RECENT CASES ON UNPAID DISTRIBUTIONS TO BENEFICIARIES OF TRUSTS

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Introduction

The decision by the High Court of Australia in *Fischer v Nemeske Pty Limited* [2016] HCA 11 (2016) 330 ALR 1 has resolved a number of legal controversies regarding the rights of beneficiaries of a trust where there has been a declaration by the trustee to distribute, but no actual transfer of funds or other property from the trust. These issues, litigated in the *Fischer v Nemeske* case, may appear to be arcane, however they have considerable practical significance.

The issue most commonly arises in circumstances where a trustee, usually of a family discretionary trust, determines to make a distribution to beneficiaries, but is either unable or unwilling to pay forthwith the amount of the distribution. It may be a distribution of income or of capital. In such circumstances, it has been common in Australia for trustees, and their accountants, to create loan accounts indicating a distribution to the beneficiary and a loan back by the beneficiary to the trust for the amount of the distribution.

Ironically, given the doubts expressed during the *Fischer v Nemeske* litigation as to whether such arrangements can have any validity, they appear to have been a common means of organising family wealth.

The taxation implications of these arrangements have been appreciated by the Australian Taxation Office for some years, and have been the subject of tax rulings and determinations[1]. Amongst accountants and tax lawyers there is a technical term for these transactions where a beneficiary is said to be presently entitled to an amount from a trust, but it has not been paid. They are commonly referred to as an "unpaid present entitlement" (UPE).

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[1] See TR 2010/3, ATO ID 2013/15, and ATO TD 2015/D5, and see *Commissioner of Taxation v Bamford* (2010) 240 CLR 481

Notwithstanding that it is likely that there are many thousands of UPE's recorded in the accounts of family trusts in Australia, the appellants in *Fischer v Nemeske* argued that a trustee is not able to create a binding obligation to distribute at a future time, capital or income to a beneficiary, at least pursuant to the terms commonly found in family discretionary trust deeds in Australia. Although that argument in its strongest form was ultimately unsuccessful, in rejecting it the High Court has now clarified the manner in which UPE's do give rise to enforceable obligations.

Apart from the issue of the validity of unpaid distributions to beneficiaries, a second question raised by the litigation was the juridical nature of the rights held by the beneficiaries against the trustee in regard to such distributions. In those matters that have made it to Court, the evidence has shown that the transactions have been accounted for as a distribution, and loan back by the beneficiary of the notionally distributed proceeds. The beneficiary's entitlements thus appear to be a claim in debt upon the loan. Despite this common accounting practice, the ATO, and Australian tax lawyers have generally held the view that the obligation was not a loan but one based on the equitable entitlement of the beneficiary against the trustee, this was thought to follow from the decision of the New Zealand Court of Appeal in *Commissioner of Inland Revenue v Ward [1970] NZLR 1.*

In the *Fischer v* Nemeske litigation, the New South Wales Court of Appeal[2] concluded that the action by a beneficiary to enforce an unpaid distribution was an action for monies had and received. It was thus held not to be an equitable claim, but a common law cause of action.

In the High Court in *Fischer v Nemeske* the majority appear to have eschewed a single doctrinal explanation of the rights of beneficiaries. The beneficiaries' entitlement will depend upon the scope of powers conferred by the trustee or by relevant statutes, together with the precise actions taken by the trustee in any particular case. Nevertheless, the High Court majority endorsed the reasoning of Barrett JA in the Court of Appeal, to the extent of finding that rights may exist in favour of a beneficiary pursuant to an action for monies had and received.

To better understand the problems and the resolution by the High Court it is useful to look at the way in which the issue has developed in Australia, firstly in the litigation that reached the New South Wales Court of Appeal as *Clark v Inglis (2010) 79ATR 447,* and then to turn to the *Fischer v Nemeske* case.

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[2] *Fisher v Nemeske Pty Ltd* [2015] NSWCA 6

The *Clark v Inglis* Case

Upon the death of Dr William Inglis, a dispute arose as to whether a beneficiary loan account, in the records of the discretionary trust that Dr Inglis had set up, was enforceable at the demand of his executors, or was void, and hence no sum was due.

The matter at first instance, *Wood v Inglis* [2009] NSWSC 601, was determined by Brereton J in the New South Wales Supreme Court. The evidence revealed that the trust accounts for the family discretionary trust of Dr Inglis for the eight odd years before his death had been prepared on the basis that the share portfolio held by the trust was revalued each year to market, and any net positive movement in the value of investments was treated as income, and distributed to Dr Inglis by being credited to his beneficiary loan account. No actual payments were made to Dr Inglis. At the date of his death as a result of the credits to his beneficiary loan account, the accounts of the trustee company showed it was indebted to his estate in the sum of $1.3 million.

At the hearing at first instance, there was controversy as to whether or not the increases in the market value of the share portfolio were income, and hence distributable as such by the trustee in circumstances where they had not been realised by a sale of the assets. Expert accounting evidence was called. His Honour concluded that the trustee was entitled to treat the increases in net value of the investments as income on account, and moreover, even if they had been unrealised capital gains, they were capable of being distributed as capital under the provision in the trust deed permitting the trustee to advance capital in its discretion.

As the case was conducted before Brereton J, the focus was on the proper characterisation of the increases in market value of the share portfolio, and whether that fell within the description of income under the deed. Further, there was substantial controversy as to whether the accounting treatment was something that had been undertaken by the accountant properly instructed by the trustee, or whether it had been merely done by the accountant on the assumption that this was how the trust had, in the past, operated. In regard to this issue Brereton J found that the late Dr Inglis had been actively involved in the administration of the trust, had viewed the accounts each year and accepted them, and that as the controlling mind of the corporate trustee, His Honour inferred that Dr Inglis had approved of the distributions of income recorded in those accounts.

Importantly, Brereton J found that Dr Inglis had made his last will on the footing that the substantial loan account in the trust was an asset of his estate (ie that the trust owed him the sum of the loan account which was in effect repayable on call).

One further issue, although having only a subsidiary significance in the initial stage of the litigation, was whether the trustee did in fact make the relevant distributions to Dr Inglis. Keeping in mind that no money was distributed, but that Dr Inglis was merely credited in the books of the trust with an amount equal to the distribution, as a sum for which the trustee was now indebted to him, His Honour nevertheless concluded that these distributions had been made. There were resolutions of the company in its capacity as trustee resolving to distribute the relevant amounts. Further, His Honour noted that there was a default distribution of income to Dr Inglis, if the trustee's discretion had not otherwise been exercised, and His Honour concluded that this would have resulted in the same practical outcome had the resolutions not been effective.

Although the issue is hinted at before Brereton J, it was not suggested in the boldest terms that distributions could not be made by accounting entries in the books of the trustee recording an acknowledgement of debt to the beneficiaries. The issue was restricted to whether the increases in value of the assets was income in the absence of realisation, but that was not a matter solely relevant to the issue of distribution under trust law, the characterisation of income being an issue which arises in a number of other legal contexts, including tax and company law.

The decision of Justice Brereton upholding the validity of the loan accounts was appealed to the New South Wales Court of Appeal (*Clark v Inglis* (2010) 79 ATR 447). Before a Bench consisting of Allsop P, McColl and Macfarlan JJA, the issues underwent a subtle change of emphasis. Allsop P noted that if the distributions in the books of the trust were effective, then the distributed income fell within the assessable income of the beneficiaries in consequence of provisions of the *Income Tax Assessment Act* 1936 (Cth), and that the tax returns of the beneficiaries, and the trust, did not appear to be consistent with the claim that there had been such a distribution.

Importantly, Allsop P characterised what had happened as - "the making of the distribution and the lending back of the distribution" at [30]. This clearly implied that the relevant entries in the accounts, showing a loan associated with a distribution, ought be understood as having reflected a notional distribution on the one hand, and a loan of the amount of that distribution

by the beneficiary back to the trustee, leaving the trustee indebted to the beneficiary by the amount of the income distributed.

Before the Court of Appeal the principal argument of the applicants was that regardless of accounting principles, income tax law, or company law concerning the availability of profit for the declaration and distribution of dividends, unrealised capital gain *per se*, is not income whether under the trust deed or at law. The increased value of the investments may constitute a profit, but that did not equate to income and was not distributable. This argument was rejected by the Court which concluded that both under the trust deed, and the law generally, unrealised increases in the value of investments were capable of being treated as income. The Court granted leave to appeal, but dismissed the appeal and upheld the decision of Brereton J.

In *Wilson v Chapman* [2012] QSC 395, a decision of Justice Daubney of the Supreme Court of Queensland, the focus of that case was again on whether the increases in value of investments constituted or could constitute income or capital gain. His Honour however noted that in *Clark v Inglis* the trust deed had merely required the trustee to "apply" the income and that this was done by crediting beneficiaries' accounts, although no money in fact was realised. In *Wilson v Chapman* the trust deed required the trustees to "pay, transfer and hand over" the income and profits, and this, His Honour concluded, could not be done in regard to unrealised increases in value by book entries.

The Fischer v Nemeske Litigation

Issues touched upon only tangentially in the *Inglis* litigation became the central question in the litigation involving the family trust of the late Mr Nemes. At the death of Mr Nemes in September 2011 the accounts kept by Nemeske Pty Limited, as trustee of the Nemes Family Trust, showed a debt owed by the trust to the late Mr Nemes of $3.9 million. Once again the issue turned upon whether that money ought be paid by the trustee to the Nemes estate for the benefit of the residuary beneficiaries of that estate, or whether the debt was void, thus enlarging the corpus of the trust to the advantage of the beneficiaries of the trust.

The origin of the debt lay in decisions of the trustee in 1994. The trustee had created an asset revaluation reserve following a revaluation of the assets by a further $3.9 million. The assets were shares in private companies which in turn held assets, largely land, in both Australia and the United States.

Some months after creating the asset revaluation reserve the trustee resolved to make – "a final distribution" out of the asset revaluation reserve, the entire reserve to be paid or credited to two of the beneficiaries, Mr and Mrs Nemes as joint tenants. Beneficiaries accounts at 30 September 1994 after the resolution showed a capital distribution of $3.9 million, and liabilities recorded as – "loans-secured B.G and M Nemes $3.9 million".

In addition to these entries in the accounts of the trustee a charge was executed by the trustee and registered, securing a debt by the trustee to Mr and Mrs Nemes of the $3.9 million dollars. The existence of that deed of charge added a number of additional issues to the litigation, and was significant in light of a limitation defence raised by the trustee. However, both at first instance and in the appeals, the primary issue was whether the relevant oral resolution and accounting entries gave rise to a debt.

The trustee raised an interesting and important argument. A distribution by a trustee, it was said, either of income or of capital, required an actual transfer of property from the trust to the beneficiaries. The issue was in part governed by the terms of the deed, and the deed in this case, gave the trustee power to "advance" or "raise" any part of the capital or income, and to "pay" or "apply" the same as the trustee thought fit for any of the beneficiaries. Even such broad words as these, so it was argued, coupled with the general law of trusts, required that the trustee transfer ownership of some property of the trust, and that the resolutions of the trustee and entries in the accounts were, until such distribution took place, nothing more than an indication of an intention which had not been acted upon by the trustee.

The trustee further argued that there appeared to have been confusion in the mind of those responsible for the drafting of the resolution and the creation of the accounts. In company law, a declaration by the Board of a company of a final dividend typically gives rise upon that declaration, to a debt by the company to the shareholder for the requisite dividend. From the time of the declaration, the declared dividend is a liability of the company until extinguished by payment. Subject to the constitution of the company and the terms of the declaration, the dividend is from its declaration a debt enforceable by the shareholder in the event that the company fails to make the payment. By contrast the trustee argued, trust law knows no analogous doctrine whereby a mere resolution or determination by a trustee of an intention to make a distribution of income or capital, gives rise immediately to a debt enforceable at the behest of the beneficiary for the quantum of the intended distribution. The determination by

the trustee reflects merely a statement of intention, and gives the beneficiary no enforceable right to sue for the distribution the trustee has resolved to make.

Applying arguments of the sort just set out, the trustee contended that the resolution made by its directors some 20 years earlier, and the entries in the accounts, were wholly ineffectual to make a distribution, or advance capital to Mr and Mrs Nemes. If there had been no effectual distribution of capital, then there was nothing to support any debt by the trustee company to the beneficiaries, and there was in consequence no enforceable loan owed by the trustee to the beneficiaries, and nothing secured by the registered charge.

The matter was dealt with at first instance by Justice Stevenson in the Supreme Court of New South Wales. There were a number of other issues not relevant to this paper concerning the proper construction of provisions of the trust deed, and further factual issues generated by the incomplete records of the trustee company. Only one of those issues is of present interest, namely, that the very words of the resolution whereby the trustee purported to distribute the "asset revaluation reserve" was clearly not capable of literal application. The asset revaluation reserve was just an accounting entity and could not, in any sense, be distributed. However, Stevenson J concluded that properly construed, the resolution clearly intended to distribute money to the value of the asset revaluation reserve, namely $3.9 million.

Having resolved the issue just described, His Honour came to the critical question, namely, given that no money was in fact paid out, whether the creation of the capital distribution entry in the beneficiaries' accounts, and creation of a non-current liability in the balance sheet styled "loans-secured EG & M Nemes" was a manner in which the trustee was able to make a distribution, and gave rise to an enforceable debt at the behest of the beneficiaries.

His Honour concluded that it was not necessary that the trustee actually distribute cash or other property, and that a distribution could be made by the creation of an indebtedness by the appropriate resolution and accounting entries. Stevenson J found support in the *Wood v Inglis* and *Clark v Inglis* cases in which at least implicitly it had been assumed that it was possible for a trustee to make a distribution by crediting the beneficiaries' loan accounts. His Honour therefore concluded that an effective distribution had been made by the resolution, coupled with the crediting of the loan accounts, and that the trustee had thereby become indebted to Mr and Mrs Nemes for the amount of the distribution.

From the decision of Stevenson J, the trustee appealed to the Court of Appeal (*Fischer v Nemeske Pty Limited* [2015] NSWCA 6). The decision of the Court (Beazley P, Barrett and Ward JJA) was given by Justice Barrett.

In the Court of Appeal the trustee now emphasised the terms of the trust deed, and that it was an impossibility under the law of trusts that a distribution could be effected without a transfer of property. The trust deed's authorisation to "advance" or "raise" the capital of the trust, and to "pay" or "apply" the same could, it was argued, only occur through a change of legal title in property of the trust. It was argued that if the *Inglis* decision was to be taken as authority for the proposition that a trustee could make a capital distribution of property by crediting loan accounts, then it had been wrongly decided. However, it was noted that in *Inglis* this argument, about the necessity for a transfer of ownership of trust property to effect a distribution of income or capital, had not been directly raised or argued.

Before the Court of Appeal the executors contended that it was legitimate to view the resolution of the trustee and the accounting entries as reflective of a distribution by the trustee to Mr and Mrs Nemes, and a loan of those distributed moneys back to the trustee, thus giving rise to the loan liability. The books of the company reflected the final position of the parties in that situation, namely the assets continued to be held by the trustee, not having been liquidated and paid out in cash. Notionally the company had advanced to Mr and Mrs Nemes the distributed sum, but had borrowed it back, thereby creating its indebtedness to the beneficiaries. It ought not to be an objection that the parties had not physically handed the money back and forth for each step of the process.

The leading decision in the Court of Appeal by Barrett JA noted that some of the language used in the resolution of the trustee appeared borrowed from the company law context, but that it was important not to simply dismiss the legal efficacy of what had occurred as a misguided attempt to apply company law concepts, but to determine whether the words drawn from a company law context would nevertheless have meaning in regard to a trust.

Barrett JA referred to the decision of the Western Australian Court of Appeal in *Chianti Pty Limited v Leume Pty Limited* (2007) 35 WAR 488, in which the Court of Appeal concluded that the crediting to the beneficiaries' accounts of distributions gave rise to debt actionable by the beneficiaries. However in *Chianti* the trust deed empowered the trustees to pay, apply or set aside the income, and specifically provided that it might be effectually done by placing the amount to the credit of the relevant beneficiary in the books of the trust. No such words

appeared in the Nemes Family Trust Deed. Barrett JA relied for a broader proposition on *Re: Baron Vestey's Settlement; Lloyds Bank Limited v O'Meara* [1951] Ch 209, which held that income could be applied for beneficiaries by the trustees resolving that the income belonged to certain beneficiaries in certain proportions.

Barrett JA noted that in *Chianti*, Buss JA had read the decision of North P of the New Zealand Court of Appeal in *Commissioner of Inland Revenue v Ward* [1970] NZLR 1 at 15, as authority for the proposition that a resolution deliberately arrived at and recorded, is itself sufficient to effect an immediate vesting of a specific part of the trust income in favour of the relevant beneficiary. Barrett JA applied that principle in regard to the Nemes Family Trust's resolution to advance capital. His Honour concluded:

> "There is nothing anomalous about the concept that a trust fund is held, to an extent defined in money terms, for one beneficiary to the exclusion of others even though the assets in the trustees' hands do not include money of the relevant amount" (per Barrett JA at [63]).

As found by Barrett JA in *Nemeske,* and as discussed by Buss JA in *Chianti*, the ultimate legal effect of the trustee's determination was not the creation of a debt owed by the trustees to the beneficiary in a fashion analogous to a corporate declaration of a dividend. In the *Chianti* case Buss JA concluded that the entitlement of the beneficiary to demand the money from the trustee where there had been a determination that it should be distributed in the beneficiary's favour was as an action for money had and received. It was not necessary to bring an equitable action in circumstances where no further conduct was required of the trustee to render the moneys payable other than simply payment itself, or where the trustee had acknowledged that the money was owed (*Chianti* at [59] and [67]). Barrett JA applied similar reasoning (at [61]).

On the approach taken by Barrett JA and Buss JA, it was not essential to conclude that there had been a notional distribution of the advance of capital, followed by a loan by the beneficiary back to the trustee of that distributed sum. However, while their legal analysis was subtly different, the practical consequences were identical, namely that by resolution to distribute, coupled with a written acknowledgment in the accounts of a distribution to the beneficiary, and a recording of a loan, there was sufficient acknowledgment by the trustee to give rise to an indebtedness enforceable by an action for moneys had and received.

UPE's in the High Court

After defeat in the New South Wales Court of Appeal, Mr Fischer and his co-litigants obtained special leave, and appealed to the High Court of Australia. The appeal was only narrowly defeated, French CJ and Bell J, together with Gagelar J by a separate judgment, determined to dismiss the appeal, while Kiefel and Gordon JJ would have upheld it.

While the decision authoritatively decides that at least in some circumstances, unpaid distributions will be enforceable, and certainly rejects the contention that only an actual transfer of a portion of the trust fund will give rise to an effectual distribution of income or capital, the judgement does not resolve all of the doctrinal issues.

The Modern Law of Trusts leaves a wide unregulated zone in which a settlor and trustee may agree in regard to the powers and obligations of a trustee. Consequently, questions regarding trustees' powers begin, and often end with the terms of the trust deed itself. On one view, the decision in *Fischer v Nemeske* simply decided the meaning of the term "advance" in the context of the relevant deed, but that is perhaps an over-simplification. Certainly the appellants contended that a substantive doctrine prevented trustees making an advance other than by way of paying over or separating from the fund the money or property the subject of the advance.

French CJ and Bell J noted in the context of a relevant deed that the terms "advance" and "advancement" were used in quite different senses. The first referring to an action that the trustee might take, the second referring to the purpose, namely an advancement of a beneficiary that could be served by the action. They concluded that the ordinary meaning of the word "advance" extended to the creation of equitable and legal rights binding the trustee, and requiring for their enforceability the trustee's ability to resort to trust capital or income.[3] Thus from this meaning for the term "advance", it followed that the power encompassed creating in favour of beneficiaries a vested absolute equitable interest realisable by payment out to the beneficiaries, or by an action for money had and received, and this could also be supported by a covenant to pay.

French CJ and Bell J also drew support from observations in several cases suggesting a result may be within power where that result could be achieved by several steps, each one of which was indisputably within power. Thus in *Pilkington v Inland Revenue Commissioner* [1964] AC 612 at 639 in response to a contention that trustees did not have power to resettle a portion of a

[3] At [21]

trust, Viscount Radcliffe noted that there was no doubt that trustees could have sold a portion of the fund to a consenting party paying the money over pursuant to a new settlement with appropriate instructions. Likewise in *Re: Collard's Will Trusts* [1961] Ch 293, where trustees were undoubtedly empowered to advance cash to an expectant contingent beneficiary to enable him to purchase a farm which was part of the trust estate, they were held entitled to convey the farm directly to the beneficiary on the principle that the Court will not insist on circuity of action if the same result can be achieved by direction action.

Thus French CJ and Bell J concluded that the creation of a debt to be satisfied out of the property of the trust was a means of effecting an advance of the capital of the trust. While they do not say it in so many words, they appear implicitly to have endorsed the argument that this was a legitimate means of making an advance to a beneficiary in circumstances where the trustee could have advanced the sum and borrowed it back.

In regard to the argument that the trustee's resolution gave rise to a binding obligation on the trustee, enforceable by way of an action for monies had and received, French CJ and Bell J applied the reasoning and conclusion of Buss JA from the Western Australian decision in *Chianti Pty Limited v Leume Pty Limited.*[4] The existence of that common law action did not depend upon the relevant sum being held as, or represented by cash at bank, or some other monetary sum. The declaration and acknowledgement by the trustee has itself the legal effect of vesting a specific part of the trust fund in the beneficiary even though that sum simply represents a part of the trust fund and is denominated only by its monetary value.

The point just made is what principally separates the majority views from those of Kiefel and Gordon JJ. In response to the question, what is it about the trustee's declaration and acknowledgement to the beneficiary which created the relevant legal obligation enforceable by the action for money had and received, the answer is, that this is the legal effect of such conduct by the trustee. The majority of Judges are effectively declaring that the legal rule inherent in the older authorities is to such effect, and that it does not depend upon the way in which the trustee has itself described its actions, if it is clear that an intention to make a relevant advance and acknowledgement can be discerned.

Justice Gagelar noted that the appellants argued that a power of advancement even if it did not involve transfer of part of the trust fund, could nevertheless only be effective if it intended to

[4] (2007) 35WAWAR 488

effect an immediate alteration of the beneficial ownership of specific trust assets, and could not be effective where it merely purported to confer rights to a specific sum of money to be paid out of the trust fund if not itself held in cash. This argument had numerous difficulties not the least of which had been the recognition that an absolute beneficial entitlement to some part of a fund defined by reference to a sum of money to be paid out of the fund, irrespective of the form in which the assets were held, had been endorsed by the High Court in *MSP Nominees Pty Ltd v Commission of Stamps* (1999) 198 CLR 494.[5]

Gagelar J noted that there were other ancillary powers contained in the trust deed including a power to raise out of capital or income any sum or sums from time to time required, and a power to sell the whole or any part of the settled fund or other investments, for such price or prices and on such terms as the trustees think fit, and powers of appropriation. These ancillary powers were sufficient to permit the subsequent liquidation of the non-monetary assets in order to meet the entitlement of the beneficiary.

In regard to the doctrinal issue concerning the nature and entitlement of the beneficiary's action for monies had and received, Gagelar J dealt with the argument for the appellants that such an action only existed where the relevant assets were held on a "bare trust" by which they had meant one in which the trustee had only legal title and no duties other than those minimal duties by virtue of the office of trustee. The appellants argued that where the trustee held the assets subject to the terms of the settlement, this could lead to potential conflict between the rights of the entitled beneficiary on the one hand, and the obligations of the trustees under the settlement on the other. However, they provided no example of such conflict. Indeed, it was argued, harking back to the separation of law and equity, that if there were any entitlements of the trustee to, for instance, indemnity from the fund, the beneficiary should be relegated to an action in equity, against which the trustee's equitable defences could be set off. The simple answer to this is that the acknowledgement of the trustee of the obligation to the beneficiary does not lead to an inconsistency with the trustee's obligations of office, whether under a bare trust or where those obligations are spelt out in the terms of settlement.[6]

Justice Kiefel and Justice Gordon, although giving separate reasons, were in general agreement as to why the appeal should have been upheld. Each referred to the fact that the resolution of the trustee had purported to distribute to beneficiaries the asset revaluation reserve. It was

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[5] See Gagelar J at [100]
[6] See Gagelar J [111]

indisputable that this was simply an accounting entity, it was not an object that could be distributed if one read the resolution literally. The Primary Judge had little difficulty in determining that properly understood the resolution was one that purported to distribute a sum of money equal to the asset revaluation reserve, namely $3,904,300. However, Gordon J concluded that this was insufficient to bring the matter within the terms of the deed which empowered only the advance of income or capital.

Further, Gordon J criticised the trustee's resolution as not having effected any immediate vesting of title to some property in the beneficiary. Her Honour concluded that simply crediting amounts to a beneficiary in the trust accounts was not sufficient to effect an immediate vesting, and no power of advancement had been exercised because no part of the funds purportedly advanced was separated from the corpus of the trust.

Kiefel J made similar criticisms of the resolution of the trustee concluding that it could not be assumed that the trustee had intended to set aside, allocate, or otherwise apply trust property, rather it appeared that the trustee intended to retain all of the property under its control after the resolution.

Turning to the question of whether the conduct of the trustee had given rise to an action for money had and received, Kiefel J concluded that the conduct of the trustee was insufficient. Her Honour, however, did not engage in an analysis of the reasoning of Buss JA from the *Chianti* decision, and it is not entirely clear why she rejected the reasoning of the majority in that regard. Likewise, Justice Gordon also rejected the reasoning and analysis of Barrett JA in the Court of Appeal suggesting that only in circumstances where there was nothing left for the trustee to do but to pay over the fund, would it give rise to the action for money had and received, but Her Honour's analysis does not grapple with the authorities analysed by Buss JA, Barrett JA and the majority.

What has the *Fischer v Nemeske* Case Decided?

The *Fischer v Nemeske* decision has clearly held that it is possible for trustees to make distributions to beneficiaries without immediately paying over the sum to be distributed and without needing to separate that sum from the corpus of the trust. The decision has also held that it is possible to make a distribution giving rise to an enforceable entitlement on the part of the beneficiary by the creation of a debt owed by the trustee to the beneficiary payable out of

the funds of the trust. In thus holding that it is possible to create so-called UPEs, the Court has perhaps vindicated the status quo, although put it on a firmer legal footing.

The case, however, has also highlighted two crucial issues that must be resolved when determining the validity of UPEs and the answers will not necessarily always be the same as those given in *Fischer v Nemeske*.

The first issue directs attention to the powers of the trustee to make a distribution without immediate payment or transfer of trust property. In the first instance the power of the trustee is derived from the terms of the trust deed. Although in some cases deeds have expressly provided a power to make advances by way of the creation and crediting of beneficiary loan accounts, this is not typical, and more usually the powers of trustees are expressed in general terms, including powers to "advance", "raise", "pay", or "apply". Subject to the usual caution about treating decisions as authoritative in regard to the meaning of words without regard to context, it may be taken that in at least many instances, the term "advance" will be found to have empowered trustees to make a distribution by appropriate declarations and acknowledgements of debt to the relevant beneficiary.

In light of the reasoning of the majority, it is also relevant to examine the whole suite of powers available to a trustee to determine whether the distribution claimed to have been effected could have been arrived at by using a combination of such available powers.

In regard to this latter issue, it is important to keep in mind the quite extensive powers conferred upon trustees pursuant to provisions such as those in Part 2 Division 2 of the *New South Wales Trust Act* 1925, many of which can supplement or act together with powers conferred under the trust deed. In this litigation the executors had sought to rely upon s.38 of the *Trustee Act* which at least superficially appeared to confer upon a trustee who had power to pay or apply capital money for any purpose, a power to raise the money required by sale, conversion, calling in, or mortgage of any part of the trust property. This provision was adverted to by Justice Stevenson at first instance.

In the Court of Appeal, in a somewhat cryptic passage, Barrett JA held that s.38 allowed the creation of a mortgage to raise money only for closely confined purposes relying on *Re: Suenson-Taylors Settlement Trusts* [1974] 1 WLR 1280, and concluded that it did not allow the grant of a mortgage as security for a pre-existing unsecured obligation. He thus concluded that

the charge created under the deed of charge was invalid, although the separate covenant to pay had remained enforceable.

The reasoning of Barrett JA in regard to the charge is worthy of further examination. It is not superficially obvious why the authority relied upon by Barrett JA should lead to the reading down of s.38 in the fashion he determined. This issue, however, was taken no further in the litigation.

The decision by the High Court may also be taken to have determined that the action against the trustee is clearly not an equitable one based upon the enforcement in equity of the trustee's obligations under the settlement. The majority appear to have endorsed the Court of Appeal's determination that the action for money had and received provides the juridical basis upon which a beneficiary is entitled to enforce a UPE. On the other hand, the reasoning of the majority appears at least consistent with the alternative analysis that the trustee may in some circumstances become indebted on a loan, if that is the way the transaction has been recorded. On a careful reading of the judgments, however, what the majority appear to be saying is that although the possibility of payments; followed by borrowing back by the trustee may enable one to determine whether or not the trustee has acted within power, where the trustee has made an advance within power, albeit not paid, an indebtedness has been created, and an action may be brought for monies had and received.

Beneficiary's Rights

A number of commentators have expressed surprise that the High Court should have found a beneficiary could have an accrued and enforceable action for moneys had and received against a trustee for an advance where the fund remains held in some illiquid form, and the subject of the advance has not been separated from the corpus in any fashion. To those surprised by this finding, several responses can be made.

Firstly, as noted by Gageler J, the interests of a beneficiary need not be simply to a proportionate part of a fund. There can be circumstances in which a beneficiary's interest in the fund is measured by a precise money sum. This still leaves open two possibilities. To the extent that the beneficiary's interest is an equitable one in the fund, albeit measured by a fixed amount, any fluctuations in the value of the corpus may expand or diminish the value of the interests of others, but not the holder of the fixed benefit. If the fund suffers a substantial loss of value, the manner in which that loss is to be shared, will no doubt be a matter of the proper

construction of the trust deed. However, the trustee's liability will still be limited to the extent of the fund.

The second issue arises in circumstances where the trustee has rendered itself liable in an action for moneys had and received. There is no reason why in that circumstance the trustee's liability would necessarily be limited to the value of the fund. Nevertheless, the trustee would have access to the fund to the extent it was sufficient, to indemnify itself in regard to its liability. If the fund was insufficient, the trustee could nevertheless have a personal liability on the common law action.

It ought not be surprising that a trustee by the exercise of a power could place itself in a position where it has a liability unsupported wholly or partly by funds held on trust. Any trustee contracting on behalf of a trust exposes itself to a personal liability under the contract which may or may not be supported by the trustee's right of indemnity from the fund.

However, if the beneficiary's entitlement lies in an action for money had and received against the trustee, then this in turn raises the question of whether the defences to *quasi* contractual claims such as money had and received, can be raised by the trustee to the beneficiary. In particular, does the action for moneys had and received by a beneficiary against a trustee, now form part of the broader modern law of restitution, and lead one to conclude that the defence of "change of position" ought be available to a trustee. Would this defence be available if through no fault of the trustee, the fund to which it was intended to have recourse to make payment of the advance, had been lost.

The flexibility of the change of position defence declared by the High Court in *AFSL v Hills Industries Limited*[7], and indeed the tracing of the equitable roots of the claim for restitution of money had and received, all suggests that this defence ought be available to a trustee.

Some Practical Implications

Thus far, the decisions just discussed suggest that the creation by accountants of book entry loan accounts has generally been successful to achieve distributions of income or capital from

[7] (2014) 253 CLR 560

trusts to beneficiaries, although it has called for some complex legal analysis to establish a precise basis upon which the effectiveness of these transactions can be understood.

Apart from the tax implications of UPEs the *Inglis* litigation and the *Fischer v Nemeske* litigation show that the issue may be of some significance in estate litigation. In both of those cases the key question was whether or not the relevant UPEs were enforceable and thus constituted assets of the deceased's estate, or whether the purported distributions could be avoided, thus enriching the trust that had been associated with the deceased.

Depending upon the wording in the trust deeds, the outcomes in future cases may not always be the same as the outcome in *Fischer v Nemeske*. The quite different wording of the deed, considered by Justice Daubney in *Wilson v Chapman* was undoubtedly correctly decided even in light of *Fischer v Nemeske* given the quite different terms of the testamentary trust in that case.

In light of the *Fischer v Nemeske* decision, one may well expect more scrutiny of the validity of UPE's where claimed to be part of the property of a deceased.

Further, while Mr Nemes and his advisers might be forgiven for not having foreseen the complex legal controversy in which his estate became enmeshed, a careful consideration of the validity of UPE's at the time of making a will might avoid the risk of an estate becoming embroiled in complex litigation.

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