Trustee Act 2000 - key provisions

Synopsis: The statutory provisions.

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Background and commencement

The law governing the powers and duties of trustees, particularly the relevant provisions of the Trustee Act 1925 and the Trustee Investments Act 1961 (TIA), has not always kept pace with the evolving social and economic role which trusts now fulfil.

For trusts subject to the law of England and Wales, the Trustee Act 2000 (TA), which came into force on 1 February 2001, repealed most of the outdated provisions of the TIA and introduced a number of other reforms of trust law.

The TA contains two types of provision.

Firstly, it provides default powers to trustees – this means that the powers will only apply if there are no express powers included in the trust which exclude the statutory powers. The importance of the TA is therefore greatest for defectively drafted trusts (especially all the trusts giving only restrictive powers, certain trusts created in the so called "DIY Wills" and to all trusts arising on an intestacy.

Secondly, the Act imposes certain statutory duties on trustees which include the statutory duty of care (which can be excluded expressly for new trusts but applies to all existing trusts), as well as certain non-excludable duties, including a duty to take advice in making/retaining investments which applies to all trusts, regardless of when made and regardless of any other provisions.

Trustees and investments

Under the TA, the investment restrictions which previously applied under the TIA are replaced by a new general power of investment given to the trustees to permit them to invest in investments of any kind as if they were absolute owners (i.e. persons owning the property for their own benefit) of the assets of the trust (Section 3 TA).

However, this new and wide statutory power, which applies to trusts whenever created, is not totally unfettered (please see below) and it does not apply to all trusts, for example charitable trusts under which the trustees manage common investment and common deposit schemes, and occupational pension trusts (please see later).

The general investment power is in addition to any limited express power in the trust instrument, but is "subject to any restriction or exclusion imposed by the trust instrument" (except for trusts made before 3 August 1961). So, for example, for a post 2 August 1961 trust, if the trust instrument authorises the trustees to invest "only in authorised unit trusts" then the general power of investment would not apply.

On the other hand, if the trust instrument authorises the trustees to invest in shares quoted on the NASDAQ, but not the shares of Microsoft, then the general power of investment would apply subject to the restriction on investing in Microsoft. The general power of investment will, however, apply to an existing trust instrument that authorises the trustees to invest in accordance with the TIA.

Under the previous law, where trustees were not given powers of investment under the trust, trustees had to invest in accordance with the TIA. This meant that the trustees had to split the trust capital into two funds with at least 25% of the investments being invested in narrower-range investments (broadly interest-bearing securities) with the balance in wider-range investments (broadly equity-based investments).

Land and insurance policies were not permitted investments under the TIA. Now under the new general power of investment, insurance policies can be assets of a trust and, subject to the satisfaction of certain conditions, trustees have been given a specific power to invest in freehold or leasehold land in the UK.

From the foregoing it will be appreciated that it will still be necessary to examine the trustees' investment powers in order to determine whether a particular investment is a permitted investment.

As mentioned earlier, the general power of investment is not unfettered. Because the trustees are obviously not the absolute owners of the assets under their control then clearly the beneficiaries of the trust need protection from the risk that the trust fund will be lost or dissipated in unwise investments.

The trustees have always been subject to their fundamental duty to act in the best interests of all beneficiaries and avoid a conflict. The exercise of the new investment powers by a trustee will now in addition be subject to the new statutory duty of care in Section 1 TA – please see below.

In connection with making investments, the TA imposes two special duties on a trustee. The first duty is a duty to have regard to the need for diversification and suitability of investments to the trust - these are known as the "standard investment criteria" (Section 4 TA); the second is a duty to obtain and consider proper advice when making or reviewing investments. We will now consider these in more detail.

Diversification…

The duty to have regard to the need for diversification and the suitability of the trust investments was previously covered by section 6 of the TIA, and applied to all trusts – both those governed by the TIA and those outside it. Broadly speaking, these duties have been retained in the TA.

The requirement to diversify the trust fund means that, where appropriate, the trustees should use a spread of investments.

Suitability…

"Suitability" relates both to the kind of investment proposed and to the particular investment as an investment of that kind. It includes considerations as to the size and risk of the investments and the need to produce an appropriate balance between income and capital growth to meet the needs of the trust. It also includes any relevant ethical considerations as to the kind of investment that is appropriate for the trust.

There is a further requirement for the trustees to keep the investments of the trust under review and to consider whether, in light of the "standard investment criteria", they should be varied.

Duty to obtain and consider proper advice...

Previously, as far as the duty to obtain and consider proper advice was concerned, the TIA only contained provisions regarding the advice where trustees were investing under that Act. Further duties to obtain advice have been considered by the courts, e.g. that the trustees should obtain advice on any matters on which they are not competent to decide for themselves.

The following provisions in the TA govern the need of trustees to obtain advice (Section 5 TA)...

- *before exercising any power of investment*, the trustees must obtain and consider proper advice about the way in which that power should be exercised, having regard to the need for diversification of investments of the trust and the suitability to the trust of the proposed investment;

- *when reviewing the investments of the trust*, the trustees must obtain and consider proper advice about whether, having regard to the "standard investment criteria", the investments should be varied.

The requirement to obtain advice does not apply if the trustees reasonably conclude that in all the circumstances it is unnecessary or inappropriate to do so. This may cover a case where, for example, the trust fund is small and the cost of advice would outweigh the benefit of it or one of the trustees is suitably qualified and can provide this advice at reasonable cost.

For these purposes proper advice would be the advice of a person who the trustees reasonably believe to be qualified to give it by their ability in, and practical experience of, financial and other matters relating to the proposed investment.

This requirement to obtain and consider proper advice applies to all trusts not just those into which the general power of investment is imported.

The TA provisions as they relate to investments do not apply to occupational pension trusts which are governed by their own statutory rules – please see later.

Duty of care

Regardless of any provisions in the trust instrument, trustees have always been subject to certain general duties of care. Their fundamental duty is, of course, to exercise their powers in the best interests of the beneficiaries of the trust. As well as having a duty to invest trust funds, trustees must not profit from their office, they must not cause loss to the trust, they must act impartially between the beneficiaries and must treat all the classes of beneficiary fairly. In particular, where some beneficiaries are entitled to income and others to capital (perhaps in the remainder) they must invest to achieve some income and capital growth.

These general duties have been established over the years, largely through case law. At common law the standard of care expected from the trustees is that of the ordinary prudent man of business. But trustees who are paid for their services as professional trustees are expected to meet a higher standard of care than other trustees.

One of the aims of the reforms in the TA is to improve the powers of trustees who do not have wide specific powers under the trust. However, the law recognises that, in conferring wider administrative powers upon trustees, an appropriate balance must be struck between extending statutory powers on the one hand and the imposition of safeguards to ensure that trustees properly exercise those powers on the other.

With this in mind, and with a view to bringing consistency and certainty to the standard of competence and behaviour expected of trustees, Section 1 of the TA imposes a new single statutory duty of care which applies when trustees carry out certain functions. This includes...

- exercising their powers of investment;
- exercising powers of delegation or powers to employ nominees and custodians;
- exercising the power to insure trust property.

When the statutory duty of care applies, a trustee must exercise such care and skill as is reasonable in the circumstances having regard in particular to any special knowledge or experience that they have or hold themself out as having; and if they act as trustee in the course of a business or profession, to any special knowledge or experience that it is reasonable to expect of a person acting in the course of that kind of business or profession.

For example, if a trustee was an investment-banker they would be expected to adopt a higher standard of care in buying stocks and shares for a trust than a trustee who was, say, a window cleaner.

In all of this it is important to remember that the statutory duty of care is not intended to impose any obligations or restrictions on the trustees in exercising their discretions under the trust. The decision whether to exercise a discretion remains, as it is now, a matter for the trustees to determine. However, once the trustees have decided to exercise a discretionary function which is subject to the new statutory duty, the manner in which they exercise it will be measured against the new duty of care.

Unlike the duties in relation to investments, the statutory duty can be excluded (obviously this applies only to trusts created since February 2001) by a specific provision in the trust instrument. In such a case there would normally be some form of modified duty of care.

It should also be remembered that the common law duty of care (to act as a prudent man) has not been repealed by the TA 2000, and so continues to apply.

Trustees' powers of delegation

The Trustee Delegation Act 1999 deals only with delegation of functions to agents by individual trustees. Delegation by trustees as a collective body is an entirely separate issue and is dealt with in the TA 2000.

As in considering the trustees' powers of investment, the first aspect to consider is the express powers of the trustees in the trust instrument. Where the trustees have wide powers of delegation no problem arises. However, what is the position when the trustees have no such powers?

In the past the law on trustee delegation was that trustees could not delegate their dispositive duties and powers under a trust. This would include their power to distribute the trust property to the beneficiaries or their fiduciary discretions, such as the selection of trust investments, or the decision whether or not to sell trust property. However, trustees could delegate their ministerial functions in that they could employ an agent to transact any business or do any act that was required in the administration of the trust.

Of course, this general rule only applied to the extent it was not displaced by an express power to delegate granted in the trust instrument and these days most modern trusts would grant such an express power. But there are a considerable number of trusts, and in particular charitable trusts, where no express powers of delegation are given.

Under the previous law, therefore, whilst certain limitations on trustees' powers of delegation would be wholly appropriate, others constitute a serious impediment to the administration of trusts.

The TA provides that, subject to the expression of any contrary intention in the trust instrument, trustees should have power to delegate to agents their powers to administer the trust, including their powers of investment and management. However, they should have no authority to delegate their powers to make decisions as to...

- the distribution of the income or capital of the trust for the benefit of its beneficiaries;
- the appointment of trustees;

- the delegation of their powers;
- the allocation of fees to capital/income.

While the granting of wider powers of delegation is to be welcomed, the issue of striking a balance between the duty of care and wide powers of delegation has been addressed by the TA which provides for restrictions on the terms of any agency agreement. In this respect, whilst there is no restriction on who trustees can appoint as agents, there is a duty of care on trustees exercising this power.

Trustees cannot...

- allow an agent to appoint a substitute;
- restrict an agent's liability to the trustees; or
- permit the agent to act in a case where a conflict of interest may arise.

Clearly this could cause difficulties as regards the ability of trustees to appoint discretionary fund managers whose terms of engagement absolve them from liability in certain cases. In order for trustees to avail themselves of such services, section 14 of the TA permits trustees to avoid these difficulties in such cases where the trustees have decided that *it was reasonably necessary for them to delegate on such terms*. The employment of a discretionary fund manager is therefore possible but subject to the trustees satisfying themselves on this aspect.

The TA also introduced special requirements where delegation to agents who provide "asset management functions" occurs. For this purpose, "asset management functions" include advice on the investments of the trust fund, the acquisition of property and managing property. In these circumstances, the trustees need to...

(a) formulate and keep under review a policy statement that gives guidance as to how the delegated functions should be exercised with a view to ensuring that they will be exercised in the best interests of the trust...

- secure the agreement of the agent to act in accordance with the policy statement; and
- from time to time assess whether the agent is doing so.

The policy statement in (a), which is an investment statement, must be in writing. Furthermore, it must be prepared before the agent acts for the trustees.

For example, if trustees delegate their powers of investment to an agent, they must enter into an agreement with the agent at the outset setting out the investment objectives of the trust. Such an agreement may include considerations as to liquidity of assets to meet the needs of the trust, the desired balance between capital growth and income yield, and any "ethical" considerations relevant to the investment policy of the trust. The policy statement may expand upon the manner in which the duty to invest and review investments (having regard to the "standard investment criteria") should be discharged in respect of the trust.

As far as delegation is concerned, special provisions have been introduced for charitable trusts and occupational pension trusts (please see later).

Miscellaneous

(i) Before enactment of the TA, there was a general prohibition on trustees employing nominees and custodians, based on the requirement that the trustees must keep the trust assets under their own control.

Sections 16 and 17 of the TA, which do not apply to occupational pension trusts, empower trustees to appoint a person to act as their nominee or as a custodian, as appropriate, provided that such person carries on a business which consists of, or includes, acting as a nominee or custodian as the case may be. Special restrictions on the kind of nominees or custodians that can be appointed apply to charitable trusts.

The TA further gives trustees a power to appoint as a nominee or custodian either one of their number, if that one is a trust corporation, or two or more of their number in any event to act as joint nominees or joint custodians.

To balance the extended power with an appropriate safeguard, trustees must, so long as the appointment of a nominee or custodian continues, keep under review the arrangements relating to it and the manner in which those arrangements are carried out.

(ii) Section 34 of the TA gives trustees power to insure in full any property which is subject to the trust against risks of loss or damage due to any event.

(iii) It is a well-known fact that trustees cannot benefit from their office as trustee unless there is an express provision allowing them to charge fees or receive other remuneration such as commission. In the absence of an express provision, trustees cannot receive any fees and any commission earned by a trustee, for example, for making recommendations on investments, has to be paid back to the trust. Rather obviously, if a trust does not contain a charging or remuneration clause, no professional trustee would be willing to administer the trust.

Accordingly, the TA provides that where there is more than one trustee, they should have power to authorise one or more of their number to receive reasonable remuneration for their services to the trust if they are acting in a professional capacity and this power applies in relation to all trusts, other than charitable trusts, whenever created.

With regard to trust corporations, except for charitable trusts a trust corporation will be entitled to receive reasonable remuneration out of the trust funds for any services it provides to or on behalf of the trust whether or not it acts as a sole trustee.

Pension trusts

The primary piece of legislation for occupational pension scheme trustees remains the Pensions Act 1995 as amended by Pensions Act 2004. In particular, section 34(1) of the Pensions Act 1995 grants occupational pension scheme trustees wide investment powers. It should be noted that the section does not apply to occupational pension schemes established by any means other than under a trust, but such schemes are rare and generally confined to insured schemes in any event.

However, the scheme need not be a registered scheme to benefit from the wide investment power in section 34(1). With regard to investment powers, the provisions in the TA and the repeal of most of the TIA were not relevant to occupational pension scheme trustees. Of course, trustees of pension schemes must be aware that whilst they have wide statutory investment powers, they are also subject to certain restrictions with regard to investments and, in particular, with regard to employer-related investments which continue to apply.

Substantial amendments to sections 35 (statement of investment principles) and 36 (regard to diversification and suitability) of the Pensions Act 1995 were introduced by the Pensions Act 2004.

Trustees of personal pension trusts are subject to the TA although in practice trust documents of such schemes would include all the relevant provisions in an express form.

The general statutory duty of care does not apply to pension trustees in relation to their investment powers or to their use of agents, custodians and nominees. This is largely because the Pensions Act 1995 already includes adequate provisions in this respect. However, the new statutory duty applies in other circumstances, for example, to the appointment and monitoring of third-party administrators, auditors and actuaries.

With regard to powers of delegation, as section 34 of the 1995 Act only gives the pension scheme trustees power to delegate their investment powers to an investment manager who is authorised under the Financial Services and Markets Act 2000, the new delegation powers under the TA apply to pension trustees as well as other trustees (other than charity trustees).

This is, however, subject to one caveat because of the special nature of pension trusts. In keeping with existing safeguards for the protection of beneficiaries of pension trusts, the power of delegation is qualified so that pension trustees may not delegate to the scheme employer or to any person connected with or an associate of the employer.

Charitable trusts

The new investment provisions apply to charitable trusts, with the exception of trustees managing common investment and common deposit schemes under the Charities Act 1993.

Trustees of charitable trusts are also subject to the statutory duty of care. As regards the other provisions of the TA, most apply in modified form.

Scotland

The Charities and Trustee Investment (Scotland) Act 2005 (CTI(S)A), which received Royal Assent on 14 July 2005 and came into force on 1 January 2006, extends the general powers of trustees along lines similar to those contained in the TA in England and Wales, subject to the satisfaction of the standard investment criteria. The legislation takes effect by amending section 4 of the Trusts (Scotland) Act 1921 and repealing certain provisions of the TIA.

The following is a summary of the provisions of the Act...

- Section 93(2) amends section 4 of the Trusts (Scotland) Act 1921 by adding a provision allowing a trustee to make any kind of investment of the trust estate (including an investment in heritable property). The effect is that trustees now generally have the same powers of investment as if they were the beneficial owners of the trust estate. Subsection (2) also provides a wide power for trustees to acquire heritable property for any other reason. These wider powers are subject to any restriction or exclusion imposed by other enactments and do not extend to certain categories of trustees (subsection (3)).

- Subsection (3) of section 93 continues the policy of the TIA in relation to pre-existing trust deeds. No term in a private trust deed made before the passing of the 1961 Act was to restrict the investment powers granted to trustees by that Act. The new general power in subsection (2) is similarly not to be restricted.

  In relation to trust deeds made after the passing of the 1961 Act, where the investment powers contained in the 1961 Act are conferred the trustees are to have the new general powers. But if trustees in existing post-1961 Act deeds or in future deeds are prohibited from making certain investments then these prohibitions will continue to apply. This is because section 4(1) of the 1921 Act, in which the new general investment power is inserted, authorises only acts which are not at variance with the terms and purposes of the trust.

- Section 94 CTI(S)A includes a number of provisions dealing with the exercise by the trustees of their power of investment. The first of these inserted section 4A of the Trusts (Scotland) Act 1921 and covers the duties trustees must follow before exercising the wider investment powers under section 93(2). They include the duty to have regard to the suitability to the trust of the proposed investment and the need for diversification – these are identical to the standard investment criteria used in the TA. There is also a duty (as under the TA) to obtain and consider proper advice before exercising the power of investment and when reviewing the investments of

- the trust. The meaning of “proper advice” and the exception to the rule are also similar to their English equivalent.
- Section 4B of the 1921 Act (inserted by section 94 CTI(S)A) deals with the trustees’ power to appoint nominees while section 4C deals with the power to delegate investment management functions. Again, these provisions are similar to their English equivalent.

Northern Ireland

In Northern Ireland the Trustee Act (Northern Ireland) 2001 came into force on 29 July 2002. This Act, broadly speaking, brings similar provisions to its equivalent in England and Wales ie. the TA. The main provisions of the Act are similar to the English equivalent, namely the wider power of investment, powers to appoint agents, nominees and custodians, power to purchase land, to insure trust property and to pay professional trustees. As in England, the Act also introduced a statutory duty of care.

In addition to the above, and this is something that is not included in the English Trustee Act, the Trustee Act (NI) 2001 also includes powers to appoint or replace trustees in certain circumstances, specifically where there is no-one eligible to appoint a new trustee and where a trustee has become incapable of acting because of mental disorder.

These provisions correspond to part 2 of the Trusts of Land and Appointment of Trustees Act 1996 which applies to England and Wales under which, in the circumstances described above, appointment or retirement of a trustee can take place at the instance of beneficiaries where all the beneficiaries are of full age and capacity and taken together as a group are absolutely entitled to the trust assets.

The Trustee Act (Northern Ireland) 2001 repealed parts of the Trustee Act (Northern Ireland) 1958 and the whole of the Trustee (Amendment) Act (Northern Ireland) 1962 (by virtue of which the TIA applies in Northern Ireland) as well as certain parts of other Northern Ireland legislation.