs). Under s 52B of the *Superannuation Industry (Supervision) Act 1993* (Cth), certain covenants are deemed into the governing rules of a SMSF – for example, duties to exercise care, diligence and skill and to perform the trustee's duties and exercise the trustee's powers in the best interests of the beneficiaries. Relevantly for present purposes, s 52C goes on to impose a covenant enforceable against each director of a corporate trustee of a SMSF to exercise a reasonable degree of care and diligence for the purposes of ensuring that the corporate trustee carries out the covenants referred to in section 52B.

Lessons for directors

54 The circumstances which gave rise to some of the cases just discussed should operate as a warning to the directors of corporate trustees as to the fundamental importance of understanding their duties as directors and their company's duties as trustee, and of distinguishing at all times their own interests, their company's interests and the interests of the trust beneficiaries.

55 In *Australian Securities Commission v AS Nominees Ltd* (1995) 62 FCR 504, the allegations against the directors included that the trustee companies had

[62] *Australasian Annuities Pty Ltd (in liq) v Rowley Super Fund Pty Ltd* (2015) 318 ALR 302, 350 [228].

[63] Ibid.

[64] Ibid 350 [229].

been run at the direction of, and for the benefit of, an interested party; that the directors had demonstrated little appreciation of their own responsibilities as directors and of the trusteeship obligations of their companies; that trust funds had been intermingled and invested recklessly and improvidently often in circumstances of blatant conflict of interest or of partiality; and that there had also been deficient and defective record keeping for both the companies and the trusts.

56 In *Australasian Annuities Pty Ltd (in liq) v Rowley Super Fund Pty Ltd* (2015) 318 ALR 302, Warren CJ provided the following summary of the impugned conduct:

> [61] [The director's] actions and evidence at trial indicated that his actions fell far short of his obligations as a director. He did not consider the legitimate interest of the beneficiaries, indeed he stated in his cross-examination that he did not look at the transactions from the point of view of the company but of the shareholders. Furthermore, [the director] appeared to do with the trust as he pleased, effecting transactions to benefit himself and his family members while having little or no regard to the fact that [the company] was the trustee of a trust.
> …
>
> [64] [T]here was no evidence that [the director] gave any thought to the interests of [the company] or the beneficiaries of the [trust]. What is even more alarming, is that alongside this failure to take into account the interests of shareholders and beneficiaries, [the director's] actions were intended to and did result in significant financial benefits to the…family.

57 The earlier discussion of the self-dealing rule, and purchases of trust property, should also sound alarm bells for the directors of corporate trustees. So much was recognised in *Re James* [1949] SASR 143. That case concerned the sale of certain real property by the corporate trustee of a testamentary trust to one of the trustee's directors. Mayo J first considered the position of company and director through the prism of agency, noting that directors "*are subject to the disabilities that are attendant upon the agency relationship*".[65] His Honour continued:

> In the ordinary relationship of principal and agent, if the latter enters into an agreement with his principal he must disclose every circumstance of which he is

[65] *Re James* [1949] SASR 143, 145.

> aware, or which in his capacity as agent it would be his duty to ascertain, which is of such a nature that it might reasonably affect the acquiescence of the principal, upon treaty for sale.[66]

58 Turning to the particular position of directors of corporate trustees, Mayo J remarked:

> When a company is a trustee, the knowledge that is possessed by it as trustee is, I think, for present purposes to be imputed to its directors. They are the persons who actually exercise the trustee powers. Such a company is not in a position to affirm the sale of trust premises to one of its directors… The absolute disqualification which attaches to a trustee for sale attaches also to his agent.[67]

Modification of no-conflict rule and informed consent

59 As we have seen with respect to trustee conflicts, a director can avoid breach of the fiduciary no-conflict rule in relation to particular circumstances or transactions of conflict by obtaining informed consent. In the joint judgment of Rich, Dixon and Evatt JJ in *Furs Ltd v Tomkies* (1936) 54 CLR 583, their Honours observed that:

> …except under the authority of a provision in the articles of association, no director shall obtain for himself a profit by means of a transaction in which he is concerned on behalf of the company unless all the material facts are disclosed to the shareholders and by resolution a general meeting approves of his doing so, or all the shareholders acquiesce.[68]

60 Likewise, the House of Lords recognised the possibility of shareholder ratification of what would otherwise entail a breach of the fiduciary no-conflict rule in *Regal Hastings Ltd v Gulliver* [1967] 2 AC 134.

61 The same position does not obtain in relation to the statutory duties of directors under the *Corporations Act,* ss 180-183. In *Angas Law Services Pty Ltd (in liq) v Carabelas* (2005) 226 CLR 507, the High Court considered predecessors to those provisions under the *Companies Code* (SA). Section

[66] Ibid.

[67] Ibid 146.

[68] *Furs Ltd v Tomkies* (1936) 54 CLR 583, 592.

229(2) of the Code imposed a duty to exercise a reasonable degree of care and diligence (now see s 180 of the *Corporations Act*), whereas s 229(4) imposed a duty on directors not to make improper use of their position (now see s 182 of the *Corporations Act*). Gleeson CJ and Heydon J made the following observations in *obiter:*

> While, in some circumstances, the informed assent of all the shareholders to a transaction might be a fact relevant to a question of impropriety, the provisions of s 229 creating offences operate according to their terms. Where ratification operates to protect a director from civil liability to a company it does so upon the principle that "those to whom [fiduciary] duties are owed may release those who owe the duties from their legal obligations and may do so either prospectively or retrospectively, provided that full disclosure of the relevant facts is made to them in advance of the decision". The shareholders of a company cannot release directors from the statutory duties imposed by sub-s (2) or sub-s (4) of s 229. In a particular case, their acquiescence in a course of conduct might affect the practical content of those duties. It might, for example, be relevant to a question of impropriety. A company's right to recover under s 229(7) depends upon the existence of a contravention. If such a contravention has occurred, the question whether a company has lost its right of action under s 229(7) because of some binding decision on the part of its shareholders to release the potential defendants is another matter, and one that did not arise in this case.[69]

62 In *Forge v ASIC* (2004) 213 ALR 574, McColl JA, Handley and Santow JJA agreeing, took the view that shareholder ratification cannot cure breaches of directors' statutory duties under the *Corporations Act*,[70] citing with approval the following remarks of Santow J in *Miller v Miller* (1995) 16 ACSR 73:

> It is also clear enough that ratification cannot cure a breach of statutory duty, more especially one imposing criminal liability. The most it can do is remove from the scope of technical dishonesty such actions as issuing shares for a purpose which is not a proper one, in the sense of not being for the benefit of the company as a whole.[71]

63 Aside from the question of shareholder ratification, it is clear that a company's constitution can authorise conduct that would otherwise amount to a breach of fiduciary duty as a matter of general law. The difficulties as a matter of commercial practice of putting all circumstances of conflict to a meeting of the

[69] *Angas Law Services Pty Ltd (in liq) v Carabelas* (2005) 226 CLR 507, 523 [32].

[70] *Forge v ASIC* (2004) 213 ALR 574, 655 [384].

[71] *Miller v Miller* (1995) 16 ACSR 73, 89.

shareholders means that company constitutions will often contain provisions purporting to allow directors to act despite circumstances of conflict. Such provisions have been considered in *Guinness plc v Saunders* [1990] 2 AC 663 and *Woolworths Ltd v Kelly* (1991) 22 NSWLR 189.

64 Again, the point to be made is that the area of contractarian decisional freedom left to the drafters of company constitutions is not unlimited, and has been circumscribed, in certain respects, by statute. In this regard, the overlay of s 191, and for public companies, s 195, in relation to interested directors, needs to be borne in mind. Importantly, s 199A of the *Corporations Act* provides that a company or a related body corporate must not exempt a person from a liability to the company incurred as an officer or auditor of the company. There are real questions as to the efficacy of conflict authorisation clauses in company constitutions in light of s 199A.

65 Professor Matthew Conaglen has considered the latter issue in detail,[72] and it is beyond the time allotted me today to enter that territory in any depth. Part of the uncertainty lies in the distinction between exemption from liability for breach and the *a priori* circumscription of duty such that no breach ever arises. There are real questions as to whether by employing drafting that circumscribes the scope of directors' duties, rather than providing an exemption from liability in a strict sense, the operation of s 199A can be conclusively ousted. It should be noted that it has been observed in the Western Australian Court of Appeal that it "*cannot be correct*" that "*a blanket provision that excluded the duties of… defaulting directors*" is to be treated as outside the prohibition on exemption from liability. [73]

[72] Matthew Conaglen, 'Interaction between statutory and general law duties concerning company director conflicts' (2013) 31 *Company & Securities Law Journal* 403.

[73] *Eastland Technology Australia Pty Ltd v Whisson* (2005) 223 ALR 123, 129 [26].

Concluding remarks

66 Although I do not have time to dwell on the issue in detail, it should be clear that the modification and exclusion of general law directors' duties raise similar questions to those that I have discussed in relation to the duties of corporate trustees. The tension is between, on the one hand, the desire for flexibility and for the accommodation of commercial expectations, and the contractarian model that reflects those desires, and on the other hand, the idea that there are certain fundamental and mandatory consequences that inhere in particular relationships.

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