

Article Information

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A Family Divided: New obligations on trustees of discretionary family trusts

When a trustee of a discretionary trust is appointed, it is assumed that the power conferred on it is absolute and unfettered. So long as the trustee exercises its discretion with the following essential components, then the courts will not have cause to intervene[1]:

- ***acting in good faith;***
 - ***acting with real and genuine consideration; and***
 - ***in accordance with the purposes for which the discretion was conferred.***
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If the trustee has not acted with these elements in mind, then any decision made by it may be challenged. Although a decision may not be impugned on the basis that it was unfair, unreasonable or unwise, it may be reviewed for want of properly informed consideration. If the consideration is not properly informed, it is not genuine[2].

In the recent Victorian case of *Owies v JJE Nominees Pty Ltd*[3], the Victorian Court of Appeal found that when making annual income distributions from a discretionary trust, the trustee had not given real and genuine consideration in the exercise of its discretion which had miscarried. That is, there was no bona fide inquiry and genuine decision making[4]. In our previous [Insight](#) we discussed this consequence for SMSF trustees which the Victorian Courts have now extended to trustees of *inter vivos* discretionary trusts.

The Owies Family Trust was established in 1970 by John and Eva. They were not only directors of the corporate trustee but also appointors of the trust. Aside from John and Eva, there was a relatively small class of beneficiaries, namely their three children (Michael, Deborah and Paul) and a few other family relatives. John and Eva were estranged from Deborah and Paul for substantial periods of time during which they would have no or minimal contact with them.

In this case, the Court considered whether income trust distributions between 2015 to 2019 were made by the trustee without any real and genuine consideration of the needs of Deborah and Paul as potential beneficiaries of the trust. On the face of it, it appeared that the trustee had devised a particular formula when making income distributions from 2015 to 2018. Throughout this period, income distributions were made by the trustee as to 40% to John, 40% to Michael and 20% to Eva. There was no deviation from this pattern until 2019 when the trustee distributed 100% of the income to John and made a capital distribution to Deborah by way of a residential unit.

The fact that Deborah and Paul had been estranged was not enough to disavow them of a distribution. At the very least, their needs should have been examined.

The Court found that the trustee exercised its discretion without real and genuine consideration for the needs of Deborah and Paul for the following reasons:

- the trustee made no enquiries of Deborah and Paul (Deborah's health and financial situation were particularly precarious);
- aside from 2019, the income distributions by the trustee were in the same proportions (in contrast to its continuing obligation to consider the distribution of income for each accounting period);
- Deborah had strong claims to a favourable exercise of discretion (this did not mean a distribution had to be made to

- her but failure to do so and repetition of the same formula in each year up to and including 2018, strongly pointed to a lack of due consideration of her position notwithstanding the capital distribution made to her in 2019);
- the extreme nature of the distribution in 2019 (providing additional merit to Deborah and Paul's argument).

As such, the Court held that the income distributions by the trustee in 2017 and 2019 were voidable (and not void as no application was made to set them aside). There were extenuating circumstances that warranted not voiding the 2015, 2016 and 2018 distributions. The breaches of duty were found on appeal to be so egregious that the Court even deemed it necessary to remove the trustee as it would not be in the best interests of the beneficiaries for it to continue in office.

The outcome of this case will significantly impact the decision making of trustees of discretionary trusts who find themselves in similar situations where the family unit has been derailed.

It is clear that careful consideration and procedures must be put in place to ensure that the trustee exercises real and genuine consideration for each distribution it makes from a trust otherwise it could be challenged by aggrieved beneficiaries. At the very least, the trustee must be seen to actively inform itself of the differing needs and circumstances of likely key beneficiaries regardless of whether the family unit is still intact.

[1] *Karger v Paul* [1984] VR 161

[2] *Finch v Telstra Super Pty Ltd* (2010) 242 CLR 254

[3] [2022] VSCA 142

[4] *Telstra Super Pty Ltd v Flegeltaub* (2000) 2 VR 276