CHAPTER 6

THE INTERACTION OF TRUST AND THE EMPLOYMENT RELATIONSHIP

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Introduction

The early capitalist development of superannuation and its subsequent civilisation by the labour movement led to employer provision for employee retirement. In the modern age of superannuation the provision of superannuation continues to be intrinsically linked to the employment relationship. It is this relationship – the exchange of consideration for employment services – that triggers either directly or indirectly the creation of the superannuation trust. To this end, superannuation trusts subsist alongside and are interrelated with employer and employee relations. Commonly portrayed as a tri-partite relationship between employer, trustee and beneficiary, the level of employer participation in this relationship is a function of the relevant type of trust and the intention of the settlor in framing its terms.

At the far end of an employer participation continuum is the type of scheme offered by a financial institution where the nexus between the employer and the operation of the fund is extremely limited – the employer does no more than direct contributions to the fund. A board of directors appointed by the financial institution undertakes the management of the fund. At the opposite end of the continuum is the company superannuation scheme (otherwise termed an "employer-sponsored fund"). In this case, the employer is usually responsible for initiating the scheme and unlike the traditional settlor has a continuing role. The employer contributes on an ongoing basis and is usually involved in scheme management via representation at trustee level. Indeed, in some jurisdictions, notably Ontario, the employer may be completely responsible at "trustee level" for management of the scheme. Further employer involvement may also be contemplated by the terms of the scheme. In what is termed a "pure balance of cost scheme" the trust instrument casts responsibility for the solvency of the scheme, and thus the risk of investment, on the employer. Moreover, the trust instrument will often vest significant powers, and in turn significant control, in the employer. Examples include the power to amend the scheme (or at the very least, a power to consent to any amendment), the power to augment benefits, and the power to wind up the scheme.

At a judicial level it is well recognised that the employment background is one of the main factors that serves to distinguish the superannuation trust from the conventional family

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1 Re UEB Industries Ltd Pension Plan [1992] 1 NZLR 294 at 307 per Hardie Boys J.
trust. Traditionally, beneficiaries as objects of the settlor's bounty are volunteers. In the commercial scenario of the superannuation trust the emphasis is on bargained nature of the relationship rather than that of gift and the concomitant fact that beneficiaries have given valuable consideration for their interest. With this in mind, Lord Browne-Wilkinson, although conceding that it is not the generally accepted view, has gone so far to suggest that the relationship between the various stakeholders in a superannuation trust is one fundamentally of contract.

Judicial recognition of contractual considerations within the context of the general law of trusts has led some commentators to argue, despite some judicial dicta to the contrary, that a distinctive set of trust principles are applicable to superannuation trusts. Notably in this respect, Milner has proffered the further suggestion that the superannuation trust is a new form of trust which is characterised by the difficulty of separating the employer (as settlor) and the trustee. Thus, whilst there is still the segregation of trust assets from those of the employer-settlor, the segregation of interest is not present. The trustees are bound to the employer/settlor by various means relevant to the workings of the trust.

There is the further tension that the appointed trustee may be a member of the fund itself. Milner argues that "the new" trust form is a hybrid body in which there is no complete separation of interests between either the relationship of: (i) employer and trustee; or (ii) trustee and beneficiary. This leads her to conclude that these distinctions dictate that a "careful and perhaps distinct approach" be taken in the application of general legal principle.

Against this background the issue that arises, in each of the jurisdictions canvassed by this thesis, is the extent to which the incidents of the employment relationship should affect the principles of law that give shape and define the trust relationship. The preliminary response, consistent with the conclusions of Chapter 4, is that of priority of trust principle.

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1 Mettoy Pension Trustees Ltd v Evans [1990] 1 WLR 1587 at 1610 per Warner J; Imperial Group Pension Trust Ltd v Imperial Tobacco Ltd [1991] 2 All ER 597 at 605 per Browne-Wilkinson VC.
3 See, for example, Wilson v Law Debenture Trust Corp plc [1995] 2 All ER 337 at 345 per Rattee J.
4 See, for example, Moffat, "Pension Funds: A Fragmentation of Trust Law?" (1993) 56 MLR 471 at 494.
The trust is the “chosen one”; the principles that give substance to the mechanism should be used in priority to all others in the resolution of tension and conflict in the law. However, the superannuation relationship framework (“SRF”) requires a deeper and more structured level of analysis. Whilst the foundation of the SRF is that trust is the ideal vehicle for the delivery of superannuation objectives, it is not the “perfect” vehicle. Attention must be given to the suitability of various trust principles in their application to superannuation schemes. To this end, the SRF provides a two-tiered framework of analysis applicable to both the present law and to proposed reform. The first inquiry is whether or not the principles applied in the superannuation context are those applied generally in respect of trusts. If so, it can be concluded that the first limb has been satisfied. If not, an assessment must be made as to whether or not the variation in principle can be justified on the basis of either the protective (or prudential security) limb, or the inapplicability limb, of the SRF. As to the future development of the law, where there exists concern or tension in the application of the relevant traditional trust principle, any suggested development or reform can be tested according to these SRF limbs.

Sir Robert Walker has commented recently that the “court has begun to work out how far trust law principles that were established and developed largely in context of family trusts are appropriate with or without modification to pension schemes”.8 It is these principles to which the application of the SRF is directed. To this end, this Chapter addresses five areas in which there are apparent tensions arising from the interaction of the employment relationship with trust principle: the general interpretation of trust deeds, the distribution of surplus, the amendment of trust deeds, and the bounds of employers’ and trustees’ powers and discretions respectively.

The customary example of a judicial willingness to consider the underlying employment relationship is the courts’ approach to the interpretation and construction of trust documents. In that the essence of every issue that arises in respect of a superannuation scheme involves an assessment of the relevant trust deed provisions, the issue of interpretation is a pervasive one. Hence, the approach adopted is to first consider the courts’ general approach and the principles utilised. Much of the remainder of this chapter deals with the application of the general approach to the specific issues mentioned above.

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Chapter 6: Trust and the Employment Relationship

### 6.1 The General Interpretation of Superannuation Trust Deeds

The overriding object of the court in considering the provisions of a trust deed, whether in a family or commercial trust, is to determine the meaning and effect of the words as intended by the settlor. In the words of Lord Upjohn:

> It is the duty of the court by the exercise of its judicial knowledge and experience in the relevant matter, [to exercise] innate common sense...to make sense of the settlor's or parties expressed intentions, however, obscure and ambiguous the language...used, to give a reasonable meaning to that language if it can do so without doing complete violence to it.

In addition to the invariable exhortation that words be given their natural and ordinary meaning and be considered by reference to the deed as a whole, two approaches have gained prominence specifically in the interpretation of superannuation trust deeds. The first is that the court's approach should be "practical and purposive, rather than detached and literal," and one that thereby tests competing permissible constructions against the consequences they produce in practice. Secondly, the constituent documents should be construed within their "matrix of fact." This requires consideration of the fact that superannuation funds are established against the background of employment and so must be interpreted against that background. In the oft quoted and almost hallowed words of

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10. *Re Courage Group's Pension Schemes* [1987] 1 All ER 528 at 536 per Millett J.


13. *Mettoy Pension Trustees Ltd v Evans* [1990] 1 WLR 1587 at 1610 per Warner J.

Warner J, this involves recognising that: 15

...beneficiaries under a pension scheme...are not volunteers. Their rights have contractual and commercial origins. They are derived from the contracts of employment of the members. The benefits provided under the scheme have been earned by the service of the members under those contracts and, where the scheme is contributory, pro tanto by their contributions.

Regard must also be had to the statutory requirements of the regulation of superannuation and common practices in the field of superannuation16 as either may reveal the rationale for the use of particular words or phrases, or their meaning.

Notwithstanding the courts' recognition of the special characteristics of superannuation trusts, especially the employment context in which they arise, the general approach to interpretation is entirely consistent with the first limb of the SRF. This is borne out by two points. First, the interpretative approach applied is that which is generally applicable to trusts and not one that results from the influence of the employment contract. Secondly, even when, during the process of interpretation, regard is had to the employment context, its influence is nevertheless limited by general principle. Each of these points is discussed in turn.

6.1.1 A GENERAL INTERPRETATIVE APPROACH

Although the general interpretative approach is typically considered a "contractual" approach, this does not stem from the influence of the employment contract. The approach applied is one applicable generally to trusts as well as to other instruments where the object is to determine the intent of the relevant parties. Indeed, it is inaccurate to view it as a purely contractual approach. The judiciary itself has recognised, specifically in respect of superannuation trusts, that no special rules of construction apply, only the ordinary rules of construction.17 That the judiciary is doing no more than adopting the interpretative approach applicable to trusts generally is illustrated by two relatively recent cases, each

15 Mettoy Pension Trustees Ltd v Evans [1990] 1 WLR 1587 at 1610.


17 Re Courage Group's Pension Schemes [1987] 1 All ER 528 at 537 per Millett J; Mettoy Pension Trustees Ltd v Evans [1990] 1 WLR 1587 at 1610 per Warner J; Gas and Fuel Corporation of Victoria v Fitzmaurice (1991) 22 ATR 10 at 20 per Hedigan J; British Airways Pension Trustees Ltd v British Airways plc [2002] PLR 247 at [38] per Arden LJ; Ansett Australia Ground Staff Superannuation Plan Pty Ltd v Ansett Australia Ltd [2002] VSC 576 at [215] per Warren J.
dealing with the interpretation of commercial trust instruments.

*Esso Australia Ltd v Australian Petroleum Agents' & Distributors' Association*\(^{18}\) concerned the interpretation of a deed poll the purpose of which was to create a fidelity trust for the protection of amounts owed by distributor members to oil companies in the event of default on their trading accounts. Hayne J accepted the plaintiff's submission that evidence of surrounding circumstances – the matrix of fact – was admissible to assist in the interpretation of a trust deed,\(^ {19}\) specifically noting that the “trust deed should be construed in light of the fact that the scheme that it creates is not one in which oil companies are to be treated as mere objects of bounty”.\(^ {20}\) On this approach, his Honour concluded that evidence of the trust deed's drafting history was relevant to its interpretation. Relying upon the trend of authority in respect of the interpretation of contracts as expressed in the *Codelfa Construction* case,\(^ {21}\) Hayne J held that the deliberate deletion of words in a draft deed poll was admissible to determine the intention of the settlor. This was notwithstanding that application of this approach to a deed poll was not without difficulty. In a contractual situation, he noted, “it is possible to examine the facts to see whether there was an actual intention of the parties evidenced by their concurrence in rejecting the deleted words”, whereas with a deed poll the bare fact of deletion may be equivocal and mean only that the draftsman had second thoughts regarding the manner of expression.\(^ {22}\) Notwithstanding this concern, this “contractual” approach to interpretation was considered appropriate.

Similarly, in *Manukau City Council v Lawson*\(^ {23}\) the New Zealand High Court applied the factual matrix approach in respect of a trust deed in which the trustees, as shareholders of an electricity company, held any dividends received for consumers as income beneficiaries, and any capital remaining after 80 years for the local councils. In describing what is usually termed the factual matrix approach, Paterson J opined that the meaning of the trust deed:\(^ {24}\)

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18 [1999] 3 VR 642.
19 *Esso Australia Ltd v Australian Petroleum Agents' & Distributors' Association* [1999] 3 VR 642 at 645.
20 *Esso Australia Ltd v Australian Petroleum Agents' & Distributors' Association* [1999] 3 VR 642 at 646.
21 *Codelfa Construction Pty Ltd v State Rail Authority of New South Wales* (1982) 149 CLR 337.
23 [2001] 1 NZLR 599.
24 *Manukau City Council v Lawson* [2001] 1 NZLR 599 at 604-605.
...is that which the trust deed would convey to a reasonable man having all the background knowledge which would reasonably have been available to the parties in the situation in which they were at the time the trust deed was entered into. That background includes absolutely anything which would have affected the way in which the language of the document would have been understood by a reasonable person, except for previous negotiation of the parties and their declaration of subjective intent.

His Honour went on to discuss the relevant background facts. Significantly for the purpose of this discussion, immediately prior to the above statement Paterson J commented that it was “common ground that the terms of trust deeds are to be interpreted in accordance with the Boat Park principles”. This was a specific reference to the principles set out in *Boat Park Ltd v Hutchinson*, a decision of the New Zealand Court of Appeal concerning the interpretation of a contract. Thus, once again the general principles of construction that apply in respect of contractual instruments are likewise relevant to determine the intention of the settlor of a trust.

That general interpretative principles are universally relevant as determinative of intention is further illustrated by the fact that similar principles are used in the interpretation of a will. It is presumed that words in a will are given their ordinary meaning and, in the case of ambiguity, evidence of the circumstances surrounding the testator at the date of the will is admissible to assist the court in the construction of the language used.

It follows that the interpretative approach applied in respect of superannuation trusts does not flow from recognition by the judiciary of the employment contract. Contractual principles of interpretation are not applied because of the interaction of the superannuation trust with the employment contract. The principles applied are those generally used not only in respect of trusts, but also is respect of other instruments such as contracts and wills, so as to determine the relevant “intention”. The principles themselves are concerned with the reliability of extrinsic evidence. The commonality that permits the broad application of general interpretation principles is simply that in respect of each instrument the court has the same task: that of determining the intention of the relevant party.

The universality of interpretative principle has not, however, led the courts to ignore distinctions between the specific natures of instruments. Specifically in respect of the

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26 [1999] 2 NZLR 74.
factual matrix approach, the Court of Chancery has warned that a superannuation or pension trust is:\textsuperscript{28}

...not be regarded as on all fours, so far as "matrix" is concerned with a commercial contract. A commercial contract represents by its very nature the culmination of a process of negotiation. By contrast, a new member joining a pension scheme must take the schemes as he finds it. As far as the new member is concerned, the scheme is a fait accompli. There is no opportunity for negotiation. A new member joining a pension scheme cannot, by definition, have any relevant intention in relation to its meaning or effect: the most he can have is an understanding of its meaning and effect.

In the search for intention, a superannuation trust can be distinguished from the bi-lateral nature of a contract; like all other trusts, it is unilateral in nature. Thus, the search is for the unilateral intention of the settlor, not the parties' bi-lateral agreement as in the case of employment contracts. This serves to reinforce the contention that in the construction of superannuation trusts the influence of the employment contract does not result in the application special constructionist principles.

\textbf{6.1.2 A LIMITED INFLUENCE}

At first instance the practical and purposive approach combined with the factual matrix approach appears to be a flexible tool that permits considerable regard to be had to the employment context in which superannuation arises. It almost suggests that the process of interpretation be conducted through "employment coloured glasses". However, the application of these interpretative approaches is limited, as it is in the construction of other instruments such as contracts, to situations where there is some ambiguity as to the meaning of the language.\textsuperscript{29} It follows that neither the purpose of a particular clause or deed, nor the fact that superannuation schemes arise out of the employment relationship, can justify an interpretation inconsistent with the clear and plain language of a deed. This point was emphasised in a recent decision of the English Court of Chancery where Rimer J commented that:\textsuperscript{30}

\textsuperscript{28} \textit{Spooner v British Telecommunications} [2000] PLR 65 at [75] per Jonathan Parker J (emphasis in original).


\textsuperscript{30} \textit{Hawood-Smart v Caws} [2000] PLR 101 at [21]. See also \textit{LGSS Pty Ltd v Egan} [2002] NSWSC 1171 at [78] where Austin J stated in respect of the interpretation of the relevant superannuation trust deed that "it is unnecessary to choose between a purposive and practical, and a detached and literal, construction here, because the meaning of the words used is plain in
Recourse to a "practical and purposive" interpretation of pension documentation is, in my view, an approach which is ordinarily only required when there is perceived to be a difficulty in identifying with confidence the message which the documentation is conveying. But if its language is clear, appears to convey an unambiguous meaning and does not produce a commercially absurd result then I do not see why it should not be taken at face value and as meaning what it says.

The New Zealand Court of Appeal has likewise noted the need to use the matrix of facts to elucidate, not contradict, the relevant terms. An illustration of this principle arises from the House of Lords' consideration of the arguments presented in National Grid Co plc v Mayes. This case concerned the validity of arrangements made by two companies in the electricity industry to deal with an actuarial surplus that had arisen in a defined benefit pension scheme. The trust deed required the employers, upon certification by the actuaries of a surplus, to make arrangements to deal with the surplus. The employers proposed to decrease the surplus by augmenting benefits and offsetting amounts that employers were liable to pay into the fund. A number of members objected to the latter arrangement on the basis that the amendment power prohibited making any moneys of the scheme payable to the employers. Their Lordships defined the central issue as one of construction, namely, whether or not the arrangement, to permit accrued liabilities of the employers to be discharged out of surplus funds, amounted to a payment to the employers out of the scheme. In response to this issue counsel for the members drew on the employment background of the pension scheme and submitted...

...it must be borne in mind that part of the surplus was funded by contributions from the employees. Indeed, the whole of the funding may be said to be either their contributions or payment for their services.

The clear inference is that the surplus should be held for the benefit of members as it was earned by their employment services. However, Lord Hoffman did not "see the relevance" of the way in which the surplus was funded. Instead, his Lordship noted that such considerations:

all relevant respects". The application of these principles to the interpretation of deeds generally is discussed in Herskope v Perpetual Trustees (WA) Ltd (2002) 41 ACSR 707 at 722-723 per Powell JA.


[2001] 1 WLR 864.

As to actuarial surpluses see 6.2.2.

National Grid Co plc v Mayes [2001] 1 WLR 864 at 869 per Lord Hoffman.

National Grid Co plc v Mayes [2001] 1 WLR 864 at 869 (emphasis supplied).

cannot displace the fact that the scheme confers the power to make arrangements upon the employer and no else. In some schemes the power is more evenly distributed but in this one it is not.

It follows that the mere fact that the employment relationship subsists alongside the trust relationship cannot operate to displace the clear provisions of the trust and ultimately the intention of the settlor. At most, this factor provides guidance to the court as to the settlor's intention in situations where the wording of the instrument is unclear or ambiguous. Yet even in cases of ambiguity the implications that flow from the employment relationship are not necessarily determinative. In the *National Grid* case the House of Lords ultimately found the most relevant background fact to be the fiscal origin of the provision that prohibited a payment back to an employer. Similarly, in *Uncle v Parker* Santow J indicated that an interpretation premised on the commercial employment bargain should be disregarded if “that should lead to an interpretation which subordinates the interests of employees to the employing company” unless there is clear language to that effect. Instead an interpretation that is protective of employees' interests was, in his Honour's opinion, to be preferred. The upshot of these two examples is that the employment relationship is simply one factor that may, in addition to other factors, be relevant to the interpretation of a deed where its provisions are unclear or ambiguous. This demonstrates that whilst the employment background has been heralded as distinguishing the superannuation trust from the traditional family trust, ultimately this feature has not been permitted, at least as far as the general interpretative approach is concerned, to override the intention of the settlor and provisions of the trust deed. Consistent with the first limb of the SRF, the trust and its provisions have been accorded primary importance.

Having stated this, it must be made clear that the arguments presented above refer only to the general interpretative approach. As discussed later in this Chapter, the influence of the employment contract has been far greater in respect of the powers and discretions exercised by the employer.

37 *National Grid Co plc v Mayes* [2001] 1 WLR 864 at 870-871 per Lord Hoffman.
38 (1994) 55 IR 120.
39 *Uncle v Parker* (1994) 55 IR 120 at 123.
40 *Uncle v Parker* (1994) 55 IR 120 at 123. See also Wilkins v District Court at Auckland (1997) 11 PRNZ 232; Kynaston v Clark (Unreported, High Court (New Zealand), Master Venning, 7 August 1998).
41 See 6.4.
6.2 Surplus

Of the issues arising in respect of superannuation and pension trusts, the ownership of surpluses has for the past two decades been one of the most contentious and highly litigated. With contested surpluses in the range of multi-million to billion dollar (or pound) amounts, there has been an understandably high level of interest from all relevant stakeholders. It is through the prism of surplus that the tension and interplay between the rights, duties and interests of employers, trustees and beneficiaries is not only readily apparent but also magnified by the high stakes in issue.

At the simplest level a surplus is generated when the assets of a fund exceed its liabilities. In the context of a "defined contribution" scheme the existence of a surplus, although possible, is uncommon. Such a scheme is primarily funded by a fixed rate of contributions, usually a percentage of salary that is paid by the employer into the fund on behalf of members. All contributions, together with a rate of investment earnings, are credited to a notional account in respect of each member. There is less potential for a surplus to arise because the end benefit received equates to that standing to the credit of the member in his or her notional account. There is no preset target; the contributions and investment earnings simply accumulate in the fund. However, a surplus may nevertheless arise in circumstances where, for example, the trustee creates a reserve for investment earnings that exceed the investment rate credited to the notional accounts or through some type of forfeiture of benefits.42

By way of comparison, in a "defined benefit" scheme the benefits are defined by the scheme as a specified amount, or by reference to a formula that takes account of the relevant member's salary upon retirement (or an average over a period of time before retirement) and the member's years of service. The potential for a surplus (and therefore a deficit also) to arise is much greater as there is no direct correlation between the level of assets in the fund and the benefits to be provided. Instead, the object is to ensure that there are sufficient assets available to match the scheme's liabilities as they arise. Thus the contribution rate required to fund liabilities will be actuarially determined by reference to factors such as future investment earnings, salary increases and the frequency of benefit

42 For example, in the United Kingdom if a member transfers out of a scheme within the first two years of membership, the employer's contributions may be forfeited: Pollard, "Pensions Law and Surpluses: A Fair Balance between Employer and Members?" (2003) 17 TLI 2 at 5.
payments. Accurately predicting such a rate so that assets always meet liabilities is practically impossible "simply because there is no practical possibility of predicting economic performance and the individual behaviour of scheme members with the accuracy which would be required". Marais JA of the Supreme Court of Appeal of South Africa captured the essence of the issue by his statement that:

Defined benefit pension funds do not exist to generate surpluses but they may arise when reality and actuarial expectation do not coincide. In assessing the financial health of a pension fund an actuary is gazing into the proverbial crystal ball to see what the future will hold. The use of the metaphor is not intended to demean the exercise; it is highly sophisticated and requires considerable training and skill, yet it remains, when all is said and done, an exercise in prophecy. Some of the data available may be relatively immutable and provide a secure foundation for predictions. Much of it is not. There are a host of factors about which assumptions have to be made because they lie in the future. Examples are rates of return upon different categories of investment, the rate of inflation, governmental fiscal policy, increases in salary, mortality rates for active and retire members, the rate of employee turnover, the incidence of disability, and the extent to which early retirement options may be exercised. This list is not exhaustive but it suffices to show the very considerable role that assumption plays in the assessment of the financial soundness of a pension fund and explains why even the most meticulously assessed valuation may be confounded by subsequent experience.

Consequently, it is unusual for a defined benefit scheme to be perfectly in balance. In other than a "pure balance of cost scheme" the employer's liability to fund a shortfall is limited to the required contributions. Where, however, it is a "pure balance of cost scheme" the employer is responsible for any deficit in funding. In contradistinction to a defined contribution scheme, the investment risk of the fund is cast upon the employer. Yet it does not necessarily follow that any surplus flows to the benefit of the employer.

Where a surplus occurs upon the termination of a fund the surplus will be "realised". However, during the fund's continuance an "actuarial" surplus may be said to arise. Such a surplus is "purely notional" in that it is not realised — "[i]t is simply an actuarial forecast of a future balance of the fund after providing over the whole of its expected life for all the benefits designated. It depends not only on an assessment of those projected benefits...but also on the future income and capital performance of the fund investments".

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44 Tek Corporation Provident Fund v Lorentz 1999 (4) SA 884 (SCA) at [16] (with whom Van Heerden DCJ, Smalberger, Grosskopf JJA concurred).

45 Re Imperial Foods Pension Scheme [1986] 2 All ER 802 at 812 per Walton J.

46 Cullen v Pension Holdings Ltd (1993) 1 NZSC $30-534 at 40,301-40,302. See also Board of Management of the Bank of New Zealand Officers' Provident Association v Bank of New Zealand [1999] PLR 117 at [41] per Ellis J.
The large surpluses witnessed in the 1980s and 1990s are a testament of the lack of predictability that can pervade this area. In the context of the New Zealand economy, Tesiram attributed the emergence of substantial surpluses to unexpectedly high investment returns combined with employment contraction:47

As it has turned out, reality has not matched the actuaries' prediction of future economic conditions. In particular, in the mid-1980s, investment returns far outstripped what the actuaries predicted in their actuarial valuations. Returns of 50% or more were not unheard of in 1985 and 1986...This period of phenomenal investment growth was followed in the late 1980s and the early 1990s by significant restructuring in many industries. The result was that many employees lost their jobs and left or were required to leave employers' superannuation schemes. Because they left well before retirement, many employees were not entitled to the full retirement benefit. Instead they received the much less valuable resignation benefit or redundancy benefit...

These two events that is, the phenomenal investment returns of the mid-1980s and the restructuring of the industry that followed, had one unambiguous effect. They contributed to the growth of very large surpluses in pension plans not only in New Zealand but throughout the world.

Similar sentiments were expressed in the United Kingdom with the Pension Law Review Committee, commenting:48

In recent years, large pension surpluses have arisen, largely because of dramatic and unexpected increases in the actuarially assessed value of equities in which pension funds are invested, but also because of lower than expected preserved pension costs resulting from the contraction of industrial employment.

Against this background, the underlying current of the surplus issue has been that of ownership. With high stakes both employers and employee members have sought to benefit from part, if not all, of any surplus on offer. In the Supreme Court of Canada decision of Schmidt v Air Products of Canada Ltd Cory J described the tension between employer and employees in the following terms:49

Many employers sought to recapture this surplus by withdrawing excess monies from pension funds as an alternative source of capital, by applying surplus funds to any required contribution to the pension plan (ie, taking a "contribution holiday"), or by claiming a proprietary right in any excess remaining upon the termination of the plan once all the employee benefits had been provided for. Employee groups have resisted such actions, claiming that the pension plans were established for their benefit, that the employers never intended or expected to recover any contributions made to the fund, and that any surplus

49 (1994) 115 DLR (4th) 631 at 625-626. See also Buschau v Rogers Cablesystems Inc (1999) 165 DLR (4th) 668 at 672 per Lowry J (BCSO).
accruing because of fortuitous economic circumstances should be paid to them when the plans are terminated.

Philosophically, arguments for ownership of surplus have been premised upon the contractual nature of the relationship between employer and employee. On the one hand, and in the context of a defined benefit scheme, employers argue that what is promised is a defined benefit; once that benefit is secured, because the employer bears the risk of any underfunding, any surplus should be available either to reduce contributions or to provide a refund. The employer, it is argued, has contributed in excess of what is required and so the excess should be returned to the employer in one form or another. On the other hand, employees, as members of scheme, contend that superannuation contributions are part of the remuneration received for their employment services. As such, any surplus funded from "their" contributions forms part of the remuneration for their services and so should be used for their benefit. Any refund to the employer or reduction of contributions due to be paid into the scheme represents a devaluation of their deferred pay.

Yet the framework within which this issue arises is not simply that of contract. The trust relationship has been interposed between the employer and employees with result that responsibility for the payment of benefits rests with the trustee, not the employer. As a result, the issue of surplus presents a complex interaction of competing interests that has given rise to a tension between trust principles and contract ideology. The following examines the response of the judiciary and the legislature to these issues and assesses whether the development of the law is consistent with the principles of the SRF. In the first instance the response of the judiciary to general concepts of ownership is addressed. This is followed by an examination of the specific issues and arguments that have arisen at general law regarding actuarial and realised surpluses. Attention is then drawn to the various statutory initiatives in this area.

### 6.2.1 The General Approach to "Ownership"

Despite the interest in surplus, and the debates and commentaries regarding its "ownership", judges have generally eschewed entry into the policy arena and theories of

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52 See, for example, Quarrell, "Whose Surplus Is It?" (1987) 2 TL&P 30; Nachshen, "Access to Pension Fund Surpluses: The Great Debate", presented at Meredith Memorial Lectures, Faculty of Law, McGill University, 1988, Les Editions Yvons Blais Inc; Quarrell, "Whose Surplus Is
ownership in the determination of surplus disputes. Instead, the courts’ approach has been to apply the relevant provisions of the trust deed; “to construe the document without any predisposition as to the correct philosophical approach”.53 “[T]he solution to the [problem of construction] lies within the terms of the scheme itself, and not within a world populated by competing philosophies as to the true nature and ownership of...surplus”.54

Initially the obiter comments of Millett J (as he then was) in the seminal case of Re Courage Group’s Pension Schemes55 were argued to support the view that surplus morally belongs to the employer. There Millett J observed that in a defined benefit scheme where the employer is bound to make good any deficit, employees “have no right to complain if, while the fund is in surplus, the employer should require them to continue their contributions while itself contributing nothing.”56 His Lordship added that a consequence of the nature of a balance of cost defined benefit fund means that “employees have no legal right to a contribution holiday”.57

These comments were subsequently relied upon by counsel in both Mettoy Pension Trustees Ltd v Evans58 and Amalgamated Metal Workers’ Union v Shell Refining (Australia) Pty Ltd59 as signifying that any surplus arising “belongs in principle” to, and is the “exclusive right” of,

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53 British Airways Pension Trustees Ltd v British Airways plc [2002] PLR 247 at [31] per Arden LJ (giving the judgment of the EWCA).


55 [1987] 1 All ER 528.

56 Re Courage Group’s Pension Schemes [1987] 1 All ER 528 at 545.

57 Re Courage Group’s Pension Schemes [1987] 1 All ER 528 at 545.

58 [1990] 1 WLR 1587.

59 (1993) 27 ATR 195.
the employer.\textsuperscript{60} In the latter case, the Australian Industrial Relations Commission completed an extensive review of the surplus cases and concluded that this reliance overstated the weight to be accorded to Millett J’s observations.\textsuperscript{61} Although the Commission considered that a pure balance of cost defined benefit scheme usually entitles the employer to take a contribution holiday,\textsuperscript{62} it concluded that, unless the deed otherwise expressly stipulates, “there is not a recognised unambiguous or unilateral right on the part of a contributing employer to any of the variously constituted kinds of ‘surplus’ which notionally may arise in defined benefit funds”.\textsuperscript{63} The ownership argument was similarly rejected in \textit{Mettoy}, Warner J noting that in \textit{Re Courage} Millett J expressly refrained from going so far as to state that any surplus arising in the scheme belonged to the employer.\textsuperscript{64} Moreover, in Warner J’s view, one cannot “in construing a provision in the rules of a ‘balance of cost’ pension scheme relating to surplus, start from an assumption that any surplus belongs morally to the employer”.\textsuperscript{65}

Whilst trust principles are thus arguably decisive, this has not prevented some members expressing personal policy preferences regarding the policy of ownership. For example, Cooke P opined that there is “nothing at all incongruous in the view that on the termination of a scheme any ultimate surplus should belong to the members and their dependents”.\textsuperscript{66} In his Honour’s view, it was reasonable that any windfall should be distributed to those for whom the fund was established. Others have expressed contrary views. Notably, Neuberger J has remarked that a general exclusion of employers from surplus may not only tend to make employers reluctant to contribute more than the bare

\textsuperscript{60} \textit{Mettoy Pension Trustees Ltd v Evans} [1990] \textit{1 WLR} 1587 at 1619 per Warner J; \textit{Amalgamated Metal Workers’ Union v Shell Refining (Australia) Pty Ltd} (1993) 27 \textit{ATR} 195 at 218 (AIRC).

\textsuperscript{61} \textit{Amalgamated Metal Workers’ Union v Shell Refining (Australia) Pty Ltd} (1993) 27 \textit{ATR} 195 at 228.

\textsuperscript{62} As to contribution holidays see 6.2.2.1.

\textsuperscript{63} \textit{Amalgamated Metal Workers’ Union v Shell Refining (Australia) Pty Ltd} (1993) 27 \textit{ATR} 195 at 228. It must be noted that the Commission further commented that although the trust deed is the primary source of rights, the common law also requires “that employer/employee interests in a fund be recognised and given weight in any distributive balance” (at 229). In that this issue relates to the factors that should be taken in account in the exercise of discretion as to the distribution of surplus by the employer or the trustee this issue is addressed in 6.4 and 6.5.

\textsuperscript{64} \textit{Mettoy Pension Trustees Ltd v Evans} [1990] \textit{1 WLR} 1587 at 1619. See also \textit{Tek Corporation Provident Fund v Lorentz} 1999 (4) \textit{SA} 884 (SCA) at [17] per Marais JA (with Van Heerden DCJ, Smalberger, Grosskopf JJA concurring).

\textsuperscript{65} \textit{Mettoy Pension Trustees Ltd v Evans} [1990] \textit{1 WLR} 1587 at 1619.

\textsuperscript{66} \textit{Re UEB Industries Ltd Pension Plan} [1992] \textit{1 NZLR} 294 at 298.
minimum to pension schemes but may also result in employers making decisions regarding the pension scheme that would not be beneficial for employees.67

Notwithstanding such personally held views, the provisions of the trust instrument have remained decisive. In the instances cited, Cooke P concluded that his personal view of policy considerations were “of little importance” and “[w]hat must be decisive are the terms of the trusts constituted by the particular scheme”.68 Nueberger J similarly noted that his policy views were “not in point in the present case”.69

Prioritising the trust instrument over competing contractual policy considerations as to ownership is consistent with general trust principle and, as such, accords with the schema of priorities underlying the SRF. Where the deed is clear as to the use of surplus, no difficulty will arise. If the deed is unclear and/or does not appear to address the issue directly, the matter turns on the appropriate interpretation of the deed according to the principles noted above.70 The attendant issue that arises for the purpose of this Chapter is whether or not policy views as to “ownership” nevertheless influence the judiciary in the application of interpretation principles in situations where destination of surplus is unclear or ambiguous. This is explored below in respect of both actuarial and realised surpluses.

6.2.2 ACTUARIAL SURPLUS

The Nature of Actuarial Surplus

An actuarial surplus, which arises where the actuarial assessed value of assets exceeds that required to meet the actuarial assessed value of liabilities,71 is amorphous in nature. It is a notional value that cannot be accurately assessed unless the fund is terminated and all liabilities are paid out.


69 Barclays Bank plc v Holmes [2000] PLR 339 at [103]. It should also be noted that Neuberger J in introducing the surplus issue stated that the “question I have to consider is whether in light of the terms of the Fund...there is any reason why the Bank should not proceed in such a fashion”. (at 103). This statement and his Lordship’s subsequent examination of the terms of the relevant deed clearly aligns his method with the traditional approach – that of the trust deed being determinative.

70 See 6.1.

71 Typically, the term “liabilities” refers to the benefits payable from a defined benefit scheme.
Moreover, due to the nature of actuarial assessment, variations, even small variations, in the assumptions underpinning the actuarial assessment of the value of assets and liabilities can result in "disproportionately large changes in the surplus or deficit or in the conversion of one into the other". The facts of LRT Pension Fund Trustee Company Ltd v Hatt vividly illustrate this point. In this case the effect of decreasing the assessed rate of future dividend growth by one half of one percent would have reduced the assessed value of the fund by £167 million and thereby reduced the past service surplus from £460 million to £293 million. Consequently, a one half percent reduction in an actuarial prediction would have changed the value of the surplus by some 36%. Due to the nature of an actuarial surplus, a proprietary interest does not subsist in the members of the fund. In a defined benefit fund the members do not have an interest in scheme funds; the fund is merely security for the payment of benefits. As such, an equitable or proprietary interest does not arise. This is the case even when upon termination the

72 United Kingdom, Pension Law Review Committee, Consultation Document on the Law and Regulation of Pension Schemes, 1992, at ¶9.7. This is not the only variant. An added complexity is the different methods that can be used to value a fund. For example, in Stannard v Fisons [1991] PLR 225 at [30] Dillon J identified three alternative bases for valuing a fund: (i) the "accrued rights" method, which involves calculating the liabilities of the Fund on the basis of salaries and service down to the date of the calculation without regard to future service up to retirement; (ii) the "past service reserve" method, which assesses the value of the benefits accrued to date by reference to anticipated salaries at the date of retirement, rather than salaries at the calculation date; and (iii) the "total service reserve" method, which allows not only for anticipated future salaries to normal retirement date but also for anticipated increment in benefits due to future service. See further Bennett, Pension Fund Surpluses (2nd ed, Longman, 1994), ¶2.3; Pollard, "Pensions Law and Surpluses: A Fair Balance between Employer and Members" (2003) 17 TLI 2 at 7.


75 Wrightson Ltd v Fletcher Challenge Nominees Ltd [2002] 3 NZLR 1 at 16 per Lord Millett (PC). See also Re Imperial Foods Ltd's Pension Scheme [1986] 2 All ER 802 at 812-813 per Walton J; Taylor v Lucas Pensions Trust Ltd [1994] PLR 9 at [24] per Vinelott J; Schmidt v Air Products of Canada Ltd (1994) 115 DLR (4th) 631 at 644-645 per Cory J; Buchau v Rogers Cathaysystems Inc (1999) 165 DLR (4th) 668 at 691 per Lowry J; Barclays Bank plc v Holmes [2000] PLR 330 at [117] per Neuberger J. This has also been held to be the case in respect of a defined contribution scheme. In Re Motorola New Zealand Superannuation Fund [2001] 3 NZLR 50 there was a windfall receipt from the sale of AMP shares after demerger. The issue that arose was whether or not the trustees were empowered to distribute the windfall to past members (that is, those who were members at the relevant qualifying date but who were no longer members at the time of realisation). The New Zealand High Court held that as the AMP shares were one of a number of investments, the windfall gain was the luck of the draw and did not give rise to an entitlement by past members to share in the proceeds: 66-67 per McGechan J.

76 Wrightson Ltd v Fletcher Challenge Nominees Ltd [2002] 3 NZLR 1 at 16 per Lord Millett (PC).
trust deed directs that surplus is to be used for the benefit of the members. On this point the Supreme Court of Canada has observed:77

While a plan which takes the form of a trust is in operation, the surplus is an actuarial surplus. Neither the employer nor the employees have a specific interest in this amount, since it only exists on paper, although the employee beneficiaries have an equitable interest in the total assets of the fund while it is in existence. When the plan is terminated, the actuarial surplus becomes an actual surplus and vests in the employee beneficiaries.

Managing an Actuarial Surplus: The Legal Issues

Notwithstanding the notional nature of an actuarial surplus, at a commercial level the recognition of a surplus in an ongoing fund raises legal, administration and management issues.8 An actuarial surplus may be managed by one or more of the following methods:79

- retention of the surplus in the scheme;
- augmentation of member benefits;80
- the creation of reserves;81
- a reduction or suspension of contributions;82 or
- a payment to employers.

The availability of any such method is governed by the terms of the trust instrument and any statutory restrictions.83 Any specific direction as regards the reduction of surplus must

77 Schmidt v Air Products of Canada Ltd (1994) 115 DLR (4th) 631 at 654-655 per Cory J. See also Burchau v Rogers Cablesystems Inc (1999) 165 DLR (4th) 668 at 691 per Lowry J (BCSC). While an equitable interest does not accrue to member beneficiaries in this situation, there is authority that members nevertheless have an expectation to be considered in any distribution of surplus. This is important in two respects. First, where a power of amendment protects against amendment that adversely affects the accrued rights of members, the expectation that members may receive a surplus distribution upon termination may be protected. Secondly, it requires trustees to consider a distribution to members in any exercise of discretion regarding the distribution of surplus. See Stannard v Fisons Pensions Trust Ltd [1991] PLR 225 at [47] per Straughton LJ; Treells Ltd v Lomas [1993] 1 WLR 436 at 468-469 per Sir Donald Nicholls VC. See further 6.4.2.1 (under the heading “(iii) Legitimate and Reasonable Expectations”) and 6.4.2.2.

78 Slater, “Superannuation Fund Surpluses” in Australian Superannuation Practice (ATP, Looseleaf), at ¶12A/25.

79 See further Slater, “Superannuation Fund Surpluses” in Australian Superannuation Practice (ATP, Looseleaf), at ¶12A/46.


81 See British Airways Pension Trustees Ltd v British Airways plc [2002] PLR 247.


83 Board of Management of the Bank of New Zealand Officers' Provident Association v Bank of New Zealand [1999] PLR 117 at [39]-[41] per Ellis J; Capral Fiduciary Ltd v Ladd (1999) 1 NZSC ¶30-
be followed. If the trust deed casts a duty or confers a discretion on either the employer or the trustee in respect of determining an appropriate scheme of reduction, the general principles governing the duties and powers of trustees and employers will also impact upon the available options and the ultimate scheme of distribution. Where the trust deed does not expressly permit the preferred method of reduction, an amendment of the trust instrument may be required to facilitate the desired outcome, although the scope of any such power is determined by its proper construction, the general law and statutory limitations on its exercise.

Adoption of any of the methods listed above raises issues as to the interaction of employers, trustees and beneficiaries. In respect of the first three methods listed, the probative issues are the performance of duties and the proper exercise of discretion by trustees and employers. It is usually an option for a trustee to retain a surplus within the scheme as, unless the deed directs the trustee to reduce the surplus, it will simply accrue as part of the fund. However, the extent of the surplus and advice received from actuaries will influence whether or not a trustee considers it prudent, and in the best interests of beneficiaries, to retain the surplus in the fund or otherwise considers a scheme for its reduction. The power to allocate an actuarial surplus, or part thereof, to a reserve is similarly guided by these principles. As to the augmentation of benefits, the trust deed will generally contain a power to augment benefits, both that will be paid out in future and those currently in payment. However, it will not necessarily vest in the trustee unilaterally. More common is the situation where the power is vested in the trustee with consent to be provided by the employer (or vice-versa). The crucial issue that arises here is the proper exercise of discretion and whether, in the exercise of that discretion, regard must be had to the interests of other stakeholders.

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84 As to the exercise of discretion by employers and trustees see 6.4 and 6.5 respectively.

85 See 6.3.

86 In this context, a power within a deed to "dispose of surplus" has been held to include the power to create a reserve: British Airways Pension Trustees Ltd v British Airways plc [2002] PLR 247 at [141] per Arden LJ (with whom Auld and Waller LJJ concurred) (EWCA).


88 It is in respect of the augmentation of benefits, particularly where consent to utilise the power is required, that the tension between the competing interests of the trustee and beneficiaries, with those of the employer is quite apparent. The requirement of consent necessitates a level of negotiation between trustee and employer and thereby affects the considerations relevant to either the exercise of the power by the trustee or the granting of consent. As to the exercise of duties, power and discretions by employers and trustees see 6.4 and 6.5 respectively.
It is in respect of the last two listed items, contribution holidays and repayments to employers, that the interaction and tension between stakeholders has been most evident. It is also in this context that employers and beneficiaries have sought to rely on themes of ownership to establish their stake in the surplus at hand. The following pursues these themes of ownership in respect of the final two methods of surplus reduction.

### 6.2.2.1 Contribution Holidays

**The General Judicial Approach**

A "contribution holiday" refers to a situation where employer and/or member contributions are suspended for a specified period of time. In a broad sense, the term can also refer to a reduction in the rate of contributions. The essence of the concept is that the assets coming into the scheme are reduced and thus the employer, and possibly also the employee members, are on "holiday" from making contributions. Typically a surplus will "fund" a contribution holiday. Since employer contributions are, by the very nature of a defined benefit fund, the variable component, for the purpose of this thesis the phrase "contribution holiday" will be taken to refer to an employer contribution holiday.

The issue of contribution holidays "typifies the wide philosophical divergence of views held by employers and employees with respect to a pension fund". The employer views the promise of a pension as contractual in nature such that the means for fulfilling this contractual promise is entirely within its purview. Conversely, as a result of employees conceptualising contributions as deferred pay, from their perspective any contribution holiday represents a decrease in remuneration for services rendered.

Sweeping notions of contractual theory have not influenced the courts in the determining whether or not a contribution holiday is permitted. Instead, resort has been had to the wording of the trust deed and to the relevant legislation. The approach adopted has been to determine whether or not the wording of the trust deed, either expressly or by implication, precludes a contribution holiday. As a matter of principle the judiciary has found no objection to employers taking a contribution holiday where

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permitted by the relevant trust deed. As any right to surplus cannot crystallize until the termination of a plan, the taking of a contribution holiday does not prima facie represent an encroachment on the trust. Ipso facto, that the employees have a right upon termination to a surplus will not exclude the taking of a contribution holiday. Similarly, a reduction in contributions or the release of an accrued debt will not offend against a provision that prohibits payments back to the employer.

The essence of the issue has turned upon the funding clause and the role of the actuary in respect of determining the appropriate contribution rate. A contribution holiday will be permitted where:

...the funding clause provides for an actuarial determination of the contribution required and the actuary, who may be presumed to apply generally accepted actuarial principles, determines that the existence of a surplus serves to reduce or eliminate the need for contributions that would otherwise be required. The narrow question becomes of what calculation the actuary is to make. Where the calculation is the amount necessary to fund the benefits, contribution holidays will be permitted.

Consequently, if generally accepted actuarial practice permits the inclusion of surplus in the calculation of contributions required, then a contribution holiday is permitted if the actuary determines that contributions should be reduced or suspended. Two examples of clauses that have been interpreted to allow a contribution holiday are:

92 Re Imperial Foods Pension Scheme [1986] 2 All ER 802 at 812 per Walton J; Re Courage Group's Pension Schemes [1987] 1 All ER 528 at 545 per Millett J; Amalgamated Metal Workers' Union v Shell Refining (Australia) Pty Ltd (1993) 27 ATR 195 at 228 (AIRC); Schmidt v Air Products of Canada Ltd (1994) 115 DLR (4th) 631 at 673 per Cory J (with whom La Forest and L'Heureux-Dubé JJ concurred); Hockin v Bank of British Columbia (1995) 123 DLR (4th) 538 at 555 per curiam; Buschau v Rogers Cablesystems Inc (1999) 165 DLR (4th) 668 at 680 per Lowry J (BCSC).

93 Schmidt v Air Products of Canada Ltd (1994) 115 DLR (4th) 631 at 653-654, 656 per Cory J.

94 Re Reevie and Montreal Trust Co of Canada (1986) 25 DLR (4th) 312 at 318 per Zuber JA (giving the judgment of the OntCA).

95 Tek Corporation Provident Fund v Lorentz 1999 (4) SA 884 (SCA) at [23] per Marais JA (with whom Van Heerden DCJ, Smalberger, Grosskopf JJA concurred); National Grid Co plc v Mayes [2001] 1 WLR 864. See also Pollard, “Pensions Law and Surpluses: A Fair Balance between Employer and Members?” (2003) 17 TLJ 2 at 16-17. As to the release of debts see further 6.2.2.2.

Chapter 6: Trust and the Employment Relationship

Example No 1:
The company shall contribute from time to time...such amounts as are not less than those certified by the Actuary as necessary to provide the retirement benefits accruing to the Members...taking into account the assets of the Pension fund and all other relevant factors.97

Example No 2:
Each contributing Member Hospital shall make contributions to the Plan on a basis determined by the Actuary from time to time.98

The taking of a contribution holiday may also be excluded by the terms of the deed. So where the trust deed specifically prevents an actuary from taking surplus into consideration in his or her contribution calculations, limits the actuary's role to the calculation of benefits,99 or does not refer to an actuarial determination or calculation,100 the use of surplus to fund a contribution holiday will be impliedly excluded.101 Where the funding clause mandates a specific, as opposed to variable, rate of employer contribution, a contribution holiday will be likewise excluded.102 Thus, if a surplus arises in a defined contribution plan, absent words that expressly permit a reduction or cessation of contributions, a contribution holiday will be impliedly excluded by the mandatory nature of contributions.103

97 Extract from the Air Products of Canada Ltd Plan (section 4.03), which was the subject of litigation in Schmidt v Air Products of Canada Ltd (1994) 115 DLR (4th) 631 (SCC).
98 Extract from the Hospitals of Ontario Pension Plan (section 6.02), which was the subject of litigation in Hospitals of Ontario Pension Plan v Ontario Hospital Association [1991] PLR 125 (OntCA).
99 See, for example, CUPE-CLC, Local 1000 v Ontario Hydro (1989) 58 DLR (4th) 552 where the provisions of a statutory plan required the employer to contribute the difference between employee contributions and “the cost of benefits as determined by actuarial valuations”. The Ontario Court of Appeal held that contribution holidays were impliedly excluded as the clause mandated the making of contributions amounting to the difference, the actuary’s role being limited to calculating the cost of the benefits and not extending to setting the overall level of employer contributions (at 561-562 per Robins JA). This decision was subsequently approved by the Supreme Court of Canada in Schmidt v Air Products of Canada Ltd (1994) 115 DLR (4th) 631 at 662 per Cory J.
101 Schmidt v Air Products of Canada Ltd (1994) 115 DLR (4th) 631 at 664 per Cory J.
102 Trent University Faculty Association v Trent University (1992) 99 DLR (4th) 451 at 456 per Callaghan CJOC (giving the judgment of the OntCA).
103 These principles apply equally to a “hybrid” plan, that is, one that has elements of both a defined contribution and defined benefit plan. In Bathgate v National Hockey League Pension Society (1994) 110 DLR (4th) 609 employer clubs were precluded from utilising a surplus for the purpose of a contribution holiday. The scheme was hybrid in nature, having both defined pension and defined contribution components, and members were entitled to receive a defined benefit. Pursuant to the funding arrangement employers were to make contributions in accordance with a schedule designed so that the contributions made by a club would be sufficient to purchase the pensions that had been promised. However, unlike the usual defined
Whilst it is difficult to utilise surplus for the purpose of a contribution holiday in a defined contribution plan, it may be possible to use surplus arising from the defined benefit section of a scheme to fund a defined contribution section of that same scheme. In Barclays Bank plc v Holmes\textsuperscript{104} an accumulation scheme was added to a defined benefit scheme. The employer sought to use a pre-conversion surplus to meet the contributions due under the accumulation section of the scheme. That the funding provision in the trust deed used the word “credit” instead of “pay” regarding contributions to the accumulation section led Neuberger J to hold that there was no express requirement mandating actual contributions. As such, the surplus that emanated from the defined section was available to fund contributions in the accumulation section.\textsuperscript{105} Conversely, in Kemble v Hicks\textsuperscript{106} an employer was precluded by Rimer J from invoking a surplus for the same purpose. Kemble can be distinguished from the situation in Barclays Bank plc v Holmes as the establishment of the money purchase section was held to involve “the setting up of what was, within the overall scheme, a scheme quite separate from the final salary scheme and to which different considerations applied”.\textsuperscript{107}

**Judicial Support for a Contractual Approach?**

Two main arguments assert judicial support for a contractual approach to this issue. The first relates to the obiter comment of Millett J (as he then was) in Re Courage Group’s Pension Schemes\textsuperscript{108} that employees have no right to complain if the employer chooses to reduce or suspend contributions. As discussed earlier, to rely on this comment as promoting a contractual approach overstates the weight that should be accorded to it.\textsuperscript{109} Moreover, if Millett J intended to imply a “right” it is difficult to reconcile this approach with his Lordship’s subsequent remark that it will “only be in rare cases that the employer will have any legal right to repayment of part of the surplus”.\textsuperscript{110} If such a

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\textsuperscript{104} [2000] PLR 339.


\textsuperscript{106} [1999] PLR 287 (EWHC).

\textsuperscript{107} Kemble v Hicks [1999] PLR 287 at [29] (EWHC).

\textsuperscript{108} [1987] 1 All ER 528 (EWHC).

\textsuperscript{109} See 6.2.1.

\textsuperscript{110} Re Courage Group’s Pension Schemes [1987] 1 All ER 528 at 545 (EWHC).
right exists at general law in respect of actuarial surplus, ispo facto it would also apply regarding realised surplus.

A second, more sophisticated, argument that needs consideration stems from a suggested interpretation of the Supreme Court of Canada’s judgment in Schmidt v Air Products of Canada Ltd.\textsuperscript{111} Schmidt involved the merger of two companies with the result that their respective pensions plans were also merged to form the Air Products plan. The issues of distribution of final surplus upon termination and the availability of contribution holidays during the life of the plan arose in respect of each of the former plans, the Stearns plan and the Catalytic plan. In respect of the latter plan, Cory J (with whom La Forest, L’Heureux-Dubé, Gonthier and Iacobucci JJ concurred) held that the employees were entitled to surplus funds upon termination; however, this did not preclude the taking of a contribution holiday by the employer during the life of the plan.\textsuperscript{112} Gillese argues that the reasoning of the Supreme Court’s decision in Schmidt is logically inconsistent, with result that the contractual terms of the plan appear to be prioritised over and above the trust deed.\textsuperscript{113}

Gillese’s argument as to inconsistency can be viewed at two levels. The first relates to the unique nature of pension scheme documentation in Canada. The governance structure of Canadian pension schemes is, unlike the other jurisdictions canvassed in this thesis, typified by two primary documents: the pension plan and the pension fund. As discussed in Chapter 3 in respect of Ontario,\textsuperscript{114} the pension plan represents the contractual arrangement between the employee and employer\textsuperscript{115} and details the rules for the administration and management of the plan. Conversely, the pension fund refers to the documents that support the creation of the actual pool of contributions that fund the pension plan. Consequently, if the pension plan is funded through the vehicle of a trust, the document creating and supporting the pension fund is the trust deed. The express distinction between the pension plan and pension fund places beneficiaries in a

\textsuperscript{111} (1994) 115 DLR (4th) 631.

\textsuperscript{112} Schmidt v Air Products of Canada Ltd (1994) 115 DLR (4th) 631 at 665, 671-673.


\textsuperscript{114} See 3.2.2.2.

position, unlike other common law counterparts, where their entitlements have a direct contractual origin.

The starting point for Gillese's contention is Cory J's statement that, where a pension plan is funded by virtue of a trust, trust principles will determine the matter.116 In that the funding obligation appears in the pension plan and thus entails a contractual promise, she argues that to permit a contribution holiday when the pension trust must be administered for the benefit of the beneficiaries ultimately prioritises the pension plan contract over the trust deed.117 In this respect, permitting a contribution holiday is inconsistent with the provisions of the trust.

If this in and of itself represents Gillese's contention the apparent inconsistency can be dispelled. It would be unusual for the trust deed funding the pension plan not at some point to make reference to the fact that the trust is funded in accordance with the plan. If this is so, the funding clause is essentially incorporated into the trust deed by reference, so that the issue is simply one of interpreting the trust instrument. This is supported by the facts of Schmidt, where the trust deed constituting the Catalytic scheme stated that the trust fund was to be held and administered for the benefit of the persons designated “in or pursuant to the plan” (emphasis supplied). Moreover, the fund was to be constituted by money paid for the “purpose of the plan” (emphasis supplied).118 These provisions make it very difficult to argue that the funding obligation subsisting in the plan was completely separate from and not incorporated within provisions of the trust deed. To this end, the plan did not take precedence over the trust deed. Cory J's comments regarding priority of trust principles can be simply seen to require that the trust deed (including any plan provisions incorporated by reference) be interpreted according to the ordinary principles of trust law. Thus, ordinary trust principles as to amendment, revocation, powers and duties of trustees and the application of a resulting trust on termination (where required) apply.119

At a secondary level, which more accurately reflects the crux of Gillese's argument, the issue is more than a battle between the pension plan and trust. Rather the second view focuses on whether or not the inconsistency results from utilising contractual notions of

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118 Schmidt v Air Products of Canada Ltd (1994) 115 DLR (4th) 631 at 667-668 per Cory J.
119 Schmidt v Air Products of Canada Ltd (1994) 115 DLR (4th) 631 at 666 per Cory J.
ownership in the interpretation of the provisions of the trust deed (including any provisions incorporated by reference). This is supported by Gillese's further contention that the existence of an apparent inconsistency is not a flaw but rather represents "the inchoate beginnings of the flexible application of trust principles".120 Such flexible principles are said to take root in the application of policy considerations of ownership.121 On this basis, Gillese argues that the decision in Schmidt, that a contribution holiday could be taken notwithstanding that upon termination the surplus was owned by the employees, can be justified on two alternative bases.

The first is the proposition, said to be premised upon traditional trust principle, that an employer may take a contribution holiday if the pension plan expressly or impliedly permits this. Accordingly, even where employees are entitled to surplus assets on termination, if it is positively (either expressly or impliedly) authorised by the trust, the taking of a contribution holiday is in accordance with the parties' agreement. Moreover, in Gillese's view "strict adherence to trust law principles is rooted in the view that pensions are a form of deferred compensation".122 While the result of Schmidt could be seen to support this proposition, Gillese argues that the reasoning for the result supports the second justification.

This second justification is that an employer may take a contribution holiday if the pension plan does not by implication prohibit the taking of such holidays.123 This is premised upon the notion that the intention of the parties is to be derived from the employment context. In that what is promised is a specific benefit, the parties have not turned their minds to the amount to be deposited. Rather, the employer must determine how to ensure there are sufficient funds available. For this purpose the employer will often choose a trust. To this end, Gillese contends that:124

[A] defined benefit plan which uses a trust mechanism for funding purposes is subject to two areas of law: contract and trust. Contract law is dominant, and contractual principles are to be used to answer questions which relate to the pension when it is ongoing. Trust law is dominant and its principles are to be used to answer questions which relate to the termination of the plan. Therefore, as the issue of contribution holidays is about an ongoing plan, the terms of the pension plan (ie the contract) dominate. Surplus entitlement, as a question which arises on termination of the plan, is resolved by recourse

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to trust law principles. The inversion of the normal dominance of trust law is based on intention of the parties.

That the reasoning in *Schmidt* is representative of the second view is said to arise from following obiter statement by Cory J that silence in plan documents can be construed as permission to take a contribution holiday:\(^\text{125}\)

The right to take a contribution holiday can be excluded either explicitly or implicitly in circumstances where a plan mandates a formula for calculating employer contributions which removes actuarial discretion. Contribution holidays may also be permitted by the terms of the plan. When the plan is silent on the issue, the right to take a contribution holiday is not objectionable so long as actuaries continue to accept the application of existing surplus to current service costs as standard practice.

Gillese's purpose in outlining the two alternative justifications is simply to identify what she views as an inconsistency and to propose alternate rationales for the inconsistency. She puts forward neither as the "preferred view". Instead each possible solution is identified as having a policy rationale to support it and in her view "policy elements will, in the end, dictate which of the two lines of reasoning should be adopted.\(^\text{126}\)

Three comments are made in respect of the justifications cited. First, Gillese's inference drawn from Cory J's comments regarding silence in trust deeds tends to ignore the qualification placed upon his comment. Although Cory J opined that "when the plan is silent on the issue, the right to take a contribution holiday is not objectionable", the sentence did not conclude at this point. The words "so long as actuaries continue to accept the application of existing surplus to current service costs as standard practice" (emphasis supplied) followed. The use of the phrase "so long as" indicates that the former point is qualified and will only hold true when the qualification is satisfied. Viewed in this context, the comment is consistent with his Honour's entire discussion of contribution holidays and refers to the situation where the right to a contribution holiday is impliedly permitted. As a general principle, Cory J stated that contribution holidays can be taken where expressly or impliedly permitted by the plan. Thus, if the funding clause provides for an actuarial determination of the contribution required and the actuary, who may be presumed to apply generally accepted actuarial principles, determines that the existence of a surplus serves to reduce or eliminate the need for contributions that would otherwise be required, a contribution holiday will be permitted. If accepted actuarial practice decreed that it was inappropriate to include

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\(^{125}\) *Schmidt v Air Products of Canada Ltd* (1994) 115 DLR (4th) 631 at 666-667.

surplus in the calculation of the rate required, then a right to a contribution holiday would be impliedly excluded.

The qualification on Cory J's "silence" comment can be seen to simply infer that in this situation the deed impliedly permits the taking a contribution holiday. This is quite different from the interpretation drawn by Gillese, namely, to allow a contribution holiday when it is not otherwise "prohibited" by the deed. If this is an accepted interpretation, the support drawn for second justification is negated.

Secondly, since the presentation of these justifications by Gillese in 1994, the progression of the general law has been in accord with the first proposition: an employer may take a contribution holiday if the pension plan, expressly or by implication, permits the taking of the holiday. Whilst this statement accords with traditional trust principle, this cannot be said of Gillese's accompanying policy rationale. It is true that superannuation and pension trusts are established for the benefit of the members (and other beneficiaries) and must be administered in the best interests of the beneficiaries. Moreover, the rationale for the use of the trust and protection therein provided may stem from an underlying conception that pensions are a form of deferred compensation and so must be protected. Yet this has not translated into direct legal principle. The rationale for choosing the trust as the appropriate legal mechanism has not altered general trust law principle. If this were the case, the general law would have no difficulty deciding the issue of surplus in favour of employees on the basis of the concept of ownership. Instead, and as is argued above, the words of the trust deed and thus the intention of the settlor(s) will take priority regardless of whether those words are consistent with an employee view or employer view of the superannuation arrangement.

Finally, the justifications proposed by Gillese are premised upon an apparent inconsistency in Schmidt: employees owned the surplus on termination, whereas ongoing surplus could be used to benefit employers. If the issue is conceptualised as one of ownership, the inconsistency holds true. Yet the courts have seen the issue as one of interpretation. Therefore, provided that the approach to both issues is the same - that of interpretation - an issue of inconsistency does not arise. In addition, use of the word inconsistency implies that like circumstances have been treated differently. Thus, in accordance with Gillese's view, different approaches have been applied to determine the like circumstances of ongoing and final surpluses. However, as was recognised by Cory J, actuarial surplus and final surplus are fundamentally different. Unlike a final surplus, an actuarial surplus results from actuarial calculation and is a function of the assumption used by the actuary. It is purely a notional amount in which an interest cannot subsist. The right to a surplus crystallises only when the surplus becomes ascertainable upon the
termination of the plan. Accordingly, the apparent inconsistency identified by Gillese may be seen to arise not from the approach of the Supreme Court of Canada or the result of the decision but rather from the fact that actuarial and realised surpluses are fundamentally different in nature. Like circumstances have not been approached differently – different circumstances have been approached consistently.

6.2.2.2 PAYMENTS TO EMPLOYERS

Because the courts have, in respect of permitting payment of an actuarial surplus out to an employer, focused on the terms of the trust deed, in the absence of a power of repayment the employer will have no right to receive a payment. As aptly commented by Marias JA of the Supreme Court of Appeal of South Africa:

Once a surplus arises it is ipso facto an integral component of the fund. Unless the employer can point to a relevant rule of the fund or statutory enactment or principles of the common law which confers such entitlement or empowers the trustees to sue the surplus for its benefit, the employer has no right in law to the surplus.

Lord Browne-Wilkinson, in his quest to characterise superannuation and pension arrangements as contractual, has suggested that an inability to pay an employer without express power rests on the contractual nature of the arrangement. To this end, although conceding that this is not the accepted view, his Lordship has made the following extra-judicial remark:

If, as I have suggested, the basic relationship is one of contract, the employers' contributions have been made on the basis that they will be held by the trustees to provide the benefits secured to the members by the rules. It is wholly contrary to that purpose to enable assets to be removed from the funds until it is known (not merely forecast) that they will not be required.

However, as is recognised by Lord Millett, "there is no need to resort to the employment contract to support the proposition that the fund is charged with the payment of the benefits and cannot be repaid to the employer without express provision in the scheme."

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129 Tek Corporation Provident Fund v Lorentz 1999 (4) SA 884 (SCA) at [17] (with whom Van Heerden DCJ, Smallberger, Grosskopf JJA concurred).
That an ability to take a contribution holiday pursuant to a superannuation trust deed does not translate into a right to payment of actuarial surplus further illustrates that the courts have shunned contractual notions of surplus ownership in this context also. If adjudged on the basis of ownership, philosophically the taking a contribution holiday equates to an ownership right over surplus assets – ipso facto, on this basis an employer could secure a direct payment from the fund. Moreover, courts have been not swayed by the general argument that the surplus represents that the employer paid more than it was contractually bound to do and therefore a refund is appropriate.

It may be possible to cure a want of power to distribute to the employer by amendment. Because an amendment will usually at the very least require the consent of the trustee, the issue turns not only upon the validity of the amendment but also the cooperation and negotiation between the employer and trustee. Although superannuation trusts are held for the purpose of providing benefits, the payment out of an actuarial surplus is not considered inconsistent with the main purpose of the scheme as a “surplus is (by definition) money in excess of what is needed to effect the main purpose”. More common than an express power of repayment is a clause prohibiting any return of trust funds to the employer or an amendment to that effect. However, as a measure of reducing surplus, the release of debt accrued within the fund in favour of the employer will not offend against such prohibition and is more akin in nature to the taking of a contribution holiday.

6.2.3 REALISED SURPLUS

Once a superannuation fund is wound up, any surplus in the fund crystallises and the rights and interests in respect of the surplus likewise crystallise. A well drafted trust deed normally makes provision for the distribution of surplus in this instance. It may direct for a specific distribution, such as payment to the employer or the augmentation of members' benefits, or may confer a discretion on either the trustee or the employer as to distribution.

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132 As to amendment and the considerations of the employer or trustee in the exercise of their powers see 6.3, 6.4.2 and 6.5.2. For an example of an amendment that successfully returned actuarial surplus to the employer as part of an overall scheme for the reduction of actuarial surplus see Lock v Westpac Banking Corporation [1991] 25 NSWLR 593.

133 National Grid Co plc v Mayes [2001] 1 WLR 864 at 869 per Lord Hoffman (HL). See further 6.3.1.1.

134 National Grid Co plc v Mayes [2001] 1 WLR 864 at 871, 873 per Lord Hoffman, at 882 per Lord Clyde, at 883 per Lord Scott (overruling on this point British Coal Corp v British Coal Staff Superannuation Scheme Trustees Ltd [1995] 1 All ER 912 (EWHC)).
In the latter case, any discretion will be constrained by the general principles regarding the exercise of discretions\cite{135} and other relevant provisions of the deed.

Where the trust instrument makes no such provision, in the absence of statutory provision\cite{136} general principles of trust law dictate that the surplus is held prima facie on resulting trust for the contributors.\cite{137} A resulting trust arises by operation of law to fill any gaps in beneficial ownership. In essence the doctrine is a foundational presumption for "locating the beneficial interest in property when the transfer of the property is itself either ambiguous as to the location of that interest or ineffective to dispose of the interest".\cite{138} In Re Vandervell's Trusts (No 2)\cite{139} Megarry J categorised this type of resulting trust (the failing trust situation) as "automatic" in that it arises outside of the trust fund and does not respond to the settlor's intention at all. However, the modern view is that the outcome reflects the presumed intention of the settlor not to depart with the beneficial interest in the circumstance where the trust fails to dispose with the entire interest.\cite{140} In other words, equity, faced with a gap in beneficial ownership, adopts a presumption based upon what it assesses to be the most likely intention of the settlor: that the settlor intended to retain the beneficial interest. Yet because this equitable presumption will not stand in face of evidence of contrary actual intent expressed in the trust deed,\cite{141} in a negative sense intention is relevant. The resulting trust will respond to the settlor's intention not to retain a beneficial interest in the event that the trust should fail. Where the presumption is rebutted, equity, as a measure of last resort, vests the beneficial interest of the remainder of the fund in the Crown as bona vacantia.\cite{142}

\begin{footnotesize}
\begin{enumerate}
\item See 6.4 and 6.5.
\item See 6.2.4.
\item Air Jamaica Ltd v Charlton [1999] 1 WLR 1399 at 1411 per Lord Millett (PC). See also Re ABC Television Ltd Pension Scheme (Unreported, Chancery Division, 22 May 1973, Foster J); Re Canada Trust Co and Cantol Ltd (1979) 103 DLR (3d) 109 at 111 per Gould J (BCSC); Re Dan Jones & Sons (Porth) Ltd [1989] PLR 17 at [28]-[37] per Knox J (EWHC); Davis v Richards & Wallington Industries Ltd [1990] 1 WLR 1511 (EWHC); Knudsen v Kara Kar Holdings Pty Ltd [2000] NSWSC 715 at [49] per Austin J.
\item Rickett and Grantham, "Resulting Trusts - The True Nature of the Failing Trust Cases" (2000) 116 LQR 15 at 19.
\item [1974] Ch 269 at 289.
\item Davis v Richards & Wallington Industries Ltd [1990] 1 WLR 1511 at 1541 per Scott J.
\item Rees v Dominion Insurance Co of Australia Ltd (in lig) (1981) 6 ACLR 71 at 79 per Waddell J.
\end{enumerate}
\end{footnotesize}
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The relevance of the resulting trust concept to resolve the issue of the destination of final surplus in superannuation trusts has been queried. In particular, Lord Browne-Wilkinson has expressed a preference for a contractual analysis of the issue, observing extra-judicially that:

I have considerable reservations whether this concept of a resulting trust is properly applicable at all to superannuation schemes; the monies have been paid to the trustee by the members and the employer, as a matter of contractual obligation between them; the doctrine of resulting trust has never applied to contractual obligations. I would have thought that the better analysis was not under trust law but in contract. The employer, being required to pay only the balance of cost, contracted to pay the amounts required them time to time by the actuary on the implied term that if the payments are excessive he is to recover the amount overpaid...The authorities are in considerable disarray...I find it impossible to state the existing state of law as to the ownership of ultimate surplus in the absence of express provision as to its destination. The matter obviously requires substantial rethought and I suggest that a contractual analysis is more appropriate than the analysis based on resulting trust.

His Lordship conceded that his view was not that reflected in the cases. There is, in any case, a fundamental difficulty with his statement. In the context of superannuation or pension schemes the rights that arise in respect of benefits arise by virtue of the trust. This is not to say that there is no contractual element; generally the contract of employment will give the employee the right, subject to the terms of the trust, to be a member of the employer's pension scheme. The contract of employment will also generally authorise the deduction of contributions and oblige the employer to make the required contributions to the trustee. But this does not mean that the matter is simply one of contract or that the employees have contractual rights to their benefits. The mechanism employed to deliver the benefits is that of the trust. A superannuation or pension scheme established by contract would have no separate fund or trustee to manage the fund. Benefits would simply be paid from the employer's account. No issue of surplus would arise. Indeed, it is by virtue of the use of a trust that potential for a surplus arises.

Lord Browne-Wilkinson's concern is that the presumption does not definitively identify the "owner" - but that it is a matter to be determined by reference to the source of contributions - and that the resulting trust principles fail to take account of the nature of the defined benefit scheme. In his Lordship's view, the nature of defined benefit schemes

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146 See 4.2.2.2.
dictates that the employer should always be identified as the default owner. However, as is argued in the following section, the process of attributing contributions to their appropriate sources not only implicitly entails consideration of the nature of the scheme, but is a major advantage of the trust approach. Moreover, the presumption furnished by equity accurately reflects what is the most likely intent of the contributor in the event of the trust failing to deal with the entire beneficial interest - that the contributor intended to retain the beneficial interest. So, fundamentally it is difficult to take issue with this presumption. As observed by Rickett and Grantham, the presumption, "sensible when it was formulated in the 16th century, remains eminently sensible today".

The application of resulting trust principles necessitates a two-step approach. The relevant contributors to surplus must first be determined, as it is to these contributors that the surplus will potentially result. Once it is determined that a surplus exists, and its source is identified, a resulting trust arises by operation of law. The second step is to determine, in respect of each identified source of surplus, whether or not the presumption is rebutted by evidence of contrary intention in the trust instrument. In each of these issues the influence of contractual notions of ownership has generated a level of tension in the application of general trust principles.

### 6.2.3.1 Source of Contributions

In a superannuation fund there are three contenders for the distribution of a realised surplus: the employer, the members and the Crown. Leaving aside the Crown, in the context of a defined benefit scheme, both employers and members defer to competing contractual notions of ownership to support their claim to surplus: either the fund is a form of deferred pay (the members' view), or the employee members have received all to which they are contractually entitled (the employers' view).

The courts have again eschewed these notions preferring instead to trace not only the source of contributions but also the use of those contributions within the scheme. Davis v Richards & Wallington Industries Ltd (the "Richards & Wallington case") provides an apposite example of this process. In respect of the pension scheme in issue, Scott J

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147 See 6.2.3.1.


149 Davis v Richards & Wallington Industries Ltd [1990] 1 WLR 1511 at 1542-1543 per Scott J.

150 Davis v Richards & Wallington Industries Ltd [1990] 1 WLR 1511.
determined that the surplus arose from three sources: employees' contributions, transfers from other pension schemes and employers' contributions. Pursuant to the scheme, the employees were obliged to contribute a set amount of five per cent of salary, whereas employers were required to pay what was necessary to the fund scheme—a typical cost of balance scheme. In addition, during the life of the scheme, funds had been transferred in from other companies' schemes. In terms of attributing a proportion of surplus, it was possible to simply calculate the total contributions from each source and return the surplus pro rata to its source. Yet Scott J preferred to take account of the nature of the scheme and the bases upon which contributions were utilised in the fund. As the employer was required to fund any deficit, in his Lordship's view, the amounts contributed by employee members, in conjunction with the amounts transferred into the scheme, represented the base against which the employers' contributions were assessed. Given it was the likely situation that some contribution was required from the employers in order to produce assets sufficient to provide overall benefits, the scheme benefits were to be treated as being funded first by a combination of the employees' contributions and the transferred funds, and then, by the employers' contributions. As a result, Scott J held that the whole of the surplus was to be regarded as being derived from the employers' contributions.

It may be argued that Scott J chose to favour the contractual position of employers. However, the above examination of his reasoning reveals that his Lordship was concerned with the nature of the trust and how the trust utilised contributions, not underlying notions of ownership. This is evident also in the judgment of the Privy

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151 Davis v Richards & Wallington Industries Ltd [1990] 1 WLR 1511 at 1542.
152 Davis v Richards & Wallington Industries Ltd [1990] 1 WLR 1511 at 1543. The process undertaken by Scott J is consistent also with the observations of Millett J in Re Courage Group's Pension Schemes [1987] 1 All ER 538 regarding the nature of surpluses in defined benefit schemes. His Lordship stated (at 545):

"Such surpluses arise from what, with hindsight, can be recognised as past overfunding. Prima facie, if returnable and not used to increase benefits, they ought to be returned to those who contributed to them. In a contributory scheme, this might be thought to mean the employer and the employees in proportion to their respective contributions. That, however, is not necessarily, or even usually, the case. In the case of most pension schemes...the position is different. Employees are obliged to contribute a fixed proportion of their salaries or such lesser sum as the employer may from time to time determine. They cannot be required to pay more, even if the fund is in deficit; and they cannot demand a reduction or suspension of their own contributions if it is in surplus. The employer, by way of contrast, is obliged only to make such contribution if any as may be required to meet the liabilities of the scheme. If the fund is in deficit, the employer is bound to make it good; if it is in surplus, the employer has no obligation to pay anything...From this, two consequences follow. First, employees have no legal right to "a contribution holiday". Second, any surplus arises from past overfunding not by the employer and the employees pro rata to their respective contributions but by the employer alone to the full extent of its past contributions..."

See also Wrightson Ltd v Fletcher Challenge Nominees Ltd [2002] 3 NZLR 1 at 14 per Lord Millett (PC).
Council in *Air Jamaica Ltd v Charlton*. In this case, the scheme was defined benefit in nature and contributions were payable by the members with matching contributions by the company. Although the employers were further obliged to make additional payments into the fund if required by the trustees, such further repayments had never in fact been required. In view of the circumstances, the surplus was "treated as provided as to one half by the company and as to one half by the members". Clearly, in this scenario, not only did the nature of the scheme and the way in which contributions were to fund end benefits influence the Privy Council's decision, but it was these factors that distinguished the situation from that in the *Richards & Wallington* case. If in the alternative, the general law had adopted a contractual approach to attribute the source of surplus, it would have been impossible for the Privy Council to conclude that the surplus was to be shared.

These two contractual theories as to ownership are by their very nature mutually exclusive. If contributions are recognised as deferred pay, the surplus will be attributed to employees. Conversely, if employees have received all that they bargained for, the surplus will be attributed to the employer. A preference for one view necessitates not only the rejection of the other, but also attribution of the entire surplus in accordance with the chosen view. Whilst the employer view may be seen to accord with the nature of the pure cost of balance defined benefit scheme, this results only from the courts' consideration of the nature of relevant scheme in the process of attribution rather than paying heed to a contractual conceptualisation of ownership.

As is demonstrated by the outcome in the *Air Jamaica* case, where the nature of the scheme and the process of funding benefits varies, the process of investigation inherent in the application of general trust law principles accounts for such variations. By comparison, the contractual approach is rigid in nature. It compels the choice of one particular view and once that choice is made, it operates independently of the nature of the individual scheme at hand. Thus the approach of the courts has been to prioritise trust principles, which in turn has prioritised the individual nature of the trusts at hand. The advantage of this approach is not only its flexibility, but also the fact that it seeks to reflect the operation and reality of the scheme in determining the source of surpluses.

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154 *Air Jamaica Ltd v Charlton* [1999] 1 WLR 1399 at 1404 per Lord Millett.
155 *Air Jamaica Ltd v Charlton* [1999] 1 WLR 1399 at 1411 per Lord Millett.
It has been argued that difficulty in attributing the source of surplus is a reason to reject the application of a resulting trust. On this point Davis argues that “whilst it may be possible to calculate how much the employer and members and former members have settled on the fund by contributions, it is generally impossible to determine what part of surplus is attributable to the various contributions, as, in many instances, surpluses are, to a significant extent, attributable to investment returns exceeding the anticipated returns”. Similarly, in the Richards & Wallington case, one of rationales put forward by Scott J for denying the operation of resulting trust was difficulty in apportioning the surplus between members and arriving at a workable scheme.

But difficulty of application has not traditionally barred a resulting trust. In Re Gillingham Bus Disaster Funds property was conveyed on trust by public subscription for the purpose of providing benefits to the families of boy cadets who had been injured or died in a bus accident. The fund far exceeded that required and the court ruled that the fund reverted on resulting trust to the subscribers. That the identification of the subscribers was difficult and time consuming Harman J found no bar to the existence of a resulting trust. The difficulty of assessing the source of contributions has also been noted, extra judicially, by Lord Millett:

...attributing a surplus can never be more than rough and ready. It is impossible to identify the contributions which were responsible for generating the surplus. It is impossible even to identify the period during which such contributions were made. Surpluses appear and disappear.

Nor have difficulties in quantifying equitable interests generally been a ground for denying such an interest, as is evident in the approach to equitable tracing adopted by the House of Lords in Foskett v McKeeown.

Given the very nature of surplus and the fluctuations that can arise in actuarial valuations during the life of a fund, it may not be possible to identify exactly the source of surplus. However, the alternatives at general law are to either adopt one of the

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157 See 6.2.3.2.
159 Re Gillingham Bus Disaster Fund [1958] Ch 300 at 314.
161 [2002] 2 WLR 1299.
162 As to actuarial valuations see 6.2.2.
two conflicting contractual views or pass the surplus to the Crown as bona vacantia. The adoption of either of these alternatives results in the application of a doctrine that essentially ignores the individual nature of trusts. Thus, whilst a difficulty in attributing source is avoided, it is replaced with an approach that disregards not only the nature of individual schemes but ultimately the intent of the settlor. At the very least the judiciary should strive to reflect the nature and operation of superannuation and pension funds in the attribution of the source of surpluses. Thus in the words of Lord Millett, “we should not strain after exact accuracy. Nor is the impossibility of attaining it an argument against the resulting trust”.

6.2.3.2 APPLICATION OF THE PRESUMPTION

Once the surplus has been attributed, the next issue is whether the presumption of resulting trust will operate in respect of the sources identified, or is rebutted by evidence of contrary intention expressed in the trust instrument. Given that the surplus, or relevant part thereof, may devolve to the Crown where the presumption of resulting trust is rebutted, it is invariably the Crown that seeks to deny the interests of the employer or employees. In each respect the issue is one of interpretation.

Employers

As to employers, the Crown has, until *Air Jamaica Ltd v Charlton* successfully relied upon a clause appearing in many deeds to the effect that “any money that has been contributed by the company is prohibited from being repaid to the company”. In *Re ABC Television Ltd Pension Scheme* and *Rees v Dominion Insurance Co of Australia Ltd (in lig)* similar provisions have been held to rebut a presumption of resulting trust. However, as a matter of interpretation, the Privy Council in *Air Jamaica* expressly disapproved of this approach, citing it as “wrong in principle”. It viewed the issue not as whether the transferor positively intended to retain a beneficial interest, but in the negative – that is, the presumption will be rebutted if it is established that the transferor

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164 (1999) 1 WLR 1399.
165 (Unreported, Chancery Division, 22 May 1973, Foster J).
166 (1981) 6 ACLR 71 (NSWSC).
167 *Air Jamaica Ltd v Charlton* [1999] 1 WLR 1399 at 1412. See also *Rees v Dominion Insurance Co of Australia Ltd (in lig)* (1981) 6 ACLR 71 at 78 per Waddell J (NSWSC).
168 *Air Jamaica Ltd v Charlton* [1999] 1 WLR 1399 at 1412.
did not intend to retain the beneficial interest in the circumstances. Speaking extra-
judicially, Lord Millett, as the member who gave the advice of the Privy Council in Air
Jamaica, has characterised the issue as one of burden of proof:

The point is that the transferor does not have to prove that he intended to retain the
beneficial interest, still less create a resulting trust in his own favour. It is enough for him
to establish that he did not intend the beneficial interest to pass to the recipient in the
events which have happened.

The Privy Council’s concern is essentially one of approach. The presumption of
resulting trust will arise “automatically” by operation of law in the failing trust scenario.
To this extent, and this extent only, the resulting trust can be considered “automatic”.
At this point the contributor is presumed to have retained a beneficial interest to the
surplus. Consequently, there is no need to assess whether or not the contributor
intended to retain a beneficial interest in the fund. In this sense the resulting trust is
not affected by positive intention. Instead, the relevant question is whether or not there
is any evidence that indicates that the contributor did not intend to retain the beneficial
interest. This is important as it affects the burden of proof.

In applying this approach to the facts, the Privy Council held that a provision that
 prohibited an amendment that resulted in monies contributed by the company being
repaid to the company was not effective to rebut the resulting trust. Instead, their
Lordships were of the view that the purpose of such a clause was to preclude any
amendment that would allow repayment of contributions under the terms of the
scheme but “not as a pre-emptive but misguided attempt to rebut a resulting trust
which would arise dehors the scheme.”

It is unfortunate that Lord Millett concluded the foregoing sentence with the words
“dehors the scheme” as it tends to confuse the point already made regarding the onus of
proof. In that the presumption of resulting trust arises to the fill a gap in beneficial
ownership (not otherwise provided for by the trust), it arises outside of the scheme.
Strictly on this basis, the statement is entirely consistent with Lord Millett’s earlier
comments regarding onus of proof. However, the danger of his Lordship’s statement is
that, read as a whole, it implies that any clause within a scheme cannot affect the
presumed resulting trust as it operates only during the continuation of the scheme. The

Pension Lawyer 1 at 9.

170 Air Jamaica Ltd v Charlton [1999] 1 WLR 1399 at 1412. See also the obiter comments of Rimer J
logical extension of this argument is that the provisions of the trust, in that they relate to the scheme whilst in operation, cannot affect the beneficial interest in surplus upon termination. Pursuant to this approach only words that specifically and expressly relate to the surplus upon winding up can operate to rebut the resulting trust. If such words exist, more likely than not they would specifically provide for the destination of surplus thereby leaving no room for the operation of the presumption. To this end, the rationale utilised by Lord Millett leads, in practice, to an irrebuttable presumption of resulting trust. Interestingly, this accords with a view expressed extra-judicially by Lord Millett that the application of the principles of bona vacantia are inappropriate in the failing trust cases\(^\text{171}\) and his characterisation of the Quistclose trust in Twinsectra Ltd v Yardley.\(^\text{172}\) If in practice the presumption of resulting trust is irrebuttable, this prevents the beneficial interest devolving on the Crown.

A better approach is to limit Lord Millett's comments to advocating a purposive approach to interpretation. At first reading the words "no moneys which at any time have been contributed by the company under the terms hereof shall in any circumstances by repayable to the company" convey that the employer has made the contributions on an "out and out" basis, evincing an intention not to retain an interest upon the failure of the trust to dispose of the entire beneficial interest. However, on a purposive approach, in the view of the Privy Council the purpose of the clause was limited and did not extend to rebutting a presumption of resulting trust. It is regrettable that the speech did not further elucidate this point as it would have provided further guidance on the application of the purposive approach. For instance, could the purpose of the limitation be conceived as being protective in nature? If this is the case then it could be argued that the fund must be protected during continuation so to ensure sufficient benefits upon termination. Thus, any payment out to the employer would not be permitted. If a surplus exists upon termination, provision has been clearly


\(^{172}\) [2002] 2 All ER 377 (HL). In Twinsectra Lord Millett characterised the Quistclose trust as "an entirely orthodox example of the kind of default trust known as the resulting trust" (at 403). Accordingly, a lender who pays money to a borrower by way of loan for a specific purpose does not part with the entire beneficial interest. Instead, the interest so retained is held on resulting trust for the lender. That this conceptualisation is an orthodox example of a resulting trust must be questioned. The resulting trust appears to arise from the settlor's intention to lend money of a specific purpose. This type of intention is more commonly associated with an express trust. Moreover, the conceptualisation does not contemplate that the presumption of resulting trust can be displaced by evidence of contrary intent. Indeed, the possibility of displacement is entirely inconsistent with the circumstances. It is in this context that Lord Millett can be said to have conceived the presumption of resulting trust as irrebuttable.
made for members' benefits and so no issue of protection or security arises. Consequently, the provision does not operate once the scheme has terminated and thus does not rebut a resulting trust.

The purposive approach is a preferred basis for the decision as it looks to ascertain specific notions of intent and does not take the presumption of resulting beyond accepted bounds. It may be asserted that there is little difference between these two bases in that the purposive approach and the irrebuttable presumption achieves the precisely same result. However, the outcomes will not always be necessarily the same. Take, for example, a situation where a taxing statute, as a prerequisite for concessional taxation treatment, requires the exact clause in issue to be included in a superannuation trust. In this scenario the fiscal origin of the clause may vary its purpose. This is similar to the circumstances in *National Grid Co plc v Mayes* where the Inland Revenue would not approve a scheme unless it included a provision prohibiting any amendments that made any moneys of the scheme payable to any employer. Although the issue in *National Grid* concerned amendment, the Privy Council's interpretative approach in *Air Jamaica* is equally applicable. As the provision was required at the instance of the Inland Revenue, in Lord Hoffman's opinion the most relevant background of the clause was its fiscal origin. Pursuant to the relevant Acts any approved scheme enjoyed great fiscal privileges in the form of taxation concessions. Given this, Lord Hoffman concluded that:

> ...it is hardly surprising that capital payments out to the fund to the employer were anathema to the revenue. They did not want the employer to be able to resort to a tax sheltered fund, either temporarily or permanently, for the purposes of business.

The application of this logic to the resulting trust example described above may tend to favour a conclusion that the employer did not intend to retain a beneficial interest in surplus. Instead, the purpose of the clause was to prevent the return of moneys to the employer once those moneys had been contributed, whether during the operation of the scheme or upon its termination. To this end, the employer contributed on an "out and out" basis and thus the presumption was rebutted.

Yet this approach should not be extended so far as the reasoning for the decision in *Simes & Martin Pty Ltd v Dupree*. Here, although the employer had made contributions

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174 *National Grid Co plc v Mayes* [2001] 1 WLR 864 at 870 (HL).
175 (1990) 55 SASR 278.
to the fund, Legoe J returned an undistributed surplus to the employee members. One of the reasons for rejecting the employer's claim for a resulting trust in its favour was that the employer had made the contributions for the purpose of attracting taxation advantages and therefore was not entitled to recoup the contribution.\textsuperscript{176} It may prima facie appear that the rationale corresponds to that extracted from the National Grid case. To the extent that consideration was given to the fiscal background of the scheme, this is correct. However, the two cases can be distinguished. In National Grid the court was interpreting a specific provision of the trust deed, inclusion of which was required by the taxing authorities. To the contrary, in Simes the fiscal origin was considered generally relevant and did not relate specifically to a provision of the deed. For this reason the approach in Simes arguably goes beyond generally accepted principles. Legoe J did not appear to examine the deed so as to determine whether or not there was any indication reposed in the deed that the employer did not intend to retain a beneficial interest in the fund in the event of a surplus.

Though it is accepted that part of the reason for employer contributions is to obtain taxation concessions, this in and of itself is arguably insufficient to rebut a resulting trust. Implicit in the Privy Council's approach in Air Jamaica is a requirement to examine the wording of the deed and to look at the purpose of the relevant provisions. If the legislature has not gone so far as to prevent the return of any part of the fund it cannot be presumed that repatriation is prohibited. Instead, the matter may be one of deterring repatriation via the imposition of taxation penalties.

To summarise, whilst the rebuttal of a resulting trust in favour of the employer has not concerned the influence of contractual considerations on general principles of trust law, it has been argued that the first possible interpretation of Lord Millett's approach in the Air Jamaica case, the irrebuttable presumption of resulting trust, arguably goes beyond established general principles. To this end, the purposive approach is preferred as one that seeks to promote the intention underlying the clause in issue.

**Employees**

The Crown has stressed the contractual background of superannuation and pension schemes as a means of rebutting a presumption of resulting trust that arises in favour of employee members. The usual argument is that employees have contractually agreed

\textsuperscript{176} Simes \& Martin Pty Ltd v Dupree (1990) 55 SASR 278 at 287-288.
that in return for their contributions to the fund they will receive a benefit at the appointed time. Where a surplus exists upon winding up, members' benefits have been provided for, and so members have received all that they have bargained for. The mere act of contributing to the fund manifests an intention to irrevocably part from their money.177

In Richards & Wallington Scott J was not totally convinced that the contractual origin of rights under a pension scheme was necessarily decisive.178 However, two further factors impressed upon him to hold that a resulting trust would not apply in respect of employees and the surplus (if any) attributed to this source would pass to the Crown. First, Scott J took in account that it would, in his view, be impossible to arrive at a workable scheme for apportioning the surplus and thus equity should not impute an intention to the members that would lead to an unworkable result.179 Secondly, permitting the members to enjoy part of the surplus would probably have resulted in the members exceeding the benefit limits prescribed by the Department of Inland Revenue in England, and permitting a resulting trust in such circumstances would impute to the employees an intention that was precluded by the relevant legislation.180

This approach was expressly disapproved in the Air Jamaica case and labelled by their Lordships as erroneous.181 The difficulty of arriving at a workable scheme arose from Scott J's belief that it was necessary to value the benefits that each member had received in order to determine the appropriate amount of surplus. According to their Lordships in Air Jamaica, this difficulty is avoided if the members' share of the surplus is simply divided pro rata according to the contributions made by each member (without regard to the benefits that each has received).182 Exceeding the benefit limits prescribed by the Department of Inland Revenue their Lordships considered was not a proper ground upon which to deny the operation of a resulting trust. The Inland Revenue had

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177 See the arguments presented in Rees v Dominion Insurance Co of Australia Ltd (in liq) (1981) 6 ACLR 71 (discussed at 78-79 by Waddell J); Davis v Richards & Wallington Industries Ltd [1990] 1 WLR 1511 (discussed at 1539-1541, 1543-1544 by Scott J); Air Jamaica Ltd v Charlton [1999] 1 WLR 1399 (discussed at 1411-1412 by Lord Millett J (PC)). See also Lord Millett, "Pension Schemes and the Law of Trusts: The Tail Wagging the Dog?" (2000) 84 Pension Lawyer 1 at 8.

178 Davis v Richards & Wallington Industries Ltd [1990] 1 WLR 1511 at 1539.

179 Davis v Richards & Wallington Industries Ltd [1990] 1 WLR 1511 at 1543-1544.

180 Davis v Richards & Wallington Industries Ltd [1990] 1 WLR 1511 at 1544.

181 Air Jamaica Ltd v Charlton [1999] 1 WLR 1399 at 1412.

182 Air Jamaica Ltd v Charlton [1999] 1 WLR 1399 at 1413.
examined the pension plan and approved its provisions. Moreover, "there is no call to distort principle in order to meet their requirements. The resulting trust arises by operation of the general law, dehors the pension scheme and the scope of the relevant tax legislation".

Whilst disapproving of the approach in Richards & Wallington, their Lordships leaned to notions of contract to determine the issue of whether or not the resulting trust applied to surplus sourced from employee members. The trust deed in question expressly provided for the distribution of final surplus by way of augmenting members' benefits, but this provision was held to be void by reason perpetuity. As such, the question of a resulting trust arose. In determining that the presumption of resulting trust was not rebutted, the Privy Council reasoned that due to the failure of the various provisions, most particularly that of surplus distribution, the members had "not received all that they bargained for". The focus upon "bargain" is clearly a contractual notion and results from the influence of the employment contract. The general interpretative approach applied to trust deeds permits reference to the factual background such as the underlying employment relationship. However, the danger of the approach adopted by the Privy Council in Air Jamaica is that if it taken to its logical conclusion contractual notions of ownership take precedence over the intention reflected in the trust deed.

To counter this it may be argued that evidence of agreement between the parties is relevant to rebut a resulting trust. Take, for example, Muschinski v Dodds where the appellant had contributed $10/11ths of the purchase money for the purchase of a house with her de facto husband. The legal title was taken as tenants in common. Upon the breakdown of the relationship the appellant claimed that she was entitled by way of resulting trust to the entire beneficial interest of the basis of her contributions. The High Court of Australia held that a presumption of resulting trust was rebutted by the parties' agreement that in return for physical work on the property the respondent "would get his name of the title"; the appellant had evinced an intention to depart with a 50 per cent share of the beneficiary interest. In similar vein, if subscriptions are made to an unincorporated association, the destination of any surplus upon winding up

183 Air Jamaica Ltd v Charlton [1999] 1 WLR 1399 at 1413.
184 Air Jamaica Ltd v Charlton [1999] 1 WLR 1399 at 1413.
186 (1985) 160 CLR 583.
187 Muschinski v Dodds (1985) 160 CLR 583 at 591-592 per Gibbs CJ.
is dictated by the rules of the association (ie a contract between the members inter se) rather than by resulting trust.\(^{188}\)

But one feature serves to distinguish these cases from that of a superannuation or pension trust: the existence of an initial trust deed. Although in the above examples the contractual nature of the circumstances was an influential factor, neither concerned the failure of an express trust created by deed. In the resulting trust scenario the only evidence of intention are the statements and conduct of the relevant parties up to the date of the transaction. In a superannuation trust the relevant intention is reposed in the terms of the trust deed. Therefore, although reference to the employment background may assist to interpret the terms of the deed, according to general principle and consistent with the SRF, the terms of the deed are decisive. As such, evidence of a bargain to make contributions in return for benefits is by itself insufficient to imply that the contributions were made on an out and out basis. Required is direct evidence flowing from the trust deed that the contributor did not intend to retain a beneficial interest in the event that the trust fails to distribute the entire beneficial interest.

In *Air Jamaica* the Privy Council was clearly influenced by the justice of the outcome. The trust deed had expressly provided that surplus was to be used to augment member benefits. Because the provision was held void for perpetuity it was not possible to apply the trust deed. Therefore, to hold that the surplus be returned to members, as they had not received all that they had bargained for, was consistent with the intent of the parties. Yet, in terms of principle, a better approach is to avoid treating the bargain as being determinative of the issue. This is not to say that the underlying employment relationship should never influence the court in interpreting a trust deed; it can be used to support an interpretation of the words of the deed rather than as independently determinative of the issue. In *Air Jamaica* Lord Millett hinted at this by his observation that\(^{189}\)

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\[...\]

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\(^{188}\) *Re Buck's Constabulary Widows & Orphans Fund* [1979] 1 All ER 623.

\(^{189}\) *Air Jamaica Ltd v Charlton* [1999] 1 WLR 1399 at 1412.
Cory J, of the Supreme Court of Canada, aligned himself with this view by expressing the following dicta:¹⁹⁰

I do not think that any general rule can be laid down as to the intentions of employees contributing to a pension trust. Where the circumstances of a particular case do not indicate any particular intention to part outright with money contributed to a pension fund, equity and fairness would seem to require that all parties who contributed to the fund should be entitled to recoup a proportionate share of any surplus subject to the resulting trust.

And finally, as noted above, in Richards & Wallington¹⁹¹ Scott J was not totally convinced that the contractual origin of rights under a pension scheme were necessarily decisive.

In a manner consistent with the SRF, courts have clearly swayed away from contractual notions of ownership. Therefore, arguments that ultimately seek to determine the issue on the grounds of a preferred policy basis that may or not be consistent with the intention expressed in the trust instrument should be eschewed.

6.2.4 STATUTORY INITIATIVES

With the exception of Hong Kong,¹⁹² all of the regulatory systems canvassed by this thesis address the issue of surplus, most particularly that of returning surplus to the employer. In Australia, repatriation of surplus is prohibited unless certain procedures have been followed. In New Zealand, Ontario and the United Kingdom, payment out to the employer is permitted with the consent of the regulator. However, in the latter two jurisdictions the prescribed conditions for consent must first be made out, and in the case of Ontario, member consent is an added prerequisite. The specific detail of each jurisdiction is set out in Chapters 2 and 3.¹⁹³ For the purpose of this section, five aspects of these statutory requirements arise for consideration.

(i) The Trust Instrument

Although the return of surplus to the employer is the subject of regulation, an express power in the trust deed to distribute to the employer is nonetheless required. In Australia,

¹⁹¹ [1990] 1 WLR 1511 at 1539.
¹⁹² In that the MPF regulatory regime in Hong Kong is premised purely upon defined contribution schemes, surplus is not a significant issue. See further 3.4.3 but note that the surplus rules pursuant to the ORSO regime have been included in that section for the sake of completeness.
¹⁹³ See 2.1.3 (Australia), 3.2.3 (United Kingdom) 3.3.3 (Ontario) and 3.4.3 (New Zealand).
Ontario and the United Kingdom this requirement is statutorily reinforced. Difficulties will arise if the trust deed is unclear as to the distribution of surplus. A particular strength of the Ontario regime is that it attempts to address this issue by making it a requirement of registration that all pension plans address the treatment of surplus during both the continuation of the plan and on its winding up. The legislature then applies two rules of construction:

- where the pension plan does not provide for the withdrawal of surplus money while it continues in existence, it is statutorily required that the plan be construed to prohibit any such withdrawal; and
- where the pension plan does not provide for the payment of surplus money on its winding up, the surplus money is to be distributed proportionately between members, former members and other persons entitled to payments under the pension plan on the date of winding up.

The advantage of this approach is that the settlor is required to specifically draw his or her mind to the issue of surplus. The rules of construction then confirm that any payment out to the employer must be expressly authorised; it cannot be implied from the words of the deed. Although this reflects the general law position – direct payment out of the fund requires an express power to that effect – the prescribed rules of construction nevertheless import a degree of certainty in interpretation. The second rule of construction has the further effect of negating the operation of the presumption of resulting trust. Regardless of the source of contributions, in the absence of alternative provision surplus will vest in the members and former members. This in turn reflects a strong policy view, more so than in the other jurisdictions, that pension benefits represent deferred pay. To this end, the object of the rule is identical to the object of the presumption of resulting trust – to fill the “intention” gap.

(ii) Exercise of the Power to Distribute

Where the trust instrument expressly permits the return of surplus to the employer and also vests in the employer the power to effect this outcome, there exists significant agency risk. The interests of the employer are not aligned with those of beneficiaries, creating a

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194 SIS Act s 117(5)(a); Pension Benefits Act RSO 1990, P8, ss 78-79; Pensions Act 1995 (UK) ss 37(1)(a), 76.
195 Pension Benefits Act RSO 1990, P8, s 10: see Table 3.1 at 3.1.2.2.
196 Pension Benefits Act RSO 1990, P8, s 79(2).
198 As to the general law position see 6.2.2.2.
199 As to resulting trusts see 6.2.3.
risk that the employer's interests will be preferred. This is not to taint employers with a "fraudulent nature" brush; it simply identifies an area of risk. To this end, the United Kingdom, regardless of alternative provision in the trust instrument, only permits trustees to exercise a power to return surplus to the employer.\textsuperscript{100} In Australia, employers are prohibited from exercising any discretion unless the trust instrument also requires the trustee to consent to that exercise.\textsuperscript{201} Moreover, specifically in respect of the return of surplus to the employer, the trustee must by resolution declare an intention to pay an amount out of the fund – the decision is not left to the employer.\textsuperscript{202} The advantage of these regimes is that the balance of control is shifted back to trustee, reinforcing the trustee as the central responsible entity. In the context of the SRF, the reduction of risk – in this case, the risk of improper employer control and influence – justifies restricting the general law freedom of the settlor to define the terms of the trust instrument.

\textbf{(iii) Regulator Consent}

Although Canada and New Zealand permit an employer to exercise a power of repatriation, like the United Kingdom, agency risks are mitigated by the requirement of regulator consent. Again justifiable on the basis of the prudential security limb of the SRF, this restriction provides a barrier against undue control and dissipation of the trust fund. It also implements a process of checks and balances. The danger with actuarial surplus is its notional nature; changes in assumptions can produce widely divergent results and thus its valuation is open for manipulation.\textsuperscript{203} Direct regulatory oversight is a final line of defence and protection for the fund and ultimately the interests of the beneficiaries.

\textbf{(iv) Balancing of Interests}

The employment context of the superannuation trust has prompted calls for trustees to consider the interests of employers and to balance those interests against the interests of the members.\textsuperscript{204} This concept of balance, it has been argued, underlies the surplus regulation provisions in the SIS Act. Pursuant to s 117 payments are prohibited unless made

\textsuperscript{100} Pensions Act 1995 (UK) s 37(2).
\textsuperscript{201} SIS Act s 59.
\textsuperscript{202} SIS Act s 117(3)(b).
\textsuperscript{203} See 6.2.2.
in accordance with the prescribed procedures. These procedures require in part that, prior to declaring by resolution an intention to make a payment out to the employer, the trustee [be]...satisfied that the payment of the amount and the making of the changes (if any) to the governing rules were reasonable having regard to the interests of the employer-sponsor and of the beneficiaries of the fund.

Prima facie this provision appears to require the trustee to go beyond the duty at trust law to act, to the exclusion of all other interests, in the interests of the beneficiaries and its statutory codification in the SIS Act s 52(2). Instead, the trustee is to ensure that the proposed payment or required amendment are reasonable having regard not only to interests of the beneficiaries but also to those of the employer-sponsor. To the extent that this represents a departure from general law principle, it is not justified. Not only is it inconsistent with the juristic nature of the best interests duty, it is fundamentally inconsistent with the protective features of the trust. On this basis, the SRF precludes a development in the law that lessens the absolute nature of the trustee's duty to beneficiaries.

Upon closer analysis, it is arguable that s 117(5) does not, in any event, support a balancing of interests approach so as to water down the trustee's duty of the beneficiaries. As a matter of statutory construction, s 117(5)(c)(ii) must be interpreted in the context of the entirety of s 117(5). Of particular significance is in this context is s 117(5)(a), which reads:

117(5) An amount may be paid out of any standard employer-sponsored fund to a standard employer-sponsor if the following requirements are fulfilled:

(a) apart from this section, the governing rules would require or permit the amount to be paid to the employer-sponsor...

So, prior to a payment being allowed pursuant to s 117(5), the trust deed must make provision for payment to the employer-sponsor. Under general trust principles, where a trust deed makes provision for distribution to a person, that person is, by definition, a beneficiary of the trust. In the circumstances set out in s 117(5), the employer-sponsor is at the very least a contingent beneficiary of the fund. Consequently, s 117(5) will not operate so that a payment can be made to an employer-sponsor unless that employer-sponsor is a beneficiary, whether discretionary or fixed, of the fund. Viewed in this context, s 117(5)(c)(ii)

205 SIS Act s 117(3).
206 SIS Act s 117(5)(c)(ii) (emphasis supplied).
208 See 6.5.2.
merely reflects the traditional trust law principle that a trustee must act in the best interests of the beneficiaries as a whole.\footnote{Cowan v Scargill [1985] 1 Ch 270 at 286-287 per Megarry VC. See 6.5.1.2.}

In the interests of consistency and clarity, the approach expressly adopted in the United Kingdom is preferred. There the regulator, OPRA, must be satisfied that the trustees are satisfied that it is in the best interests of members that a payment be made to the employer. This not only reinforces trustees' general law duty but also clarifies the role of trustees as protectors of the trust fund and beneficiary interests.\footnote{See further the arguments and conclusions drawn in 6.5.2.}

\section*{(v) Member Consent}

Both the Australian and United Kingdom regimes require that members be notified of a proposed return of surplus to the employer, thereby affording an opportunity for member objection. By comparison, the regime in Ontario embraces the full ideal of member consent. Where a return from actuarial surplus is proposed, the consent of all members and pensioners is mandated.\footnote{Pension Benefits Act RSO 1990, P8, ss 10(1), 79(1).} In the context of returning a realised surplus, the consent of the collective bargaining agent, or otherwise at least two-thirds of members, is required.\footnote{Pension Benefits Act RSO 1990, P8, s 79(1), Pension Benefits Act RRO 1990, Reg 909, s 8(1).} This system promotes what is in essence a surplus sharing agreement. In turn it reflects the underlying nature of the Ontario regime; there is a direct contractual obligation to provide pensions and the employer is most often the administrator of the scheme.\footnote{See 3.2.2.2. As to the practical difficulties of implementing this consent based scheme see Steeves, “The Treatment of Pension Surplus in Canada” (1998) 23 International Pension Lawyer 8.} This scenario yields potential for a significant conflict of interest,\footnote{See 6.4.3.} thereby concomitantly necessitating greater control over the employer/administrator's actions. To this end, an additional line of defence is supplied – the express consent of the members. In the Australian context, there would be little prudential advantage in such an approach. Member representation at the trustee level, combined with member notification of the proposed return of surplus (thereby permitting member objection), provides a sufficient line of prudential defence against the risk of undue employer influence and control. Regulator consent would be a more advantageous and less costly option if further protection were desired.
6.3 AMENDMENT

6.3.1 GENERAL LAW

Although the power to amend a trust deed flows from several sources, trust instruments usually contain an express power of amendment. This is particularly so in superannuation trusts, the ongoing nature and operation of which within a constantly changing commercial and regulatory background necessitates the provision of flexibility.

A power to amend in a superannuation trust is generally conferred on either the trustee or the principal employer-sponsor of the fund. However, its scope is limited by general law principles and any specific limitation expressed in the trust instrument, and an amendment that falls outside such bounds is invalid. The scope of an amendment power is often limited by a requirement of consent. Where the power to amend is conferred upon the trustee, a prerequisite to its exercise may, for instance, be the consent of the employer-sponsor (and vice-versa). The addition of a consent requirement contemplates a level of negotiation between the trustee and employer to effect an amendment, which in turn highlights the tripartite nature of the superannuation trust. It also adds a layer of protection for beneficiaries. Where the power of amendment is vested in the employer, a prerequisite of trustee consent ensures that members' interests are safeguarded by the amendment.

Where the power is vested in the trustee, a prerequisite of employer consent prevents benefit or contribution levels being increased to amounts that are not sustainable by the employer.

Other common express restrictions include prohibiting amendments that alter the main purpose of the fund or result in the return of moneys to the employer (otherwise termed a

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215 In the absence of a power of amendment in the trust deed, application for amendment must be made to the court pursuant to its inherent or statutory jurisdiction, or otherwise pursuant to the consent of the beneficiaries (Spellson v George (1992) 26 NSWLR 666). As to the inherent and statutory jurisdiction of the court see Dal Pont and Chalmers, Equity and Trusts in Australia and New Zealand (2nd ed, LBC Information Services, 2000), pp 672-679; CCH, Australian Superannuation Law and Practice (CCH, Looseleaf), ¶21-210-¶21-220.

216 See Case 22/98 98 ATC 282 at 290 where the Administrative Appeals Tribunal (Australia) commented that “[a]mendment and modifications of the constituent documents of superannuation funds are normal and in accord with common practice in the industry...Amendments – even far-reaching amendments – are therefore not only usual but are accepted and expected in the indefinitely continuing life of the fund”. See also Arthur, Pensions and Trusteeship (Sweet & Maxwell, 1998), p 181.

217 This flows from the duty of trustees to act in the best interests of beneficiaries: see 6.5.1.
"permanent alienation" clause). Additionally, prohibiting any amendment that reduces accrued rights or adversely affects the beneficiaries' interest in the fund may foster protection for members and beneficiaries. The trust deed constituting the Airways Pension Scheme provides an apt example of a power of amendment expressly qualified by all of the above restrictions. The relevant deed provided:

The provisions of the Trust Deed may be amended or added to in any way by means of a supplemental deed...No such amendment...shall take effect unless the same has been approved by a resolution of the management trustees in favour of which at least two thirds of the management trustees for the time being shall have voted PROVIDED THAT no amendment or addition shall be made which:

(i) would have the effect of changing the purpose of the Scheme, or

(ii) would result in the return to an employer of their contributions or any part thereof, or

(iii) would operate in any way to diminish or prejudicially affect the present or future rights of any then existing members or pensioner...

Express restrictions on amendment may, moreover, have a wider operation than simply limiting amendment. The scope of general powers under other provisions may be limited by the restrictions placed upon the amendment power. For example, if a wide power to make arrangements for the distribution of surplus is conferred upon the trustee, absent powers for reducing surplus by specific means, any restriction on the amendment power will operate to concomitantly restrict the avenues for reducing surplus or providing for its distribution upon termination.219 To this end, the restrictions are relevant to defining the bounds (or the "four corners") of the scheme.

Normal principles of interpretation apply to determine whether or not a proposed amendment is within power.220 Words are to be given their natural meaning and construed in the context of the entire trust instrument.221 As is discussed below, the practical and purposive approach heralded by Millett J in Re Courage Group's Pension Schemes is especially relevant in the context of the interpretation of amendment powers. In addition, the courts do not interpret such a power restrictively as it is considered important "to

218 The Airways Pension Scheme was the subject of dispute in British Airways Pension Trustees Ltd v British Airways plc [2002] PLR 247.

219 National Grid Co plc v Mayes [2001] 1 WLR 864 at 873-874 per Lord Hoffman, at 882 per Lord Scott; British Airways Pension Trustees Ltd v British Airways plc [2002] PLR 247 at 134 per Arden LJ (with whom Waller and Auld LJJ concurred) (EWCA).

220 As to the general principles of interpretation relevant to superannuation trusts see 6.1.

221 Lock v Westpac Banking Corporation (1991) 25 NSWLR 593 at 602 per Waddell CJ.

222 [1987] 1 All ER 528 at 537.
avoid unduly fettering the ability of trustees to amend the provisions of the trust instrument so as to make those amendments which are required by the exigencies of commercial life. However, the power cannot be used once the process of winding up has commenced. Nor can even a very broad power of amendment be utilised for the purpose defeating the objects or "substratum" of the trust. The amendment power, it is said, is "given for the purpose of promoting the purposes of the scheme, not altering them" or for any extraneous or ulterior purpose. In essence, these principles are a specific application of the equitable fraud on a power doctrine.

As with the issue of surplus, the judiciary had steadfastly refused to directly utilise contractual conceptions of ownership to assess the validity of an amendment. Consistent with the treatment of the surplus issue, the question that arises is whether or not principles of interpretation have been utilised as a means of giving effect to an underlying current of ownership. To this end, the common restrictions placed upon the power of amendment provide a structure though which the courts' approach to amendment can be examined.

6.3.1.1 THE MAIN PURPOSE OF THE FUND

A prohibition on amendment that alters the main purpose of the fund may be expressly stated in the trust deed and is also inherent in the general law principle that amendment cannot alter the substratum of the trust. The facts of Re Courage Group's Pension Schemes [1987] 1 All ER 528 at 537 per Millett J. See also Re UEB Industries Ltd Pension Plan [1992] 1 NZLR 294 at 307-308 per Thorp J; Boynton, "Trends in Australian and New Zealand Superannuation Law" (1992) 6 TLI 95.


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Schemes\textsuperscript{230} illustrate the operation of this restriction. There an employer company established three contributory pension schemes (the "Courage schemes") for the benefit of its employees. The Courage schemes could be amended provided the amendment did not have the "effect of altering the main purpose of the Fund, namely the provision of pensions on retirement at a specified age for members". In anticipation of a takeover, the Courage schemes were closed to new entrants, including employers. The company was eventually taken over by H, who then agreed to on-sell the company to E. H proposed that the pension scheme not form part of the sale to E and that the employee members of the Courage schemes become members of E's scheme. With this in mind, H sought to be substituted as the primary company in the deeds of the Courage schemes and, once sufficient money had been transferred to E's scheme for benefits, it was then H's intention to remove the Courage scheme surpluses for its own use. The committee of management sought direction from the court on whether it was at liberty to concur in executing the required amendment deed. Millett J commented that prima facie an amendment to effect a substitution did not change the essence or part of the main purposes of the Courage schemes and in normal circumstances such substitution permitted the continuance of the scheme for the benefit of the employee members. However, in the specific circumstances before him, his Lordship held that "the proposed substitution would manifestly alter the main purpose of the schemes and be ultra vires".\textsuperscript{231} The purpose of the proposed substitution was not to preserve the Courage schemes but to prevent the schemes from continuing for the members' benefit and to bring about an unnecessary dissolution so as to gain control of the surpluses within the schemes. As the purpose for amendment was not that of promoting the trust but an extraneous and ulterior purpose, the amendment was invalid.\textsuperscript{232}

The rationale underlying Re Courage has been employed to support arguments that an amendment that seeks to confer a benefit out of surplus upon an employer is invalid by reason that it offends against the general purpose of the trust; the purpose of fund is to confer benefits upon employee members and other beneficiaries and so the entire fund should be held for their benefit. In essence, this argument is an attempt to import a de facto notion of contractual ownership in favour of the employee members through trust

the settlor: see further Ford, Austin and Ramsay, \textit{Ford's Principles of Corporations Law} (10th ed, Butterworths, 2001), [27.020].

\textsuperscript{230} Re Courage Group's Pension Schemes [1987] 1 All ER 528 at 537 (EWHC).
\textsuperscript{231} Re Courage Group's Pension Schemes [1987] 1 All ER 528 at 541.
\textsuperscript{232} Barclays Bank plc v Holmes [2000] PLR 339 at [114]-[115] per Neuberger J.
law principles of interpretation; that is, to bring through the back door what has not been accepted at the front. Again the judiciary has sheltered from these arguments by delving into the express words of the trust deed and prioritising the obligations and rights that flow from that source. Three prominent cases exemplify the curial response and approach to this issue.

The first case, *Lock v Westpac Banking Corporation*, 233 concerned the validity of a proposed amendment that sought to return a payment of surplus to the employer Bank as part of an overall scheme for the reduction of actuarial surplus. 234 It was argued that the proposed amendment was beyond power in that, as was declared by the recital to the deed, the fund was established for the purpose of providing superannuation benefits for employees and so was impressed with a trust solely for this purpose. Consequently, surplus funds could not be returned to the employer as no power to do so was reserved in the original deed. Accordingly, the amendment was said to be ineffective in that it would destroy the substratum of the trust. Waddell CJ of the Supreme Court of New South Wales accepted that an amendment could not alter the substratum of the trust, but considered that in this case the recital was not solely indicative of the substratum. Instead, it was necessary to “construe the deed as a whole” to determine whether the deed authorised the proposed variation. 235 His Honour concluded that, while a scheme may be established for the provision of benefits, “this does not mean that, should there be a surplus, the whole of it should be held irrevocably on trust to provide defined benefits for the eligible employees”. 236 On the facts, two considerations negated any such implied qualification: there was no obligation to convert actuarial surplus into benefits for members, and the Bank’s contributions could be reduced where determined by the actuary. Consequently, the amendment was held to be within power.

Similar sentiments were expressed in *National Grid plc v Mayes*, 237 where counsel representing the employees argued that the main purpose of the scheme - the provision of pensions for the employees - was inconsistent with a proposed action to make

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234 So as to reduce an actuarial surplus it was resolved that $300 million be returned to the employer Bank and a further $300 million be returned to members by way of reduced contributions and benefit improvements: *Lock v Westpac Banking Corporation* (1991) 25 NSWLR 593 at 595 per Waddell CJ.
payments or the equivalent of payments (the release of a debt) to the employer. The Privy Council rejected this argument in respect of surplus because a “surplus is (by definition) money in excess of what is needed to effect the main purpose of the scheme”. Although the issue at hand concerned the interpretation of a power vested in the employer to make arrangements to deal with surplus, the observation is relevant to amendment as their Lordships ultimately held that the other provisions of the deed, including the amendment power, restricted this power. In conclusion, the arrangement power could not give the employer power, without amendment, to do something that would contradict the express provisions of the scheme.

The main purpose and substratum argument was taken to its furthest extreme in *Hockin v Bank of British Columbia*. There the employer Bank sought the return of actuarial surplus prior to conversion of the fund from a contributory defined benefit balance of cost scheme to a defined contribution scheme. At first instance it was held that an amendment to effect a return of surplus was not beyond power as the employer had not irrevocably alienated its interest. This was confirmed on appeal, with the British Columbia Court of Appeal going so far as to state that fundamentally the pension trust was “a trust not of property, but for a purpose”, and consequently:

\[\text{[when the whole reason for that part of the settlement moneys which are in excess of the purpose to provide pension benefits is not essential to the purpose of the trust, then to that extent the trust becomes unfounded and it is necessarily implicit that the settlement ought to be partially revoked to restore the excess to the settlor.}\]

As a result of this conceptualisation of the trust, the employer was not precluded from amending the plan prior to termination to effect a return of surplus. In essence, the decision represents the use of the “purpose” argument to import a contractual notion of

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238 *National Grid Plc v Mayes* [2001] 1 WLR 854 at 860 per Lord Hoffman (with whom Lords Slynn, Steyn, and Scott concurred).

239 *National Grid Plc v Mayes* [2001] 1 WLR 854 at 873 per Lord Hoffman (with whom Lords Slynn, Lord Steyn, and Lord Scott concurred).


241 *Hockin v Bank of British Columbia* (1989) 36 BCLR (2d) 220 at 227 per Spencer J (also discussed in *Hockin v Bank of British Columbia* (1990) 71 DLR (4th) 11 at 18 per Carrothers JA (giving the judgment of the court (BCCA)).

242 *Hockin v Bank of British Columbia* (1990) 71 DLR (4th) 11 at 20 per Carrothers JA (giving the judgment of the BCCA).

243 *Hockin v Bank of British Columbia* (1990) 71 DLR (4th) 11 at 21 per Carrothers JA (giving the judgment of the BCCA).

244 *Hockin v Bank of British Columbia* (1990) 71 DLR (4th) 11 at 23 per Carrothers JA (giving the judgment of the BCCA).
ownership, in favour of the employer, to determine disputes as to actuarial surplus. For this reason, the decision was resoundingly rejected by the Supreme Court of Canada in Schmidt v Air Products of Canada Ltd. Cory J held that a pension trust is a "classic" or "true" trust and not a mere trust for a purpose. Consequently, the proposition accepted in Hockin, that once the benefits have been provided the purpose is fulfilled and the unexpended portion of the trust expires, was rejected. Quoting from a decision of the Pension Commission of Ontario, it was his Honour's view that:

...[t]he characterisation of pensions trusts as purpose trusts results in the pension text, a contract, taking precedence over the trust agreement. That is, it makes common law principles of contract paramount to the equitable principles of trust law. It is trite law that where common law and equity conflict, equity is to prevail. In light of that rule, it seems inappropriate to do indirectly that which could not be done directly.

To paraphrase Cory J's conclusion, prioritising the contract text and thereby importing de facto conceptions of contractual ownership cannot be achieved under the guise of interpretation and characterisation of the trust. As is also demonstrated in both Lock v Westpac and National Grid, the rights, interests, powers and duties of the stakeholders must be derived from the trust instrument. The substratum, purpose and parameters of a trust are defined not only by the relevant recitals but also any restrictions detailed in the words of the deed.

6.3.1.2 THE PERMANENT ALIENATION CLAUSE

A clause that prohibits the return of moneys of the fund or contributions to the employer is commonly termed a "permanent alienation" clause. The clause may be freestanding or expressed to limit amendments to that effect. In either case, an amendment that attempts to return moneys to the employer is prohibited.

248 Permanent alienation clauses expressed as a limitation on amendment were a particularly common feature of schemes in the United Kingdom during 1921 to 1970. During this period their inclusion was a prerequisite to obtaining scheme approval by the taxing authorities and so a prerequisite for concessional taxation treatment: Finance Act 1921 (UK) s 32 (now repealed); Income Tax Act 1952 (UK) s 375 (now repealed). See also National Grid Co plc v Mayes [2001] 1 WLR 864 at 870 per Lord Hoffman (HL); Arthur, Pensions and Trusteeship (Sweet & Maxwell, 1998), p 189.
A Purposive or Contractual Approach?

The courts have generally been critical of attempts to circumvent the permanent alienation restriction by methods such as categorising the contributions as prepayments or attempting to amend the amendment power itself to delete the prohibition.\(^9\) Given the nature of the prohibition, its interpretation has not been particularly susceptible to the influence of alternate contractual ownership notions. Yet, despite the proscriptive nature of a permanent alienation clause, Richardson J in \textit{Re UEB Industries Ltd Pension Plan}\(^5\) suggested in dissenting obiter comments that there may be substance to the proposition that the contractual nature of the employment relationship should over-ride the application of trust principles. Operating on the foundation that a defined benefit scheme is fundamentally a contract entered into by an employer for payment of defined benefits to members, his Honour suggested that any surplus upon termination results from over-funding and should be returned to the employer. On this view, a permanent alienation clause is inconsistent with the “contractual” nature of the bargain and it may be argued that the parties never intended a permanent alienation clause should extend to disposal upon termination. Therefore, Richardson J considered that on “a proper construction of the documents it may not be appropriate to override their intentions through invoking conventional trust principles”.\(^5\)

His Honour appears to have been interested in stimulating debate as he noted that these complex issues were not fully argued on appeal and he was not persuaded that the legal answer was so simple and obvious.\(^5\) His proposed arguments, nevertheless, suffer the same weakness as the argument proposed by Lord Browne-Wilkinson in respect of resulting trusts.\(^5\) Fundamentally, the relationship is one of trust, not contract, and the responsibility for the payment of benefits rests upon the trustee, not the employer. To this end, the intention of the parties is reposed in the trust documents and is not based upon sweeping notions of contract law.\(^5\) Even if the relationship could be categorised as one “fundamentally of contract”, the presence of a permanent alienation clause within

\(^{249}\) See, for example, \textit{Re UEB Industries Ltd Pension Plan} [1992] 1 NZLR 294 at 300-303 per Cooke P, at 308-309 per Thorp J (NZCA); \textit{Air Jamaica Ltd v Charlton} [1999] 1 WLR 1399 at 1411 (PC).
\(^{253}\) See 6.2.3.
\(^{254}\) See \textit{Re National Trust Co and Sulpetro Ltd} (1990) 66 DLR (4th) 271 at 277 per Bracco JA (giving the judgment of the AltaCA); \textit{Caboche v Ramsay} (1993) 119 ALR 215 at 232-233 per Gummow J.
a contract would on basic principles of interpretation negate the proposed argument. This dictates that Richardson J’s suggestion goes beyond accepted principles and is not a true reflection of intention. Instead, as indicated by Cooke P and Thorp J in the same case, the presence of a permanent alienation clause is fundamental to defining the substratum of the trust. The substratum is not premised upon vague notions of purpose or contractual ownership but is characterized by the terms of the actual trust instrument. Accordingly, in Re UEB a permanent alienation clause was held to invalidate an amendment that attempted to remove the permanent alienation restriction and a subsequent amendment that sought to refund surplus upon termination to the employer. It was held to be fundamental to the trusts that the “company’s contributions or moneys or investments to any extent representing them were never to be returned to the company”.

Releasing an Accrued Debt

Another issue that has arisen in respect of permanent alienation clauses is whether they prohibit amendment to utilise actuarial surplus for the purpose of releasing an accrued debt in favour of the employer. The House of Lords in National Grid Co plc v Mayes, adopting a purposive approach, held that a permanent alienation clause attaching to the amendment power did not prevent surplus being applied to release a debt. As the prohibition was included in the deed in order to obtain Inland Revenue approval, the purpose of Inland Revenue’s insistence on such a provision was relevant. According to the Lord Hoffman, as Inland Revenue approval generated taxation concessions for the employer in the form of tax deductions for contributions paid, “capital payments out of the fund to the employer were anathema to the revenue”. Thus, inclusion of the

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255 Re UEB Industries Ltd Pension Plan [1992] 1 NZLR 294 at 300-302 per Cooke P, at 308-309 per Thorp J (NZCA). See also Re Reevie and Montreal Trust Co of Canada (1986) 25 DLR (4th) 312 (OntCA) (where an amendment that replaced the members’ right to surplus upon termination with a clause that destined realised surplus to the employers was held invalid by reason that the trust deed stated that: (i) it was “impossible” for the trust fund “to be used for, or diverted to, purposes other than for the exclusive benefit of the employee members of the Plan or their beneficiaries” (at 314-315); and (ii) all contributions made by the company were irrevocable and were only to be used exclusively for the benefit of the members (at 314)); Air Jamaica Ltd v Charlton [1999] 1 WLR 1399 (where an amendment that proposed to return surplus upon termination to the employer was, in part by reason of the existence of a permanent alienation clause, held to be “incurably” bad: at 1411 (PC)); Harwood-Smart v Caws [2000] PLR 101 at [21]-[22] per Rimer J (EWHC).

256 Re UEB Industries Ltd Pension Plan [1992] 1 NZLR 294 at 300 per Cooke P (see also at 309 per Thorp J (NZCA)).


258 National Grid Co plc v Mayes [2001] 1 WLR 864 at 870 per Lord Hoffman (with whom Lords Clyde and Scott concurred).
prohibition was required so as to ensure that the employer did not direct payments to the fund, either temporarily or permanently, for the purposes of sheltering money from taxation. Given this, the prohibition was directed at capital payments to employers. As the debts that had fallen due were not deductible until paid, they were not caught within the amendment prohibition.\footnote{National Grid Co plc v Mayes [2001] 1 WLR 864 at 870 per Lord Hoffman (with whom Lords Clyde and Scott concurred). The case of British Coal Corp v British Coal Staff Superannuation Scheme Trustees Ltd [1995] 1 All ER 912 was expressly overruled on this point. In this case the terms of the trust deed prohibited any amendment that made any moneys of the scheme payable to the employer. The employer had previously agreed to fund the cost of enhanced benefits and a liability had arisen in the scheme in this respect. Because the liability had already accrued, Vinelott J held that any application of the surplus to reduce or release this liability constituted a payment to the employer and thus contravened the scheme (at 922-923). For further discussion of these cases see Fenton, “Electricity Supply Pension Scheme: International Power plc (formerly National Power plc) v Healy & Others; National Grid plc v Mayes”, presented at Association of Pension Lawyers Spring Conference, May 2001, Association of Pension Lawyers (see www.apl.org.uk); Pollard, “Pensions Law and Surpluses: A Fair Balance between Employer and Members?” (2003) 17 TLI 2 at 17-18.}

Importantly, the purposive approach was not utilised on the pretext of implementing contractual notions of ownership. Rather, the court was concerned to discover the intention reposed in the specific words of the trust deed, namely whether the word “payment” was limited to an actual exchange of money or also encompassed the release of debts.

6.3.1.3 Protection of Members’ Interests and Benefits

A prohibition on amending in a manner that will adversely affect members’ benefits may take different forms, the most prevalent being one against reducing or adversely affecting: (i) benefits secured by contributions; (ii) accrued benefits; or (iii) the interests of the members in the fund. In Australia and the United Kingdom statute also prohibits an amendment that adversely affects accrued benefits.\footnote{See 6.3.2.}

These three forms of limitations have been interpreted to afford different degrees of protection for members. The words “benefits secured” extend to all benefits conferred by the trust deed, including present or future, contingent or expectant.\footnote{James Miller Holdings Ltd v JD Graham (1978) 3 ACLR 604 at 617-618 per McGarvie J; Wilson v Metro Goldwyn Mayer (1980) 18 NSWLR 730 at 736 per Kearney J; Gas and Fuel Corporation of Victoria v Fitzmaurice (1991) 22 ATR 10 at 25 per Hedigan J; Asea Brown Boveri Superannuation Fund No 1 Pty Ltd v Asea Brown Boveri Pty Ltd [1999] 1 VR 144 at 158 per Beach J; BHLSPF Pty Ltd v Brasbs Pty Ltd [2001] VSC 512 at [50]-[43] per Warren J.}

For example, in BHLSPF Pty Ltd v Brasbs Pty Ltd\footnote{[2001] VSC 512.} an amendment power was subject to the proviso that no amendment would detract from the benefits secured to a member by
the contributions paid prior to the date of the amendment. A purported amendment sought to remove the members' rights to both augmentation of benefits and receipt of surplus upon termination. As it detracted from a future contingent benefit—a "benefit secured"—it was held to be void.*63

The words "interest in the fund" have been similarly interpreted to include future contingent benefits, such as the prospect of participating in a surplus distribution upon termination.*64 By way of comparison, the term "accrued benefits" has attracted a more restrictive interpretation. Use of the word "accrued" limits the type of benefits relevant to the restriction. The term is essentially an actuarial one, and has been held to refer to benefits that members become entitled to by virtue of their years of service and salary at the time of the amendment.*65 On this basis, future and contingent rights, such as to surplus upon termination, are not captured by the term.*66

In respect of interpretation, the decisions have turned upon the specific wording used and the nature of the interest conferred by the trust deed. In addition, specifically in relation to the phrases "benefits secured" and "interest in the fund", the courts have favoured a purposive approach. For example, in Cullen v Pension Holdings Ltd*67 the purpose of the fund, as defined by the specific extent to which benefits were conferred on members, was relevant to determining of the meaning of "interest". As the deed in question contemplated that only members could benefit from the fund and members' rights of participation were not limited to defined benefits, it was held that any attempt

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263 BHLSP Pty Ltd v Brashe's Pty Ltd [2001] VSC 512 at [30]-[43] per Warren J.
265 Hockin v Bank of British Columbia (1990) 71 DLR (4th) 11 at 21 per Carrothers JA (giving the judgment of the court (BCCA)) (overruled in Schmidt v Air Products of Canada Ltd [1994] 115 DLR (4th) 631 but on a different point); Lock v Westpac Banking Corporation (1991) 25 NSWLR 593 at 606 per Waddell CJ; CASAW Local 1 v Alcan Smelters and Chemicals Ltd (2001) 198 DLR (4th) 504 at 509-517 per Levine JA (giving the judgment of the BCCA). See also Board of Management of the Bank of New Zealand Officers' Provident Association v McDonald [2002] PLR 501 (NZCA) where the relevant trust deed permitted amendment provided the amendment did not adversely affect any member's or pensioner's interest in the fund already accrued at the date of variation. Although not strictly an "accrued benefits" case, given the occurrence of the word "accrued" after "interest" the court interpreted the words on a similar basis.
267 (1993) 1 NZSC ¶30-534.
to remove an interest in the augmentation of benefits, or an interest in participation in any surplus in the fund on termination, adversely affected their interest in the fund.

Similarly, and in a more general sense, where the whole purpose of an amendment limitation is to protect the interests of the beneficiaries, any ambiguity or doubt as to the extent of the limitation has been construed in favour of protecting and preserving their position. Contractual notions of ownership or the background of the employment relationship have not influenced interpretation in this respect. Again the focus of the court has been the trust instrument and the intent reposed therein.

6.3.1.4 SYNTHESIS: GENERAL PRINCIPLES OF AMENDMENT

A consistent theme in the interpretation of amendment powers has been the use of purposive approach. However, as demonstrated in the above discussion, the purposive approach is not a guise for the implementation of contractual notions of ownership through the principles of interpretation applicable to trusts. Instead, it is one that looks to the specifics of the trust instrument. In this regard the prohibition against altering the main purpose of the fund or substratum of the trust is not be tested by reference to generalised contractual notions of ownership in favour of employees. It is true to state that superannuation and pension funds are held generally for the benefit of employees. But the extent of that holding and the precise substratum of a trust will be defined by reference to the specific provisions within the trust, as it is these provisions that reveal the intent of the settlor. Similarly, in the context of permanent alienation clauses, the employment contract will not be interpreted to override the provisions of the trust instrument in favour of the employer. Instead, the existence of the clause is fundamental to defining the substratum of the trust.

Another dimension to the purposive approach is its application in the interpretation of specific provisions and words. In this context the courts have again eschewed generalised notions of contractual ownership. Instead, their focus has been upon the specifics of the provisions and the direct purpose for their inclusion in the deed. Thus, the intention of the legislature in imposing a permanent alienation clause is relevant to

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its meaning. The protective nature of prohibiting amendment that adversely affects benefits is also relevant to interpretation.

Perhaps what is most revealing is that in each instance it was open to the judiciary to taper their judgments in favour of a contract-based approach and adopt a policy approach favouring either employers or employees. However, consistent with general trust principles of interpretation – which in turn is consistent with the first limb of the SRF – the courts have prioritised the trust instrument as the repository of settlor intent.

6.3.2 STATUTORY INITIATIVES

Each jurisdiction canvassed in this thesis imposes statutory restrictions upon the amendment of the trust instrument. As the concept of freedom of trust permits the settlor (in superannuation trusts, often the employer) to define the terms of the trust, any statutory restriction constricts that freedom. The restrictions are detailed in Chapters 2 and 3. Briefly, the least restrictive is Hong Kong, where approval of the regulator is required before the amendment takes effect. The remaining jurisdictions limit amendment that adversely affects or alters members’ rights to benefits, the form of which varies between jurisdictions. In Australia the restriction relates to accrued benefits, whereas in the United Kingdom an actuary must certify that the amendment does not adversely affect entitlements or accrued benefits. The scope of the restrictions in Ontario and New Zealand is broader. In Ontario the restriction refers to an amendment that reduces the amount of prescribed benefits and accrued benefits, or adversely affects rights or obligations of members, former members or any person entitled to a benefit. In New Zealand the proposed amendment must not adversely affect benefits, remove the right of members to participate, increase contributions, fees or charges, or provide for further reversion of assets to the employer. Excepting Ontario, in each of these remaining jurisdictions an amendment that falls within the scope of the restriction is permitted if the written consent of the relevant beneficiaries is first obtained. In Ontario, any

270 See 2.3.2 (Australia), 3.1.3 (United Kingdom), 3.2.3 (Ontario), 3.3.3 (New Zealand), 3.4.3 (Hong Kong).
271 Mandatory Provident Fund Schemes (General) Regulation 1998 (Cap 485A) (HK) reg 63(1), 63(2).
272 SIS Act, s 31; SIS Regulations, reg 13.16.
275 Superannuation Schemes Act 1989 (NZ) s 9.
276 See 2.3.2 (Australia), 3.1.3 (United Kingdom), 3.3.3 (New Zealand).
amendment that purports to reduce the prescribed or accrued benefits is void,\textsuperscript{277} whereas an amendment that adversely affects either the amount of accrued benefits subsequent to amendment, or the rights or obligations of members, will be permitted where the prescribed requirements as to member and beneficiary notification have been fulfilled.\textsuperscript{278}

Although these statutory restrictions circumvent the settlor’s freedom, they are clearly justified, if not necessitated, under the SRF. An historical concern of utilising the trust was its flexibility and the absolute freedom of the settlor in framing its parameters.\textsuperscript{279} It follows that at general law an amendment power could be drafted so as to permit the reduction of benefits or entitlements. Here the flexibility of the trust vehicle could negate its protective qualities. To permit unregulated freedom exposes members and beneficiaries to prudential risk. To this end, the protective limb of the SRF justifies the restriction of general principles. The further question that arises is the appropriate extent of the protection. On the basis of the authorities cited above\textsuperscript{280} the Australian and United Kingdom provisions do not protect future contingent benefits or entitlements, only those benefits that had accrued at the date of amendment.\textsuperscript{281} The broader phrases used in Ontario and New Zealand protect mere expectancies, such as surplus and the augmentation of benefits. At a minimum level core benefits must be protected and this is achieved in all jurisdictions except Hong Kong. However, to go further and protect \textit{all} future rights and entitlements may unduly restrict the operation of the scheme. The Goode Committee in the United Kingdom argued against such further protection on the basis that:\textsuperscript{282}

\begin{quote}
It would be unreasonable to allow the employer to procure changes to the pension scheme for future service. To insist that the terms on which the pension rights accrued did not change (and that in consequence the scheme could not be wound up) for any employee who was a member of the scheme at the point of change would make pension provision extremely inflexible. Pension schemes are established by the voluntary act of the employer, who should equally be free to stop providing pensions, or to change the way in which they are provided. Locking employers in to a single pattern of provision would be a major disincentive to their making any provision at all. The employer’s ability to procure such changes would, of course, be subject to the scheme rules, employment law and the contract of employment.
\end{quote}

\textsuperscript{277} Pension Benefits Act RSO 1990, P8, s 14.
\textsuperscript{278} Pension Benefits Act RSO 1990, P8, s 26.
\textsuperscript{279} See the heading “Criticisms of the Trust” in 4.2.2.1.
\textsuperscript{280} See 6.3.1.3.
\textsuperscript{281} See also Barclays Bank plc v Holmes [2000] PLR 339 where Neuberger J held that the terms “entitlement” or “accrued benefits” do not include rights or entitlements to surplus (at [125]-[130]).
This reasoning is not so apposite in Australia, where employers are statutorily compelled to provide a prescribed minimum level of superannuation support for each employee.\(^3\) However, it arguably holds true in respect of any additional contributions made by employers over and above the prescribed statutory minimum. The extent of protection provided for benefits and entitlements must also be viewed against any other protections within a scheme of regulation. In Australia, where a power of amendment is vested in the employer the SIS Act requires that the trustee consent to that amendment,\(^4\) another additional layer of protection. The trustee, to exercise the power of consent, must determine that the amendment is, in all the circumstances, in the best interests of the beneficiaries.\(^5\) Viewed in this context, protection of benefits over and above "accrued benefits" is arguably not required. By way of comparison, in the United Kingdom this issue is not approached from the perspective of trustee consent, but the trustee must be satisfied that statutory requirement of obtaining the relevant actuarial opinion or consent of the members has been complied with.\(^6\) This, however, imports no requirement for the trustee to exercise judgment regarding the substance of the amendment and, in particular, whether or not it is in the best interests of the beneficiaries.

The apparently stricter protection in Ontario must be judged against the fact that the employer is most often the administrator of the scheme.\(^7\) In this case, there is no independent entity representing the interests of the employees having a mandate to act only in their interests. Consequently, greater constriction upon the power amendment may be required to counter the effects of the potential risk of this arrangement.

On the basis of prudential security each of these statutory restrictions can be justified. In fact, protection of accrued benefits is necessitated on the basis of the SRF. The extent of the protection required cannot be judged in isolation but must be considered against the backdrop of the other protective features of the regulatory scheme, as well as the political climate at the time of enactment and the degree of influence exercised by the relevant stakeholders at that time. An advantage of the Australian position, in requiring trustee

\(^3\) See 2.2.4.1.

\(^4\) SIS Act s 60. See also SIS Regulations reg 4.01 for the exceptions to this requirement for employer-sponsored funds.

\(^5\) See 6.5.

\(^6\) Pensions Act 1995 (UK) s 67(3)(b).

\(^7\) See 6.4.3.
consent, is that it invokes a key feature that goes to the heart of the protective attributes of the trust – that the trustee act in the best interests of the beneficiaries.

6.4 EMPLOYERS: THE EXERCISE OF POWERS AND DISCRETIONS

The special nature of the superannuation trust arises in part from the presence and influence of the employer in scheme operation. Unlike a traditional family trust, the trust instrument, particularly in the context of a defined benefit scheme, will often confer significant powers or discretions on the employer (as settlor). This vests significant control in the employer over scheme operation. Examples include the power to amend the scheme (or at the very least, a power to consent to any amendment), the power to augment benefits, and the power to wind up the scheme. The provisions of the trust instrument, in conjunction with any applicable general law principles, define the nature and scope of such powers and discretions. An important issue is whether an employer can unilaterally pursue its own interests without regard to those of the members and beneficiaries. This turns on whether the power or discretion is interpreted as being fiduciary or non-fiduciary.

6.4.1 FIDUCIARY POWERS AND DISCRETIONS

A power or discretion that is fiduciary in nature must be exercised in accordance with the twin fiduciary prohibitions: the employer must not place itself in a position of conflict vis-à-vis the employees or make a profit from its position. The nature of the duty expressly prohibits pursuit of individual interest. It is unusual for powers and discretions conferred upon employers to be characterised as fiduciary in nature. After all, a general objective in conferring powers is precisely so that, inter alia, the employer can further its own interests. This is particularly so in the context of a defined benefit fund where the employer is responsible for scheme solvency. Mettoy Pension Trustees Ltd v Evans 288 provides an example that goes against this general trend. There a power conferred upon an employer to use realised surplus to augment member benefits was held to be fiduciary in nature. Two considerations tipped the scale in favour of this conclusion. Most significantly, the discretion was otherwise illusory as any remainder upon termination vested in the

288 [1990] 1 WLR 1587 (EWHC).
employer. The words conferring the power would have meant no more than that the
employer was free to make gifts out of property of which it was the beneficial owner.\textsuperscript{289} Confirming this interpretation was the second factor: the beneficiaries were not volunteers
and their rights and contributions were earned by service in employment.\textsuperscript{290}

\subsection*{6.4.2 Non-fiduciary Powers and Discretions}

Although any power or discretion conferred upon an employer is commonly intended to be
non-fiduciary in nature, the conferral of even a very broad non-fiduciary power or
discretion is not unlimited in scope. The general law has held that such powers and
discretions are subject to the implied obligation of mutual trust and confidence.
Originating from the field of employment law, the application of this implied obligation in
the context of superannuation and pension trusts had its genesis in the seminal decision of
Sir Nicolas Browne-Wilkinson VC in \textit{Imperial Group Pension Trust Ltd v Imperial Tobacco
Ltd}.\textsuperscript{291} His Lordship held that the employer's power to grant or withhold consent to
amendment was not fiduciary in nature and nor was it necessary to engraft an implied
limitation of reasonableness on the employer's right to refuse consent.\textsuperscript{292} However, the
power was limited by an implied obligation of good faith. Focusing on the special nature of
pension trusts, his Lordship described the obligation and its source in the following
terms:\textsuperscript{293}

\begin{quote}
Pension benefits are part of the consideration which an employee receives in return for the
rendering of his services. In many cases, including the present, membership of the pension
scheme is a requirement of employment. In contributory schemes, such as this, the
employee is himself bound to pay his or her contributions. Beneficiaries of the scheme, the
members, far from being volunteers give valuable consideration. The company employer is
not conferring a bounty. In my judgment, the scheme is established against the background
of such employment and falls to be interpreted against that background. In every contract
of employment there is an implied term-

that the employers will not, without reasonable and proper cause, conduct themselves in a
manner calculated or likely to destroy or seriously damage the relationship of confidence and
trust between employer and employee...

...I will call this implied term 'the implied obligation of good faith'. In my judgment, that
obligation of an employer applies as much to the exercise of his rights and powers under a
pension scheme as they do to the other rights and powers of an employer.
\end{quote}

\textsuperscript{289} \textit{Metloy Pension Trustees Ltd v Evans} [1990] 1 WLR 1587 at 1614-15 per Warner J.
\textsuperscript{290} \textit{Metloy Pension Trustees Ltd v Evans} [1990] 1 WLR 1587 at 1614 per Warner J.
\textsuperscript{291} \cite{ImperialGroupPensionTrustLtdvImperialTobaccoLtd1991} 2 All ER 597 (EWHC).
\textsuperscript{292} \textit{Imperial Group Pension Trust Ltd v Imperial Tobacco Ltd} [1991] 2 All ER 597 at 605.
\textsuperscript{293} \textit{Imperial Group Pension Trust Ltd v Imperial Tobacco Ltd} [1991] 2 All ER 597 at 605-606 (paragraph
break omitted).
Most significantly, as a result of Browne-Wilkinson VC's decision, a claim for breach of the good faith obligation arises not only in contract but also in trust—"the pension trust deed and rules themselves are to be taken as being impliedly subject to the limitation". Accordingly, an obligation that arises in the employment contract operates to modify the powers and discretions conferred by the trust instrument. This represents a striking example of the direct influence of the contract of employment which ultimately promotes principles of contract law over equitable principles of trust law.

6.4.2.1 THE IMPLIED OBLIGATION OF GOOD FAITH—MEANING AND SCOPE

The House of Lords has confirmed that the implied term of mutual trust and confidence is implied by law as an incident of all contracts of employment. Being implied in law, it operates as a default rule and can be excluded or modified by the parties. Lord Steyn described its origin as flowing from the general duty of cooperation between contracting parties and, although a "mutual" obligation, "the major importance of the implied duty of trust and confidence lies in its impact on the obligation of the employer". Following the Imperial Tobacco case the application of the implied term to superannuation and pension trusts has been accepted throughout the common law world. In Australia, although accepted at a Supreme Court and Federal Court level, the issue has not arisen for determination by the High Court. However, given that the obligation is firmly entrenched in English jurisprudence with recognition

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294 Imperial Group Pension Trust Ltd v Imperial Tobacco Ltd [1991] 2 All ER 597 at 606.
296 Malik v Bank of Credit and Commerce International SA (in liq) [1997] 3 All ER 1 at 5 per Lord Steyn.
by the House of Lords and Privy Council, there is little reason to doubt that it would not be similarly accepted by the Australian High Court.

The substance of the obligation, as traditionally cited, is that:

The employer shall not without reasonable and proper cause, conduct itself in a manner calculated and likely to destroy or seriously damage the relationship of confidence and trust between employer and employee.

Although implication of the duty has been described as a sound development of the law, the substance and practical scope of the duty is nebulous. This is not surprising given that the obligation is "formulated to cover the great diversity of situations in which a balance has to be struck between an employer's interest in managing his business as he sees fit and the employee's interest in not being unfairly and improperly exploited". What is clear is that it is not to be equated with a standard of reasonableness. Nor is it to be presumed to be fiduciary in character, even though the phrase "mutual trust and confidence" conjures up fiduciary-like notions. The duty is an objective one and the impugned conduct need not be directed specifically at an employee in order to destroy or seriously damage the relationship of trust and confidence, nor is it necessary that the employee be aware of the conduct whilst an employee.

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299 Imperial Group Pension Trust Ltd v Imperial Tobacco Ltd [1991] 2 All ER 597 at 606 per Browne-Wilkinson VC. See also Malik v Bank of Credit and Commerce International SA (in liquidation) [1997] 3 All ER 1 at 5 per Lord Nicholls, at 15 per Lord Steyn.

300 For a discussion of the various possible meanings of the implied duty of good faith see Peden, Good Faith in the Performance of Contracts (LexisNexis Butterworths, 2003), Ch 7.

301 Malik v Bank of Credit and Commerce International SA (in liquidation) [1997] 3 All ER 1 at 15-16 per Lord Steyn.

302 Imperial Group Pension Trust Ltd v Imperial Tobacco Ltd [1991] 2 All ER 597 at 607 per Browne-Wilkinson VC. His Lordship could see no need to engraft an implied limitation of reasonableness but rather "good reasons why such limitation should not be implied" (at 609). Given that the employer (in the case of a defined benefit scheme) has a direct personal interest in how the scheme is to operate, what is reasonable from the point of view of the employer may be unreasonable viewed through the eyes of the members. The court would therefore be required to choose a particular view or "seek to balance the reasonableness of both viewpoints". This would be, in Browne-Wilkinson VC's view, an unworkable situation.

303 Imperial Group Pension Trust Ltd v Imperial Tobacco Ltd [1991] 2 All ER 597 at 607 per Browne-Wilkinson VC; National Grid Co plc v Lates [1997] PLR 157 at [87]-[92] per Walker J (affd on different grounds National Grid Co plc v Mayes [2001] 1 WLR 864 (HL)). Although the duty of mutual trust and confidence is not of a fiduciary character, the employer's obligation may be so interpreted if it exhibits the requisite fiduciary characteristics. See, for example, the discussion of Mettrey Pension Trustees Ltd v Evans [1990] 1 WLR 1587 at 6-4.1.

304 Malik v Bank of Credit and Commerce International SA (in liquidation) [1997] 3 All ER 1 at 5 per Lord Nicholls, at 16-17 per Lord Steyn.
Pollard describes the implied obligation of good faith as operating at two levels: as a free standing obligation, and as a limit or fetter on an express power.\textsuperscript{305} In relation to superannuation trusts, the main impact of the obligation has been the latter—to limit the express power of the employer.\textsuperscript{306} In this context, three main themes emerge from the relevant cases, which themes shed light on the underlying scope of the duty.

(i) \textit{Collateral and Improper Purposes}

The first theme is that breach of the duty will occur if an employer exercises a power for a collateral or improper purpose. This is evident from the \textit{Imperial Tobacco} case. It concerned a contributory defined benefit scheme where the employer was responsible for the solvency of the fund—a typical balance of cost scheme. Two corporate trustees and a committee of management ("committee") managed the scheme, its rules setting out the benefits to which members were entitled. Although there was no express provision for augmenting such benefits, in practice pensions were increased in line with the retail price index ("RPI"). The trust deed permitted amendment by the committee with consent of the company provided that the amendment did not, inter alia, alter the main purposes of the fund, result in any return of the fund to the company, or substantially prejudice the rights or interests of any existing member. In the wake of a takeover bid, the company and the committee amended the trust instrument to automatically close the fund in the event of a takeover and to institute a mandatory annual increase in pensions by at least the lesser of 5 per cent or the RPI percentage increase. The takeover was ultimately successful and, in accordance with the previous amendment, the fund was automatically closed. At this point the fund was some £130 million in surplus, with the employer already taking a contribution holiday. The new employer sought to reopen the fund and, in negotiations, the committee sought an assurance from the company that it would adhere to the previous practice of increasing pensions in line with the RPI. The company refused to give such an assurance, stating that it would not in any circumstances agree to further increases other than the minimum guaranteed by the fund (as per the previous amendment).

Negotiations then broke down and the company inaugurated a new scheme for new employees where annual benefits improvements were guaranteed to be the lesser of 15%
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or the percentage increase in the RPI. The company proposed that employees from the old scheme transfer to the new scheme taking with them an aliquot share of the fund, including each member’s share in the surplus. Thus, if 100% of members accepted the proposal the entire fund, including surplus, would be transferred. However, one significant difference between the schemes was that under the initial scheme any surplus upon termination was applied for the benefit of members, whereas in the new scheme it vested in the company. Following member concerns to this end, the committee sought directions from the court on whether any constraints attached to the employer’s power to grant or withhold consent to amendment. Browne-Wilkinson VC held that the power of consent was subject to an implied duty of good faith, which required the company to exercise its rights with a view to the efficient running of the scheme, and not for the collateral purpose of forcing members to give up their accrued rights in the existing fund.307 Indeed, in respect of the latter his Lordship stated:308

The duty of good faith required the company to preserve its employees’ rights and pension fund, not destroy them. If there are financial and other considerations which require the fund to be determined, so be it. But if the sole purpose of refusing to consent to an amendment increasing benefits is the collateral purpose of putting pressure on members to abandon their existing rights (including the right to the surplus on determination) in my judgment the company would not be acting in good faith.

As the case concerned an emergency application, the facts were not fully explored and the court was not called upon to affirmatively decide whether or not the employer had breached its duty of good faith. Notwithstanding this, the facts taken in conjunction with Browne-Wilkinson VC’s comments give insight to the relevant types of offending conduct. Most particularly, the exercise of a power for a collateral purpose is invalidating conduct.

Walker J in the National Grid case also described the duty as one that prohibits the exercise of powers for a collateral and improper purpose. However, although similar in this respect to a fiduciary power, his Lordship identified the one essential difference as being that “the Imperial Tobacco duty does not prevent the employer from looking after its own financial interests, even where they conflict with those of members and pensioners”.309 For example, in Buschau v Rogers Cable systems Inc310 the absence of a

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307 Imperial Group Pension Trust Ltd v Imperial Tobacco Ltd [1991] 2 All ER 597 at 607.
308 Imperial Group Pension Trust Ltd v Imperial Tobacco Ltd [1991] 2 All ER 597 at 607.
collateral purpose in an employer decision *not* to exercise a power to increase member benefits served to validate the employer's conduct. The fund was in substantial surplus and the actuary recommended that the employer augment member benefits. Acting against that advice, the employer elected to take a contribution holiday rather than to increase member benefits. Distinguishing *Imperial Tobacco*, Lowry J held there was no evidence of a collateral purpose in the employer to destroy the plan or gain something to which it was not entitled. As such, the employer was merely exercising a discretion, as it was so entitled pursuant to the trust instrument.311

(ii) Compelling a Consideration

The second theme also has its genesis in the *Imperial Tobacco* case, where Browne-Wilkinson VC said that the implied duty of good faith requires the employer to exercise its rights "with a view to the efficient running of the scheme".312 According to his Lordship, where the power to withhold or grant consent to amendment is vested in the employer, this requires that the employer consider proposals each time they are made. This in turn prevents the employer from adopting a stand whereby amendments are never considered, which would be an improper use of the power and may be seen to undermine the employees' trust in their employer. Thus, the implied duty may serve to compel an employer to consider the exercise of a discretion or power.313


312 *Imperial Group Pension Trust Ltd v Imperial Tobacco Ltd* [1991] 2 All ER 597 at 607.

313 See also *Milbentstedt v Barclays Bank International Ltd* [1989] PLR 91 (EWCA), where it was held that the implied duty of trust and confidence required an employer Bank to give consideration to a member's application for a disability pension. In this context Nourse LJ stated that (at [15]):

> [i]f the matter had rested on the trust deed and the rules alone, I would have held that the Bank was under no obligation in regard to the plaintiff's application for an ill health pension. But it was a term of her contract of employment with the Bank that she should be entitled to membership of the pension scheme and to the benefits thereunder. Under that it must follow, as a matter of necessary implication, that the Bank became contractually bound, so far as it law within its power, to procure for the plaintiff the benefits to which she was entitled under the scheme.

Nicholls LJ came to the same conclusion but did not think that it was necessary to pursue the points of trust law (at [78]). There are two important aspects to note regarding this decision. First, although the implied duty operated vis-à-vis the employer's power within the trust deed, the remedy granted was contractual as the obligation was not seen, at the time of the decision, as being imported into the terms of the trust instrument. Secondly, the employer was also the trustee of the fund. Although the trust deed clearly identified the relevant discretion as one conferred upon the employer, as opposed to the trustee, Nourse LJ gained assistance from the analogous situation of a trustee who is required to form an opinion under the terms of the trust. Thus, Nourse LJ's view seems to be that the employer was required to exercise the discretion as a quasi-trustee. Interestingly, counsel's suggestion that the plaintiff's right was analogous to the administrative law concept of "legitimate expectations" was discounted as being "unnecessary and undesirable" (at [17]).
(iii) Legitimate and Reasonable Expectations

The final theme revolves around the concept of protecting the legitimate and reasonable expectations of the members. The implied duty is said to restrain a unilateral pursuit of the employer's own interests without proper regard to those of the members. In essence it prevents an employer exercising a discretion without regard to the employees' "expectations". Knox J in LRT Pension Fund Trustee Company Ltd v Hatt described the relevant expectations in the following terms:

There are expectations which members might quite legitimately harbour that discretions will be exercised in their favour where no such breach of a duty of good faith by the employer or abuse of a fiduciary power is involved in the non exercise of the discretion. Typically this situation arises where there is a surplus discerned by the actuary to the fund and one possibility is for pensions to be increased. No doubt the larger the surplus the livelier the expectation but in the great majority of pension funds it remains an expectation rather than a right. This is not to say that it is either without value or that the law will not protect it in appropriate circumstances.

It is clear that an attempt to remove an existing expectation, such as a power in the deed to augment member benefits, is inconsistent with the implied duty. Indeed, this would also be the case pursuant to the "collateral purpose" theme discussed above. However, the legitimate expectations concept appears to go further and also prevent an employer, despite the terms of the trust instrument, from benefitting itself without first satisfying members' legitimate expectations. This Knox J contemplated in the LRT case in his description of the various rights and interests of members. His Lordship identified the right "which is correlative to the duty of an employer to observe the implied term in contracts of employment that the employer will not act in breach of the implied obligation of good faith" as second only to the right to receive benefits. Most significantly he then stated that:

This right of employees is therefore capable of securing to them as members of a pension scheme benefits over and above what the current rules of the scheme taken by themselves provide as their lawful entitlements.

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314 LRT Pension Fund Trustee Company Ltd v Hatt [1993] PLR 227 (EWHC); Hillsdown Holdings plc v Pensions Ombudsman [1997] 1 All ER 862 at 890 per Knox J (EWHC).
316 See Air Jamaica Ltd v Charlton [1999] 1 WLR 1399 (PC), where the employer sought by amendment to remove the members' right to have surplus upon termination applied to provide additional member benefits, and by subsequent amendment to include a provision that enabled the surplus to be paid to the company. The Privy Council held that the amendments were incurably bad because, inter alia, the obligation of good faith precluded the company from disregard or overriding the interests of the members (at 1411 per Lord Millett).
317 LRT Pension Fund Trustee Company Ltd v Hatt [1993] PLR 227 at [158] per Knox J.
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Two examples serve to illustrate the possible application of the implied duty of good faith to secure "benefits over and above what the current rules of the scheme" provide. The first arises from the comments of Knox J in *Hillsdown Holdings plc v Pensions Ombudsman*.39 His Lordship suggested that introducing new employers, and therefore members, into a scheme whilst the principal employer was on a contribution holiday is a breach of the implied duty. This was so even when an employer had the express power under the deed to suspend or determine its contributions. Apparently, "it is one thing for an employer to take a contribution holiday in respect of a category of existing members and quite another to introduce a large class of new members and take a contribution holiday in relation to them so as to accelerate the effect of the contribution holiday in relation to the existing members".320 Given the courts' general refusal to ascribe ownership in an actuarial surplus and therefore allow contribution holidays if so permitted by the trust deed, the only explanation for this suggestion is that there was some expectation in the members that the surplus would be held for their benefit. It followed that the surplus could not be used in respect of contributions for new members or for the benefit of the employer in reducing its contributions.

The second example arises from the discussion of Vinelott J in *British Coal Corp v British Coal Staff Superannuation Scheme Trustees Ltd*.321 In the context of exercising a power of amendment, his Lordship described the employer's duty as follows:322

The employer, if he has a power of amendment, is entitled to exercise it in any way which will further the purpose of the pension scheme to ensure that the legitimate expectation of the members and pensions are met without, so far as possible, imposing any undue burden on the employer or building up an unnecessarily large surplus...If the assets are so large that all legitimate expectations of the members and pensioners can be met without continued contribution by him at the rate originally provided, he can by amendment reduce or suspend contributions for a period.

On this basis, to amend without satisfying members' legitimate expectations would constitute a breach of the implied duty of mutual trust and confidence. Nolan is similarly of the view that where the implied obligation of good faith is applicable "it means that even if beneficiaries have no legal right to participate in surpluses under a

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319 [1997] 1 All ER 862 (EWHC).
320 *Hillsdown Holdings plc v Pensions Ombudsman* [1997] 1 All ER 862 at 890.
321 [1995] 1 All ER 912 (EWHC).
322 *British Coal Corp v British Coal Staff Superannuation Scheme Trustees Ltd* [1995] 1 All ER 912 at 926.
fund's rules while the fund continues they are entitled to have surpluses dealt with by consultation and negotiation".\textsuperscript{333}

This concept extends the scope of the implied duty much further than that of "collateral purpose". Nolan aptly summarises the consequences of adopting such a wide scope as follows:\textsuperscript{334}

...the obligation of good faith can confer on fund beneficiaries a right to, or expectation of sharing in, surpluses which they would not otherwise have. It is widely accepted that where the principle is applicable it will, save perhaps in very exceptional circumstances, as a practical matter usually compel an employer who wishes to undertake a surplus repatriation to share the surplus with fund beneficiaries, whether by way of cash payment to beneficiaries, benefit improvements and/or member contribution holidays. In this regard, it should be noted that the employer-sponsor's right to exhaust even an entire surplus by taking a "contribution holiday"...is not sufficient to displace this rule of thumb. Nor, it seems, does the fact that the fund already provides comparatively generous benefits, although this is relevant to the quantum which it is "fair" or "reasonable" to receive.

**6.4.2.2 ANALYSIS – SRF AND THE IMPLIED OBLIGATION OF GOOD FAITH**

The framing of a trust instrument is based upon the fundamental concept of freedom of trust. The settlor is free to settle the trust on whatever terms he or she thinks fit subject only to the qualification that the irreducible core of obligations fundamental to the concept of a trust must be maintained.\textsuperscript{335} The implied term of good faith fetters that freedom. Clear words that confer a broad discretion or power are limited by the employer's contractual obligation of mutual trust and confidence. That contractual obligations operate to directly modify the terms of the trust instrument turns the usual priority of principles on their head and represents a departure from ordinary trust principle.

In the context of the SRF, this departure is arguably justified on the basis of the prudential security limb. As defined in Chapter 4,\textsuperscript{336} the essence of prudential security is the minimisation of risk. The risk inherent in the conferral of power upon the employer is that the employer's interests are not aligned with those of the members, whose interests may be subjugated to those of the employer. The implied obligation of good


\textsuperscript{335} Anmitage v Nurse [1997] 3 WLR 1046 at 1056 per Millett LJ. In this case Millett LJ considered that the "irreducible core" obligation of the trust was the "duty of the trustees to perform the trust honestly and in good faith for the benefit of the beneficiaries": at 1056.

\textsuperscript{336} See 4.4.
faith mitigates against this type of risk by limiting the scope of any power conferred upon employers. This is not to say that the employer must act in the interests of the members but that the ability to entirely pursue its own interests is confined. This is evident from Lord Steyn's identification of the purpose of the implied obligation as one that seeks to balance "an employer's interest in managing his business as he sees fit and the employee's interest in not being unfairly and improperly exploited". Viewed in this light the objective of the good faith duty is protective in nature. It protects against the removal of existing rights or expectations and prevents the employer from exercising the powers conferred for a collateral purpose. Moreover, it seeks to ensure that the scheme will not be held to ransom by an employer refusing to give consideration to the possible exercise of powers. For these purposes an implied obligation of good faith can be entirely justified to limit the settlor's dispositive freedom.

It is more difficult to justify the expanded scope of the doctrine in relation to legitimate expectations. The scope of the obligation envisaged by Knox J in the LRT case can be interpreted to transform a mere expectation, say in relation to surplus, into something closer to a right. Nolan contemplates that it may extend so far as to create an expectation where none previously existed. Application of the legitimate expectations concept in the superannuation arena had its origin in Stanhard v Fisons Pension Trust Ltd, where Straughton LJ considered that employees have a legitimate expectation that surplus will result to them or be used for their benefit in the future. His Lordship considered that a trustee should bear this mind when apportioning the fund to effect a transfer. This line of reasoning was subsequently taken up by Nicholls VC in Thrells Ltd v Lomas, who was called upon to exercise the relevant trustees' discretion in a winding up of a defined benefit fund. The trust instrument in issue empowered the trustee, in the event of a realised surplus, to augment members' benefits, any balance remaining thereafter vesting in the company. According to his Lordship, this meant that


330 Stanhard v Fisons Pension Trust Ltd [1991] PLR 225 at [47]. This point of reasoning was not taken up by the other members of the Court of Appeal (Dillon and Ralph Gibson LJ).

331 Stanhard v Fisons Pension Trust Ltd [1991] PLR 225 at [50].

the members had a *reasonable expectation* that if the fund was in surplus "the trustee [would] exercise that power to the extent that [was] fair and equitable in all the circumstances".333

The importation of the administrative law doctrine of legitimate expectations in this context has been the subject of judicial criticism.334 Yet regardless of its legitimacy or otherwise, there is one stark distinction between the circumstances in both *Stannard* and *Thrells* and the application of the concept to the employer's role. *Stannard* and *Thrells* concerned the exercise of discretion by the trustee, not the employer. Trustees are required to act in the best interests of the members. This is the very essence of their role. Therefore, where a power is vested in the trustee, it may well be reasonable or legitimate that the members expect the trustee to utilise that power for their benefit. The same cannot be said where the power is vested in the employer; the very purpose of so vesting is to permit the employer to pursue its own interests subject to not using the power for improper purposes, to undermine the scheme or to remove the actual rights of the beneficiaries.

To the extent that the "legitimate expectations" concept prevents an employer from exercising a discretion in its interests (as contemplated by the trust instrument) without first satisfying members' expectations, it falls outside of the parameters of the SRF. Protection of the scheme and the rights and interests therein validates a departure from traditional trust principle. It will not pray in aid of transforming a mere expectancy into something closer to a right. The extended scope of the implied obligation of good faith is grounded in the concept that members have "paid" for their benefits. Where a deed, in addition to the provision of pension benefits, contemplates that members may share in surplus, all that has been "bought" is an expectation, a mere hope. Ironically, to widen the scope of the obligation to encompass "legitimate expectations" is also problematic on a pure contractual analysis, as it can grant more to members than what has been bargained for.335 In a trust context, application of the "legitimate expectation" doctrine

333 *Thrells Ltd v Lomas* [1993] 1 WLR 456 at 468-469 (EWHC).

334 See *Milbenstedt v Barclays Bank International Ltd* [1989] PLR 91 (EWCA) where counsel's suggestion that the plaintiff's rights were analogous to the administrative law concept of "legitimate expectations" was discounted as being "unnecessary and undesirable" (at [17]). Moreover, Lord Millett has stated extra-curially that he is "not convinced that this public law import is itself legitimate"; Lord Millett, "Pension Schemes and the Law of Trusts: The Tail Wagging the Dog?" (2000) 84 Pension Lawyer 1 at 5.

335 On this point McLachlin J in *Schmidt v Air Products of Canada Ltd* [1994] 115 DLR (4th) 631 at 693 has argued that:

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smells strongly of an attempt to import notions of contractual ownership – another means of bringing through the back door what has been firmly closed off at the front.336

6.4.2.3 A PREFERRED APPROACH?

Although an implied term of good faith can, apart from the extended scope of "legitimate expectation", be justified on the basis of the SRF, a preferable approach is to eschew notions of contract law in favour of an approach based on equitable doctrine. There is arguably no need to resort to an implied contractual duty to limit the power of the employer; resort may be had to a broad application of the equitable doctrine of fraud on a power.

The fraud on a power doctrine requires that a power must not be exercised for a purpose, or with an intention beyond the scope of, or not justified by, the instrument creating the power.337 The power must be exercised for the purpose for which it was conferred. That the term fraud does not necessarily denote conduct of a dishonest or immoral nature is evident from the words of Lord Westbury:

[T]he settled principles of the law upon this subject must be upheld, namely, that the donee, the appointor under the power, shall, at the time of the exercise of that power, and for any purpose for which it is used, act with good faith and sincerity, and with an entire and single view to the real purpose and object of the power, and not for the purpose accomplishing or carrying into effect any bye or sinister object (I mean sinister in the sense of its being beyond the purpose and intent of the power) which he may desire to effect in the exercise of the power.

This definition is near identical to Browne-Wilkinson VC's conceptualisation of the implied duty of good faith in the Imperial Tobacco case. The breach of the duty of good faith by way of exercising a power for a collateral or improper purpose is the very essence of the fraud on a power doctrine. It may be argued that the ability of the implied duty of good faith to compel an employer to consider the exercise of a discretion or power is

336 As to the judiciary's approach to notions of ownership see 6.2.1.


338 Duke of Portland v Topham (1864) 11 HLC 32 at 54; 11 ER 1242 at 1251.
not replicated in this context. However, to the extent that a failure to consider the exercise of a power or discretion undermines the operation of the scheme or inhibits the fulfilment of its purposes, this could be interpreted to fall within the scope of the fraud on a power doctrine. Finally, although the broad concept of legitimate expectations falls outside the fraud on a power doctrine, any attempted removal of rights, interests or expectancies could, depending on the circumstances, be viewed as an attempt to exercise a power for a purpose not justified by the trust instrument.

The degree of similarity between the implied duty and the equitable doctrine has not gone unnoticed by the judiciary. In *Lock v Westpac Banking Corporation* Waddell CJ did not find it necessary to address an allegation that the employer had committed a fraud on the power of amendment as that allegation simply "put in another way" the allegation, already discussed and rejected, that the employer had breached it implied obligation of good faith. Going a step further, in *LGSS Pty Ltd v Egan* Austin J equated the implied duty of good faith with the doctrine of fraud on a power. In this case the deed of the "Local Government Superannuation Scheme" required the trustee to obtain the consent of Treasurer of the State of New South Wales for any distribution of surplus other than an employer contribution holiday. The Treasurer refused to consent to a proposal by the trustee to apply surplus assets for the benefit of employee members. The trustee contended that the Treasurer owed fiduciary duties in respect of the power. Relying on *Lock v Westpac* and *Imperial Tobacco* as authority, Austin J held that a power vested in a non-fiduciary was nevertheless subject to the doctrine of fraud on a power. Specifically in respect of the Treasurer his Honour stated that:

In my view, in exercising his power to grant or withhold consent under clause 8.2, the Treasurer was subject to the doctrine of fraud on a power. His decision would be open to challenge if he failed to act in good faith, or if he acted for purpose foreign to the power. The critical issue is to determine the proper purposes for which the power may be exercised. It is not important to decide, in this case, whether the Treasurer's power is a fiduciary power in the sense described above, or is a power to exercise in good faith, or whether the administrative law cases apply directly or by analogy to the exercise of the power.

343 *LGSS Pty Ltd v Egan* [2002] NSWSC 1171 at [109].
344 *LGSS Pty Ltd v Egan* [2002] NSWSC 1171 at [111].
Although the judgment mistakenly relies on *Lock v Westpac* and *Imperial Tobacco* as fraud on a power cases, it nonetheless demonstrates the degree of correspondence between the duty and the equitable doctrine. Indeed extra-curially, Lord Millett has expressed a preference for subsuming the implied duty of good faith under the doctrine of fraud on a power, opining that the "obligation from the contract of employment...could equally well be derived from trust law".\(^{345}\)

As an interesting analogy in terms of facts and doctrine, the judgment of the House of Lords in *Equitable Life Assurance Society v Hyman*\(^ {346}\) demonstrates that the equitable doctrine of fraud on a power can also restrain an exercise of a discretion that arises by way of contract. The case concerned retirement annuity contracts under which the policyholders could, upon maturity, elect to take either: (i) an annuity based upon a guaranteed annuity rate ("GAR"); or (ii) an alternative benefit such an annuity calculated at current rates, whether with the Society or some other provider (commonly described as taking a benefit "in fund form").\(^ {347}\) The policies were also "with profits", which entitled policyholders to participate in the profits of the Society by way of the declaration and payment of bonuses. It was the practice of the Society's directors to set the level of a "final bonus" annually, so that a bonus would be automatically allotted to any policy that matured during the year.\(^ {348}\) From 1995 onwards GAR rates began to significantly exceed current annuity rates, making the guarantees expensive to honour. As a means of countering this, the directors resolved to allot different levels of final bonuses to those policyholders who elected to take benefits calculated by reference to the GAR as opposed to those who elected to take their benefits in fund form. The

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346 [2000] 3 All ER 961.

347 Lord Steyn, in the course of describing the contextual background to the facts, commented that one of the most attractive methods in the United Kingdom of retirement saving for the self-employed or those otherwise in non-pensionable employment has been life assurance policies with profits. The premiums paid under such policies attract taxation relief provided that the policyholders take their retirement benefits in the form of a taxable annuity. As the quantum of retirement benefits ultimately payable under a general annuity contract depends on variable investment returns and annuity rates, policies containing guaranteed minimum annuity rates are an attractive way for investors to reduce uncertainties in retirement: *Equitable Life Assurance Society v Hyman* [2000] 3 All ER 961 at 962.

348 The directors declared "reversionary bonuses" annually. These bonuses were irrevocably allotted to policies when declared and thus constituted a vested legal entitlement of the policyholder that was available when the policy matured. By way of comparison, prior to the maturity of the policy "final bonuses" were provisional only, and did not represent a legal entitlement of the policyholder: *Equitable Life Assurance Society v Hyman* [2000] 3 All ER 961 at 964-965 per Lord Steyn.
articles of the society gave the directors a discretion to apportion surpluses "on such principles and by such methods as they from time to time determine".

The issue was whether there was any constraint upon the directors in the exercise of this discretion. Lord Steyn resolved the issue by resort to the traditional contractual approach of implying a term in fact: that the articles of association contained an implied term that prevented the directors from exercising their discretion in a manner which deprived the relevant guarantee of any substantial value. Based upon the strict test of necessity, his Lordship considered the implication was "essential to give effect to the reasonable expectations of the parties".349 Lord Cooke, although agreeing that the matter could be viewed in this way, preferred to adopt a simple fraud on a power approach: that no legal discretion, however widely worded, can be exercised for purposes contrary to those of the instrument by which it is conferred. The directors were not, according to his Lordship, "entitled to exercise the power for a purpose of subverting the basis of the policies fairly interpreted".350 The use of a differential bonus policy Lord Cooke found inconsistent with the object of the policy, namely, to guarantee that when current rates fell below the GAR the annuity received would be higher than were there no GAR. Bonuses were a very significant part of the benefits promised, and ultimately the directors' bonus policy treated the right to a GAR as a disadvantage to those who elected to exercise that right in respect of the benefits payable.351

The preference for the fraud on a power approach is premised upon four significant advantages. The first is simplicity. The process of implying a term in a contract of employment, which is in turn implied into a trust deed, is a convoluted means to achieve the desired end. By comparison, the doctrine of fraud on a power pre-exists in equitable doctrine and provides an automatic fetter on power. Moreover, unlike the imprecise and nebulous concept of good faith, it is based upon well-established authority with a clearer objective.

The second advantage is that its preference reinforces that the legal mechanism governing the relationship: that of trust. It is peculiar to elect a path that requires established priorities of the law to be overturned, when a well-trodden existing path
leads to the same result. In choosing the fraud on power path, focus is turned to the trust instrument and purposes therein stated. A focus on the contract of employment unnecessarily broadens the scope of the obligation beyond what the trust seeks to achieve. A case in point is the application of the concept of legitimate expectations in respect of employers. As discussed above, the purpose of utilising the trust is that of protection – legitimate expectations goes beyond that envisaged by the trust and has the potential in practice to convert mere expectancies into rights. To this end, it masquerades the importation of contractual notions of ownership.

The third advantage is consistency. The fraud on a power doctrine applies equally to trustees. Thus, at a base level all powers within the trust instrument are subject to the same limitation. It is the fiduciary nature of the trustee role that is the fundamental distinguishing feature that compels trustees to act solely in best interests of the beneficiaries and permits employers to guard their own.

Finally, by its very nature, a term implied by law can be modified or excluded by the intention of the parties. Thus, as is a common feature of many schemes, a provision that the employer is not subject to any fiduciary or other duty and may act entirely in its own interests may be sufficient to oust the implied term. Ouster of the fraud on a power doctrine is more difficult, in light of the basis of equitable intervention being premised upon the existence of fraud, broadly defined.

In short, whilst the narrow scope of the implied duty of good faith can be justified on the basis of the SRF, the preferred vehicle is the equitable doctrine of fraud on a power. Not only is it a simpler, more consistent means of achieving the appropriate outcome, it also preserves and promotes the trust relationship.

35 The Pensions Ombudsman in the United Kingdom has held that the employer is not entitled to rely on such a provision to exclude the doctrine of mutual trust and confidence (Poole v Trustees of the Cytec Industries (UK) Ltd Pension Scheme, 16 May 1997). The rationale for this decision, as reported by Pollard, was that such a term was unusual and oppressive and the implied duty cannot be excluded by an agreement to which the member was not a party (Pollard, “Employers’ Powers in Pension Schemes: The Implied Duty of Trust and Confidence” (1997) 11 TLI 94 at 102). Apart from the fact that this decision does not have the status of a judicial opinion, it can be criticised on the further basis that it would seem somewhat unusual for an implied term to operate to modify the terms of a trust instrument, but that the direct intention reflected in that instrument is not sufficient to oust an implied term. Moreover, the notion of an “oppressive and unusual” term appears a curious attempt to apply the contractual doctrine of illegality to the terms of a trust instrument.

353 This approach bears similarity to that argued by Nolan, namely the adoption of a purpose based approach in preference to the implied duty of mutual trust and confidence. However, to the extent that her proposed approach is premised upon the characterisation of a superannuation trust as non-charitable purpose trust (see Hockin v Bank of British Columbia
The protective features ingrained in the trust relationship are soon negated by undue employer influence and control. A prominent feature of the Australian SIS regime is the primacy given to the trust relationship and the position of the trustee. As discussed in Chapter 5, the equal representation rules provide a direct control upon the actions of the employer and its representatives, and alleviate the risk that the employer's interests will be preferred to those of the members. Sections 58 and 59 of the SIS Act further alleviate this risk. Pursuant to s 58, the governing rules of a superannuation entity must not permit the trustee in the exercise of its power to be subject to the direction of another party. Section 59 prohibits a person other than the trustee from exercising a discretion conferred by the governing rules, unless the rules also require the consent of the trustee. These provisions, combined with the equal representation rules, reinforce and protect the position of the trustee and aim to ensure that all decisions taken are in the interests of the beneficiaries. Even where discretion is vested in the employer, the requirement of trustee consent ensures that the exercise of that discretion is bounded by the trustee's duty to act in the best interests of the beneficiaries. One need only look to the Maxwell fraud in the United Kingdom to appreciate the risk of unbounded employer control. Together, the provisions counter a significant agency risk and, to this end, are necessitated by the SRF.

The position is somewhat different in Ontario. There the administrator of a pension plan is conferred overall responsibility by the PBA for the general administration of the pension plan and the investment of plan funds. An administrator is required to carry out the duties and exercise the powers specified in the pension plan and the PBA, and acts in a fiduciary capacity vis-à-vis the members. In this respect, an interesting issue arises from the fact that the administrator is generally the employer-sponsor of the plan. Unlike


The prohibition on “direction” does not prevent the governing rules from vesting a power of consent in the employer: LGSS Pty Ltd v Egan [2002] NSWSC 1171 at [78]-[90] per Austin J.

See 5.2, note 169.


Australia, there is no prohibition on the employer acting unilaterally in that capacity. As a consequence, there is potential for the administrator’s own interest as the employer to conflict with its duties as the administrator (for example, in relation to withdrawal of surplus or termination of the fund). In *Re Imperial Oil Ltd Retirement Plan (No 2)* the former Ontario Pension Commission expressed the following view:359

[although] [the words “employer” and “administrator” are used throughout the [Pension Benefits Act RSO 1990, P8]...they are not used interchangeably. Rather, they are used to describe the two different functions that an employer may serve in respect of a pension plan. The Act recognises that an employer may wear “two hats” in respect of pension plans. Indeed, section 8 specifically states that an employer may be an administrator. In that way, it acknowledges that an employer may play two roles and it is self evident that the two roles may come into conflict from time to time.

Whilst giving the employer a split personality prima facie resolves the issue, at a practical level, the joint role of employer and administrator is arguably not ideal. The first drawback is that it is difficult to compartmentalise employer and administrator functions in respect of the pension plan. Take, for example, a situation where an employer seeks repatriation of a surplus during the continuance of a defined benefit fund. Presuming the employer is granted the discretion in the plan rules to seek such repatriation, the employer is entitled to make a completely self-interested decision to do so. However, as administrator the employer is required to effect that decision in accordance with its duties to the members as set out in the Pension Benefits Act RSO 1990, P8, and as a fiduciary. Within the context of this one power, an employer is conferred two entirely conflicting roles.360 A second drawback follows on from the first: a blurred distinction between powers that can be carried out in a self-interested fashion (ie as employer) and those that must be carried out in a fiduciary capacity (ie as administrator) conceivably creates an environment of uncertainty and confusion for both the employer and the plan members.

The approach taken in Australia is prudentially stronger. Yet given the pensions regime in Ontario is not compulsory, practically, it may be difficult to introduce reforms that curb employer control. As pension plans are provided at the complete discretion of the employer, to shift the balance of control of the plan away from the employer may have the undesired result of decreasing the attractiveness of making provision for employees in their retirement.

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360 It may be argued in respect of the withdrawal of surplus that the statutory requirement that members consent to the proposed withdrawal partly alleviates this problem. As to surplus withdrawal procedures see 3.2.3 and 6.2.4.
6.5 TRUSTEES: THE EXERCISE OF DUTIES, POWERS AND DISCRETIONS

6.5.1 GENERAL PRINCIPLES

Trustees are the central responsible entity of a superannuation or pensions trust. Their role is the most demanding known to equity, requiring action in the best interests of the beneficiaries to the exclusion of all other interests. Trustees are, to this end, the "classic" fiduciaries and thus must not place themselves in a position of conflict with their duty as trustee, or make an unauthorised profit from their position as trustee. The nature and strictness of duties imposed upon trustees is an inverse reflection of the wide discretion conferred upon them. In addition to the usual powers conferred for the purpose of managing a trust and investing its fund, trustees of superannuation funds are conferred various other powers and discretions. Typically the trustee will determine whether an application for a disability benefit meets the required criteria. In the case of the death of a member, power is usually vested in the trustee to determine the destination and division of death benefits to be paid out of the fund. Common also is the conferral of a power to augment benefits. Moreover, the trust deed may even cast a duty on the trustee to reduce actuarial surpluses. Powers to adhere new employers and admit employees are another usual feature of a scheme. Finally, the power to amend the trust deed, or at the very least consent to an amendment, will most often vest in the trustee.

By definition, the exercise of a power is at the discretion of the trustee. Yet this discretion, even if expressed in absolute terms, is not completely unfettered. The equitable doctrine of fraud on a power, discussed earlier in this chapter, is a policy tool that permits judicial control of trustee action. Accordingly, powers must be exercised for the purpose for which they were conferred and not for any collateral or improper purpose. Moreover, the malafide principle dictates that a trustee's discretion must not be exercised irresponsibly, capriciously or wantonly but demands good faith and real and genuine consideration.

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361 Cowan v Scargill [1985] 1 Ch 270 at 287 per Megarry VC; Asea Brown Boveri Superannuation Fund No 1 Pty Ltd v Asea Brown Boveri Pty Ltd [1999] 1 VR 144 at 159 per Beach J.
362 See 6.4.2.3.
363 Grbic, "Fraud on a Power: Judicial Control of Appointments by Discretionary Trustees" (1977) 3 Mon LR 210 at 211.
364 Re Beloved Wilkes' Charity (1851) 3 Mac & G 440 at 448; 42 ER 330 at 333 per Lord Truro; Pilkington v Inland Revenue Commissioners [1964] AC 612 at 641 per Viscount Radcliffe; Gartside v
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It is against this background that at least two important issues arise in the context of superannuation trusts. The first concerns the appropriateness of the trustee giving consideration to the interests of the employer in the exercise of a power or discretion. The second focuses upon whether trustees should be required to give reasons for the exercise of its discretion.

6.5.2 THE RELEVANCE OF THE EMPLOYER'S INTEREST

It cannot be denied that the employer's role within an employer-sponsored or “corporate” superannuation trust is of some significance and importance. The employer is usually responsible for initiating the scheme and, unlike a traditional settlor, has a continuing role. The employer will contribute on an ongoing basis and may even be named as a contingent beneficiary. Moreover, in the case of a defined benefit scheme the employer is generally responsible for its solvency. Given this role, whether it is appropriate for the trustee to consider the interests of the employer in the exercise its duties, powers and discretions conferred by the trust instrument must be considered.

It is in disputes regarding the destination and appropriate use of surplus that the role of trustees is particularly accentuated. For example, where trustees have the power to augment benefits, will they be acting in the best interests of beneficiaries if they do not augment to the full extent of the surplus but permit part of it to benefit the employer? Similarly, is it permissible for the trustee to enter into negotiations with the employer regarding a scheme for the reduction of surplus or accede to an employer request to amend the trust deed so as to permit a payment back to the employer? The traditional legal answer to these questions is that trustees must act in the best interests of the beneficiaries. Thus, to the extent that the employer's interests further those best interests, it is a relevant trustee consideration.

It has been suggested that, in light on the contractual background of the superannuation


A further important issue that arises in this context is the appropriate breadth of the courts' ability to intervene in the exercise of trustees' discretion. Much of the law in this area revolves around the appropriateness of importing administrative law concepts, such as the notion of legitimate expectations, into traditional trust principles. In that the issue concerns the interaction of administrative principle with trust principle, its falls outside the scope of this chapter.
“bargain”, the role and duty of the trustee be formulated by reference to the tripartite nature of the superannuation arrangement. This requires that trustees act fairly with respect to participants in the scheme, permitting consideration of the “legitimate rights” of the employer, and envisaging that the trustee balance the interests of the employer and the beneficiaries. Some would not go so far as to import an extensive requirement of fairness but prefer a more subtle approach of permitting consideration of employer interests where to do so would not detriment the beneficiaries. It is contended that neither approach accords with current authority or the juristic nature of the best interests duty. Nor do their premises, in the context of the SRF, justify any lessening of the absolute nature of a trustee’s duty to beneficiaries.

6.5.1.1 **SUPPORT FOR A REFORMULATION OF THE BEST INTERESTS DUTY?**

Support for a reformulation of the best interests duty in line with the “balancing approach” is usually drawn from two cases: *Lock v Westpac Banking Corporation* and *Edge v Pensions Ombudsman*. Although isolated strands of reasoning from these cases may give some support this approach, a contextual analysis of both cases firmly identifies the trustee in the traditional and exclusive role of the beneficiary representative.

**Lock v Westpac Banking Corporation**

An issue arising in this case was the assessment of whether or not the trustees of a superannuation scheme could take account of the interests of the employer-sponsor in the determining whether to give their consent to an amendment that would allow the return of surplus to members. Prima facie the judgment of Waddell CJ suggests that it is entirely appropriate for trustees to take account of the interests of the employer in the exercise of their power under the trust instrument. His Honour’s comments that appear to support this approach read as follows:

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It seems to me that in the present case the Trustees, while they had a duty to act in the interests of the members, were entitled to take into consideration the interests of the Bank in relation to the surplus which had accumulated in the fund in considering whether or not to consent to the proposed amendment to the deed. If they were satisfied on reasonable grounds that the overall package was a resolution of the interests of the parties in the surplus which was *fair both to the Bank and to the members*, they were, in my opinion, entitled to consent to an amendment enabling part of the surplus to be returned to the Bank.

The above statement must, however, be read in the context of the entire judgment. On the page immediately preceding, the Chief Justice interpreted the provisions of the trust instrument relating to the appointment of trustees to require the trustees to be representative of both the employer Bank and the members. Therefore, in ruling that the trustees were entitled to take into consideration the interests of the Bank, Waddell CJ was doing no more than giving effect to the terms of the trust instrument as he interpreted them. Rather than a departure from ordinary trusts law, his approach is wholly consistent with it – at general law, the terms of the trust can direct or empower a trust to take into account interests other than those of the ultimate beneficiaries.

The reason for this is that the court gives effect to the settlor's intention. If, as evidenced by express trust terms to that effect, the settlor clearly intends the trustee in making discretionary decisions to be entitled to take into account interests beyond those of the beneficiaries, the court cannot fetter that discretion except where its exercise is *mala fides*, wanton or capricious. Where the trust instrument makes no such provision, the court assumes that, consistent with the purpose of creating a trust, the settlor intends the trustee to take account only of the beneficiaries' interests. On this basis, *Lock v Westpac* supports neither a general “balancing of interests” approach nor a general modification of the “best interests” duty in respect of superannuation.

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372 This conclusion is founded upon the trustee appointment and voting clauses, the effect of which were to ensure that the employer appointed trustees were always in a position to outvote the elected employee members. From this it was concluded that the trustees were representative of both the employer Bank and the members: *Lock v Westpac Banking Corporation* (1991) 25 NSWLR 593 at 609 per Waddell CJ.

373 *Harries v Church Commissioners for England* [1992] 1 WLR 1241 at 1247 per Nicholls VC. In this case the court recognised that the trustee could have taken into account non-financial factors in investment decisions had this been expressly prescribed by the terms of the trust instrument. On the facts, as no such prescription appeared in the trust instrument, the trustees were not permitted to take account of interests other than those of the ultimate beneficiaries of the trust.

374 See also *Howkin v Bank of British Columbia* (1990) 71 DLR (4th) 11 (BCCA), where the court held that a superannuation trust is a purpose trust and that the role of a trustee is more akin that of a stakeholder. This led the court to imply that the trustee may take into account the interests of the employer. The incorrectness of this approach was recognised when *Howkin* was heard for a second time in 1995 by the same court: (1995) 123 DLR (4th) 538 at 547. During the period intervening the two hearings the Supreme Court of Canada definitively declared superannuation trusts not to be purpose trusts: *Schmidt v Air Products of Canada Ltd* (1994) 115 DLR (4th) 831. The 1995 *Howkin* case proceeded on the footing that the implications drawn in
**Edge v Pensions Ombudsman**

The *Edge* case concerned the exercise of discretion by trustees to amend the scheme rules. The employer-sponsored fund was in substantial surplus and to avoid adverse taxation consequences the trustees amended the rules so as to reduce contributions payable by both employers and employees and augment the benefits of members in service. Pensioners who received no benefit from the amendment complained to the Pensions Ombudsman. The Pensions Ombudsman held that the trustees had in acted in breach of trust in part because they did not act in the best interests of all of the beneficiaries. This finding of breach was inextricably linked with a finding that the trustee had failed to act impartially vis-à-vis the various classes of beneficiaries. The Ombudsman criticised the trustees' actions for failing to exercise the required degree of independence from those they represented, stating that:

> They attempted to represent both sides of the negotiations at the same time and make only such recommendations as they felt to be fair to “everyone involved with the Funds”. In doing so they created a situation in which their conflicts of interests overwhelmed their duty to be impartial and represent the interests of all classes of beneficiaries.

In allowing an appeal by the trustees, Sir Richard Scott VC expressly rejected this criticism, arguing that in his view “such an attempt as that [to be fair] would have been beyond reproach and exactly what responsible pension fund trustees ought to have done”. It is these comments that have been argued to fortify the fairness debate. In isolation they prima facie enliven the hope of incorporating a “fairness” or “balancing” approach within the best interests duty. However, other comments by Scott VC, when read with the judgment of the Court of Appeal in *Edge*, demonstrate that the focus of the duty continues to be tunnelled exclusively to the best interests of the beneficiaries.

Taking first the further comments of Sir Richard Scott VC. On the page preceding the “fairness” comments his Lordship emphatically disagreed with the Ombudsman’s position that the trustee was not entitled to take account of the position of the employers. In his view, the employers played a critical in the pension scheme: they paid contributions to keep the scheme solvent and encouraged employees to join the scheme and thus pay contributions. However, that the importance of the employers' role was

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375 As cited in *Edge v Pensions Ombudsman* [1999] 4 All ER 546 at 557 per Chadwick LJ (EWCA).

376 *Edge v Pensions Ombudsman* [1998] 3 WLR 466 at 490 (EWHC).

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critical to the best interests of the beneficiaries is evident from his Lordship’s statement that:378

It seems to me obvious that the continued viability of the respective employer was something that, in the interests of the pension scheme and its member as a whole, the trustees were entitled to want to promote. Otherwise, if one or more of the employers went into decline or collapsed, the financial projections, on the basis of which the actuarial calculations had been made, would become invalidated.

Viewed in this light, his Lordship’s subsequent comment that it was appropriate for the trustees to consider “fair” proposals is a reflection only that this was in the best interests of the members in the circumstances. The Court of Appeal confirmed this view of his Lordship’s comments. Chadwick LJ, delivering the judgment of the court, confirmed that on the facts the continued viability of the scheme depended on the continued participation of the employers.379 Moreover, the amendment power required the express consent of the employers. The situation was not similar to that in Re Courage Group’s Pension Scheme,380 where Millett J observed that in such circumstances the “trustees...can be expected to press for generous treatment of employees and employers”. Instead, it was Chadwick LJ’s view that the trustees were in no real position to bargain with the employers:381

The trustees were almost wholly dependent on the goodwill of the employer to obtain any increase in benefits at all. To make only such recommendations as they felt to be fair to everyone involved in the fund was the only sensible and proper course which the trustees could adopt in the circumstances.

The trustees’ overriding concern was to reduce the actuarial surplus in the fund so to avoid the loss of a tax exemption. This was clearly in the best interests of the beneficiaries. The structure of the fund dictated that the means to achieve the objective was by a reduction in contributions382 and that any increase in benefits required employer consent. With this in mind his Lordship further commented that:383

The employers were in a position, in effect, to dictate which classes of members should benefit from that bonus. We do not find it in the least surprising, in those circumstances,

378 Edge v Pensions Ombudsman [1998] 3 WLR 466 at 489 (EWHC) (emphasis supplied).
379 Edge v Pensions Ombudsman [1999] 4 All ER 546 at 572 (EWCA).
380 [1987] 1 All ER 528 at 545.
381 Edge v Pensions Ombudsman [1999] 4 All ER 546 at 574 (EWCA).
382 Pursuant to the trust instrument, the trustee was under a duty to accept the actuary’s advice as to the rate of employer contributions. In that employer contributions were required to be at least equal in amount to the members’ contributions, the effect of reducing the employer contributions was to also automatically reduce member contributions: Edge v Pensions Ombudsman [1999] 4 All ER 546 at 549 (EWCA).
383 Edge v Pensions Ombudsman [1999] 4 All ER 546 at 574 (CA).
that the trustees should take the view that they should put forward a proposal which the
employers would be likely to find attractive. They were entitled to take the view that
half a loaf was better than no bread.

At all the times the concern of both the High Court and the Court of Appeal was the
interest of the beneficiaries. The interests of the employer were relevant, indeed critical,
but only as a function of the furthering the interests of the beneficiaries. To forward
proposals, as was suggested by the Ombudsman, which were not fair to the employers,
would not in the circumstances of the case have furthered the beneficiaries’ interests.
The structure of the scheme necessitated negotiation between the employer and the
trustee and in the circumstances the trustee achieved an outcome that furthered the
best interests of the beneficiaries. Neither Sir Richard Scott VC nor the Court of
Appeal reformulated the role of the trustee to one that balances or represents the
interests of both employees and employers. Instead, under Edge the role of the trustee
remains that of representing, and acting in, the best interests of the beneficiaries.

6.5.1.2 The Juristic Nature of the Best Interests Duty

Not only can any judicial support for the view that the best interests duty encompasses
a balancing role be dismissed, any such reformulation is contrary to the juristic nature of
the best interest duty and ultimately undermines the protective features of the trust.
The starting point for an examination of the juristic nature of the best interests duty is
the oft quoted decision of Cowan v Scargill, where Megarry VC summarised the content
of this duty as follows:384

The starting point is the duty of trustees to exercise their powers in the best interests of
the present and future beneficiaries of the trust, holding the scales impartially between
different classes of beneficiaries. This duty of the trustees towards their beneficiaries is
paramount. They must of course, obey the law, but subject to that they must put the
interests of their beneficiaries first.

The focus of this statement is on the position of the beneficiaries – their interests are
paramount. Thus, subject to the qualification that trustees must obey the law, the duty
of trustees is of the greatest importance or significance. This principle may even require
the trustee to act dishonourably (though not illegally) if the beneficiaries’ interests
require it.385 The facts of Cowan v Scargill demonstrate the strictness with which this

384 [1985] 1 Ch 270 at 286-287. This principle has been followed in Lock v Westpac Banking
Corporation (1991) 25 NSWLR 593 at 609-610 per Waddell CJ; Registrar of Accident Compensation
Tribunal v Commissioner of Taxation (Cth) (1993) 178 CLR 145 at 182 per Brennan, Dawson and
McHugh JJ; Jones v AMP Perpetual Trustee Company NZ Ltd [1994] 1 NZLR 690 at 706 per
Thomas J; Knudsen v Kara Kar [2000] NSWSC 715 at 57 per Austin J.

385 Cowan v Scargill [1985] 1 Ch 270 at 287-288 per Megarry VC.
duty is viewed. The case concerned a pension scheme for miners. The committee of management, constituted by five union trustees (as member representatives) and five employer trustees, controlled and administered the scheme. An investment plan was established that specified a scheme of investment for the asset categories of marketable securities, land and industrial finance. It contemplated investments overseas as well as in oil and gas in respect of each category. The scheme was subsequently revised, to which the union trustees objected on the ground that it failed to take account of union policy not to invest overseas or in oil. Despite argument that such prohibitions were in the best interests of the beneficiaries, Megarry VC held that the prohibitions the union trustees sought to impose were not, according to the evidence, in the best interests of the beneficiaries.386

Specifically in respect of the overseas investments, evidence was led on behalf of the union trustees that tended to show that the prohibitions would not be harmful to the beneficiaries or jeopardise the aims of the fund.387 His Lordship's reply to this argument demonstrates the importance attached to the best interests duty:388

Such evidence misses the point. Trustees must do the best they can for the benefit of their beneficiaries and not merely avoid harming them. I find it impossible to see how it will assist trustees to do the best they can for their beneficiaries by prohibiting a wide range of investments that are authorised by the terms of the trust.

Further evidence was led by the union trustees that the proposed prohibitions against oil and overseas investments would revive the nation's economy and aid the prosperity of the coal industry (being a competitor to oil). The end result, it was argued, would be to aid the prosperity of the scheme and lead to increased benefits for the members. Megarry VC, although appreciating the possible benefit for the economy, stated that any such benefit that would flow to the scheme was "far too remote and speculative" to consider.389

Two important points can be drawn from this judgment:

386 Cowan v Scargill [1985] 1 Ch 270 at 293.
387 The employer trustees had sought directions from the court to the effect that the member trustees had breached their fiduciary duty to the beneficiaries. Interestingly, the court did not canvass the issue of fiduciary duty. Instead Megarry VC repeatedly referred to the applicability of the principles of trust law. At no time was reference made to a breach of fiduciary duty or the no-profit or no-conflict rules. Rather the actions of the union trustees were considered to be a breach of trust principles.
That trustees must act in the best interests of the beneficiaries is a positive duty to act as opposed to the mere avoidance of harm.

In the assessment of the best interests duty only direct benefit to the beneficiaries can be considered – evidence that points to benefits that are remote and speculative is irrelevant.

Relating these points of principle to the two alternative reformulations of the best interests duty – incorporation of a fairness or balancing concept (the "fairness approach") or permitting consideration of the employer's position where the interests of the beneficiaries would not be prejudiced (the "permissive approach") – are both not only beyond authority but fail to account for or address the juristic nature of the duty.

The juristic nature of the best interests duty underpins Megarry VC's judgment. There are two aspects. First, in requiring a trustee's duty to beneficiaries to be paramount, the sole focus of the trustee is the interests of the beneficiaries. To permit or require the consideration of third party interests, or in this context the interests of the employer, distorts that focus and creates the danger that any decision will be tainted by a clouded perspective. What then of a situation in which a number of options are open to a trustee and it is considered that each option is equally beneficial – can the interests the employer be used to tip the scales one way or the other? Despite the likely rarity of such a situation, to allow a consideration of the interests of the employer immediately shifts the focus of the trustee away from the beneficiaries. It is this shift in focus that the decision in Cowan v Scargill is concerned to prevent. Not only does requiring or permitting consideration of the interests of the employer distort the considerations to which the trustee may have due regard, it may also result in the trustee assessing the best interests of the beneficiaries through "employer coloured" glasses. In other words, it confuses the role of the trustee and creates a danger that the "best interests" of the beneficiaries will not be served.

Secondly, the mere avoidance of harm results in a loss of opportunity. To suggest that the beneficiaries would be in the same position whether or not third party interests are taken into account is to deny the existence of the lost opportunity. Thus, if a loss of opportunity can be considered a "benefit" to the beneficiaries, it is doubtful that a situation could arise where the preference of the employers' interests would not prejudice the beneficiaries.

The best interests duty is a fundamental tenet of the protective nature of the trust instrument. The requirement that trustees must act exclusively in the interests of the beneficiaries ensures that the position of the trustee is not compromised. As was highlighted in Cowan, the very nature of a superannuation or pensions fund makes it "all the more important that the interests of the beneficiaries should be paramount so that
they may receive the benefits which in part they have paid for." On this basis, the SRF precludes a development in the law that lessens the absolute nature of the trustee's duty to beneficiaries.

6.5.1.3 APPROPRIATE CONSIDERATION OF THE EMPLOYER'S INTEREST

The final question to be considered concerns the issue of when the trustee can take account of the interests of employers. The interests of the employer are potentially relevant in two contexts. In the first instance, because trustees are bound to act in the interests of all beneficiaries, if the trust instrument confers beneficiary status upon an employer, the trustee is bound by general principles to consider the interests of the employer as a beneficiary and the employee beneficiaries as a whole. In all other contexts, the interests of the employer are relevant, if and only if, such interests are in the best interests of the beneficiaries and the benefit is one that is not too remote or speculative. In essence, consideration of the employer's interest is coincidental—it can only occur when the interests of the employer coincides with the best interests of the beneficiaries. This point was recognised in *Asea Brown Boveri Superannuation Fund No 1 Pty Ltd v Asea Brown Boveri Pty Ltd* where Beach J, reflecting specifically upon amendment of the trust instrument, commented:

In my opinion trustees of a superannuation fund owe a duty of loyalty exclusively to the members. It does not follow from that, however, that a trust deed can never be altered to meet the interests of the employer. Trustees are free to negotiate with an employer for a package of amendments that may include benefits to the employer if in the opinion of the trustees that would benefit the members.

It has been argued that this quote is "clear authority for asserting that, in superannuation schemes, the views of the employer are a relevant consideration which trustees may validly take into account". To a limited extent this is correct. However, the words of Beach J add a crucial qualification, which in turn summarises the crux of the issue—"if in the opinion of the trustee that would benefit the members."

The structure and provisions of the trust deed dictate the weight that a trustee can legitimately accord to employer considerations. Of particular importance is whether

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390 Cowan v Scargill (1985) 1 Ch 270 at 290 per Megarry VC.
391 [1999] 1 VR 144 at 161 (emphasis supplied).
393 *Asea Brown Boveri Superannuation Fund No 1 Pty Ltd v Asea Brown Boveri Pty Ltd* [1999] 1 VR 144 at 161 (emphasis supplied).
employer consent is a prerequisite to an exercise of the relevant power. This was crucial in the *Edge* judgment. The structure of the scheme combined with the possibility of losing a valuable taxation concession placed the ball very much in the court of the employer. So much so that the Court of Appeal was led to conclude that the “trustees were in no real position to bargain”. By way of comparison, in *Hillsdown Holdings plc v Pensions Ombudsman* Knox J held that the trustee was mistaken as to the extent to which it had to negotiate with the employer regarding the application of surplus. The trust deed conferred a unilateral discretion upon the trustee. Subject to taking the advice of the actuary, there was no requirement as to employer consent. In these circumstances it was held that the trustee gave too much weight to employers’ views.

Hence, the terms of the trust deed may contemplate employer and trustee interaction and negotiation, but at all times the trustee acts in a representative capacity with a view to furthering the interests of the beneficiaries. This does not mean the trustee should treat the employer with contempt, seek to frustrate the reasonable objectives of the employer, or never enter into negotiations with the employer. Indeed, the circumstances may even be such that the exercise of a power (for example, the power of amendment) in manner that prima facie seems to prejudice the interests of the beneficiaries may be in their best interests as a whole. It simply means that the circumstances should be viewed through “beneficiary coloured glasses” so as to further the best interests of the beneficiaries.

In conclusion, the foregoing is not designed to negate or minimise the role of the employer in superannuation. Nor should it be taken to propose that recognition of employer interests and the provision of a commercially viable inducement to attract employers further into the realm of superannuation are not worthwhile objects.

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394 *Edge v Pensions Ombudsman* [1999] 4 All ER 546 at 574 per Chadwick LJ (giving the judgment of EWCA). See further the heading “*Edge v Pensions Ombudsman*” in 6.5.1.1.

395 [1997] 1 All ER 862 (EWHC).

396 *Hillsdown Holdings plc v Pensions Ombudsman* [1997] 1 All ER 862 at 891 per Knox J (EWHC).

397 See, for example, *Gru-bam Australia Pty Ltd v Perpetual Trustee WA Ltd* (1989) 1 WAR 65. Here a unit trust deed provided for the redemption of units to be valued at the value of the units seven days before the request was made. Following the 1987 stock market crash the value of the investments comprised in the fund fell dramatically and certain unit holders sought to redeem their units. In response, the manager convened a meeting of unit holders at which the deed was amended to substitute a current realisation value for the units required to be repurchased under the deed. The Full Court of the Supreme Court of Western Australia held that the manager had acted in the best interests of the beneficiaries notwithstanding that the amendment diminished the rights of unit holders that had sought to enforce their pre-amendment realisation claim (at 92 per Pidgeon J, at 84-85 per Malcolm CJ).
However, it is submitted that a reformulation of the best interests duty is not the appropriate means to achieve this recognition. The very core of the institution of the trust and the accompanying position of trusteeship is that of protection of the beneficiaries. This demands that trustees act in the best interests of the beneficiaries — to the exclusion of all other interests, including the employer. As a matter of the priority of interests, the object of protection demands that in respect of the guardian's role in superannuation that the interests of the employer are subjugated to those of the beneficiaries.

6.5.3 Reasons

The general law trustees' duty to account is a corollary of the beneficiaries' right to secure proper administration of the trust, and requires trustees to furnish beneficiaries (upon request) with full information concerning the management of the trust fund. However, the general law also affords to trustees protection in the exercise of their discretion. This is demonstrated by the well-established principle of ancient origin that “trustees exercising a discretionary power are not bound to disclose to their beneficiaries the reasons actuating them in coming to a decision” (the “no reasons” principle). It follows that information required to be furnished pursuant to the duty to account cannot extend to the reasons for the exercise of discretion. This receives corresponding recognition in the context of the disclosure of trust documents — beneficiaries are not entitled to access trust documents that disclose the reasons for the exercise of trustees' discretion.

Yet it appears that the “no reasons” protection afforded to trustees is set at an unreasonably high level in the context of superannuation trusts. In particular, a relaxation of the general law “no reasons” principle is justified upon the basis of the SRF. In this instance the departure from trust principle is justified upon the basis that the “no reasons” principle is based upon a rationale that is not applicable in the superannuation context. Instead, the protection of beneficiaries' interests is facilitated if beneficiaries that are

398 Re Pennell (decd) [1945] VLR 302 at 305-306 per O’Bryan J; Hartigan Nominees Pty Ltd v Rydge (1992) 29 NSWLR 348 at 356 per Hope JA.


400 Re Londonderry's Settlement [1965] 1 Ch 918.
affected by a trustee's exercise of discretion have a right to access reasons for that discretionary decision. This argument is also consistent with the nature of superannuation trusts and the general trend in superannuation regulation of increased disclosure and open accountability.

6.5.1.1 INAPPLICABLE RATIONALE

It was in the context of beneficiary access to trust documents that the English Court of Appeal in Re Londonderry’s Settlement addressed the rationale for the “no reasons” principle. A beneficiary of a family trust (the settlor’s daughter) sought access to various documents in the possession of the trustee, namely, copies of the minutes of trustees’ meetings, documents prepared for these meetings, and correspondence between the trustees, beneficiaries and settlor. The court held that even if such documents were “trust documents”, they were not accessible by the beneficiaries if they contained matters the trustee was not bound to disclose. Salmon LJ, giving primacy to the “no reasons” principle, explained its rationale as follows:

[A] ground for this rule is that it would not be for the good of beneficiaries as a whole, and yet another that it might make the lives of trustee intolerable should such an obligation rest upon them: Re Beloved Wilkes’s Charity (1831) 3 Mac & G 440; 42 ER 330; Re Gremham Life Assurance Society (1872) 8 Ch App 446. Nothing would be more likely to embitter family feelings and the relationship between the trustees and members of the family were trustees obliged to state their reasons for the exercise of the power in trusted to them. It might indeed well be difficult to persuade any persons to act as trustees were a duty to disclose their reasons, with all the embarrassment, arguments and quarrels that might ensue, added to their present not inconsiderable burdens.

Harman LJ also commented on the rationale underlying the principle, opining that:

This is a long-standing principle and rests largely I think on the view that nobody could be called upon to accept a trusteeship involving the exercise of a discretion unless, in the absence of bad faith, he were not liable to have his motives or his reasons called in question either by the beneficiaries or by the court.

These extracts identify three justifications for the principle in question. First, the giving of reasons is inconsistent with the principle that trustees’ decisions cannot be challenged where the discretion is exercised bona fide and without improper motive. Secondly, to require the giving of reasons would be likely to embitter family feelings, and the relationship between the trustees and members of the family. Finally, such a

401 [1965] 1 Ch 918.
402 Re Londonderry’s Settlement [1965] 1 Ch 918 at 933 per Harman LJ, at 935-936 per Danckwerts LJ, at 936-937 per Salmon LJ.
403 Re Londonderry’s Settlement [1965] 1 Ch 918 at 937.
404 Re Londonderry’s Settlement [1965] 1 Ch 918 at 928.
requirement adds to trustees’ already onerous obligations. It is argued that none of these justifications apply in the superannuation context, or even generally in the commercial sphere. Each is discussed in turn.

(i) Offends against the “Mala Fides” Principle

General principles of trust law dictate that a court will only interfere with the exercise of a discretionary power by a trustee if the discretion has been exercised *mala fide* having regard to the purpose for which it is given (the “*mala fides* principle”). An alternate formulation of the rule is that a trustee’s discretion cannot be exercised irresponsibly, capriciously or wantonly. In the determination of this issue, the court may look at whether the discretion has been exercised with real and genuine consideration. In *Karger v Paul*, McGarvie J succinctly stated the relevant principles as follows:

...it is open to the Court to examine the evidence to decide whether there has been a failure by the trustees to exercise the discretion in good faith, upon real and genuine consideration and in accordance with the purposes for which the discretion was conferred. As part of the process of, and solely for the purpose of, ascertaining whether there has been any such failure, it is relevant to look at evidence of the inquiries which were made by the trustees, the information they had and the reasons for, and manner of, their exercising their discretion. However, it is not open to the Court to look at those things for the independent purpose of impugning the exercise of discretion on the grounds that their inquiries, information or reasons or the manner of exercise of the discretion, fell short or what was appropriate and sufficient. Nor is it open to the Court to look at the factual situation established by the evidence, for the independent purpose of impugning the exercise of the discretion on the grounds the trustees were wrong in their appreciation of the facts or made an unwise or unjustified exercise of discretion in the circumstances...In short, the Court examines whether the discretion was exercised but does not examine how it was exercised.

Thus the duty of supervision on the part of the court has traditionally been confined to questioning the honesty and integrity with which the deliberation has been conducted and does not extend to an examination of the soundness of the conclusions. The court cannot usurp the function of the trustee and intervene merely because it would have reached a different decision on the facts.

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405 *Re Beloved Wilkes’s Charity* (1851) 3 Mac & G 440; 42 ER 330; *Karger v Paul* [1984] VR 161.
406 *Pilkington v Inland Revenue Commissioners* [1964] AC 612 at 641 per Viscount Radcliffe; *Gartside v Inland Revenue Commissioners* [1968] AC 533 at 617-618 per Lord Wilberforce; *Lutheran Church of Australia South Australia District Incorporated v Farmers’ Co-operative Executors and Trustees Ltd* (1970) 121 CLR 628 at 639 per Barwick CJ; *Karger v Paul* [1984] VR 161 at 164-166 per McGarvie J.
Added to these traditional grounds are two further facets of review. First is the "reasonableness requirement". In the situation where there is an obligation to form an opinion as part of an exercise of discretion, the decision will be invalidated if it is "one which no reasonable trustee could make on the material which was before it".\footnote{Maciejewski \textit{v} Telstra Super Pty Ltd (No 2) [1999] NSWSC 341 at [21] per Windeyer J (emphasis supplied). See also Telstra Super Pty Ltd \textit{v} Flegeltaub (2000) 45 ATR 470 at 477 per Callaway JA (VCA). It is interesting to note the comments of Mahoney JA in \textit{Hurtigan Nominees Pty Ltd \textit{v} Rydge} (1992) 29 NSWLR 405 at 428 that, in principle, it is not clear whether the unreasonableness of a particular exercise is itself a ground for setting an exercise of discretion aside or whether it is merely evidence that the exercise was mala fides or otherwise not within power.}

In essence the decision is required to fall within a spectrum of reasonableness. This is of particular relevance in the superannuation context where trustees are most often required to determine if, in their discretion, a member meets the criteria for a disability benefit.

Secondly, in the United Kingdom a further basis for intervention in the decision-making of trustees has developed. Termed the rule in \textit{Re Hastings Bass},\footnote{Re Hastings-Bass (decd) [1975] Ch 25 at 41 per Buckley LJ. See also \textit{Mettoy Pension Trustees Ltd \textit{v} Evans} [1990] 1 WLR 1587 at 1624 per Warner J; \textit{Stannard \textit{v} Fisons Pension Trust Ltd} [1992] RLR 27 at 31 per Dillon LJ. For a more detailed discussion of the rule in \textit{Re Hastings-Bass} see Maclean, \textit{Trusts and Powers} (Law Book Company, 1989) pp 47-49; Sir Robert Walker, "Some Trust Principles in the Pensions Context" in Oakley (ed), \textit{Trends in Contemporary Trust Law} (Clarendon Press, 1996), pp 126-129; Hillard, "Re Hastings-Bass: Too Good to be True?" (2002) 16 TLI 202.} it dictates that the discretion of a trustee can be interfered with by the court if it is clear that the trustee would not have acted as he or she did "(a) had he not taken into account considerations which he should not have taken into account, or (b) had he not failed to take into account considerations which he ought to have taken into account".\footnote{\textit{Mettoy Pension Trustees Ltd \textit{v} Evans} [1990] 1 WLR 1587 at 1624 per Warner J.}

This rule focuses on the examination of the constituent elements of the trustee's decision in order to determine whether the trustee failed to take into account considerations he or she ought, or ought not, have taken into account.\footnote{[1999] 1 VR 144 at 155 per Beach J.} This approach goes further than that stated in \textit{Karger \textit{v} Paul} but has subsequently been rejected in the Australian context in \textit{Asea Brown Boveri Superannuation Fund No 1 Pty Ltd \textit{v} Asea Brown Boveri Pty Ltd}.\footnote{See also \textit{Telstra Super \textit{v} Flegeltaub} (2000) 45 ATR 470 at 477 per Callaway JA (VCA).}

The objection to the disclosure of reasons appears to be premised upon a concern that a relaxation of the principle will concomitantly widen the review function of the
court – if reasons are voluntarily disclosed the court is required to examine the substance of those reasons. That there is an appreciable difference between the two review functions is doubtful. Moreover, as a matter of general principle, the specification of different review functions arguably lacks logic and consistency. In light of these considerations, close scrutiny of the foregoing principles indicates that while the giving of reasons is touted as offending against the "mala fides" principle, in practice, it supports the principle.

A purview of three aspects of the courts' application of the mala fides principle serves to amplify the doubt that the courts' supervisory function widens upon the voluntary disclosure of reasons.

The first aspect relates to the courts' response to the failure of a trustee to offer reasons. When a beneficiary challenges through the process of legal proceedings the exercise of a trustee's discretion on the basis of mala fides, the court may, despite the "no reasons rule" in certain circumstances, draw an adverse inference where reasons are not proffered. The comments of Robert Walker J in Scott v National Trust for Places of Historic Interest of Natural Beauty are apposite in this respect:

[i]f a decision taken by trustees is directly attacked in legal proceedings, the trustees may be compelled either legally (through discovery or subpoena) or practically (in order to avoid adverse inferences being drawn) to disclose the substance for their decision...Indeed whilst trustees do not have to give reasons in a case where a plaintiff puts forward a prima facie case that the trustee's discretion has miscarried, the absence of reasons and the absence of any evidence before the Court as to what happened, will tend to make that prima facie case a virtual certainty.

So whilst as a matter of legal principle trustees are not required to express reasons for their discretionary decisions, practically they may be compelled to do so. In fact, the failure to provide reasons will tend to make any prima facie case put forward by the beneficiary a "virtual certainty". The facts of the Maciejewski v Telstra Super Pty Ltd illustrate this point. They revolved around a decision of Telstra Super Pty Ltd (as trustee of the Telstra Superannuation Scheme) not to award a claim by Miss

44 Re Beloved Wilkes's Charity (1851) 3 Mac & G 440 at 447-449; 42 ER 330 at 333-334 per Lord Truro; Karger v Paul (1984) VR 161 at 166 per McGarvie J; Rapa v Patience (Unreported, Supreme Court of New South Wales, McLelland J, 4 April 1985) at 11; Meat Industry Employees Superannuation Fund Pty Ltd v Petrucci (Unreported, Supreme Court of Victoria, Nathan J, 28 February 1992) at 2; Esso Australia Ltd v Australian Petroleum Agents' & Distributors' Association (1999) 3 VR 642 at 651-652 per Hayne J; Telstra Super Pty Ltd v Flegeltaub (2000) 45 ATR 470 at 477 per Callaway JA (VCA).

45 (1998) 2 All ER 705 at 719 (EWHC) (emphasis supplied).

Maciejewski for a total and permanent incapacity benefit. The primary issue for the
trustee's consideration in determining Miss Maciejewski's claim was whether:

in the opinion of the trustee, after consideration of all relevant information,
evidence and advice, is the member unlikely ever to engage in any gainful work for
which s/he is, for the time being, reasonably qualified by education, training, or
experience?

For the purpose of answering this question the trustee had before it a document
prepared by the death and invalidity benefits manager ("the manager"). The
document set out various extracts from medical reports that were submitted by both
the trustee and Miss Maciejewski. However, the medical reports were gathered some
five to six years earlier for the purpose of establishing workers' compensation
liability. The manager recommended that the claim be denied and the trustee
concluded likewise. The reasons for this decision were not recorded and the minutes
of the meeting merely noted that the directors of the trustee "unanimously resolved
to deny the claim". The New South Wales Supreme Court held that the trustee
failed to give the claim real and genuine consideration.

During the course of argument, counsel for the trustee argued that the decision was
not reviewable because the trustee was not required to give reasons for its decision.
Young J correctly rejected this argument on the ground that "[a]lthough the Court
will not interfere with the proper discretion of trustees, the Court will also not allow
people who are using their power under a trust deed to deny the beneficiary rights by
incompetence or inaction". His Honour, commenting on the lack of the evidence
presented on behalf of the trustee which told "the Court absolutely nothing", and
relying on Scott v National Trust, drew an adverse inference from the trustee's
failure to provide any reasons for the decision. In other words, it was presumed that
there was no evidence that could have assisted the trustee.

A supporter of the "no reasons" principle would seek to counter this argument with
the principle that when a trustee discloses reasons as a matter of litigious necessity a
trustee's legal protection is maintained in that the beneficiaries are precluded from

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417 Maciejewski v Telstra Super Pty Ltd (1998) 44 NSWLR 601 at 603 per Young J.
418 Maciejewski v Telstra Super Pty Ltd (1998) 44 NSWLR 601 at 604 per Young J.
421 Scott v National Trust for Places of Historic Interest or Natural Beauty [1998] 2 All ER 705 (EWHC).
relying upon that evidence to examine and review the substance of the trustee’s exercise of discretion.\textsuperscript{422} This leads to the second aspect of the issue. In response, it is submitted that as a matter of practice, the court will examine the substance of a trustee’s decision in order to draw a conclusion on the\textit{bona fide} exercise of discretion.

Curial assessment of whether the trustee has taken account of irrelevant considerations, or has failed to give a real and genuine consideration, essentially necessitates reviewing the rationale underlying the decision – ie the reasons for the decision. It is the very substance of the decision that determines if there has been a\textit{bona fide} exercise of discretion. The case of \textit{Vidovic v Email Superannuation Pty Ltd}\textsuperscript{423} provides an example of this point. It concerned a claim for a total and permanent disablement benefit. Upon consideration of medical reports, the trustee of the Email Superannuation Scheme denied Mr Vidovic’s claim. The minutes of the relevant trustee meeting recorded that Mr Vidovic was not totally and permanently disabled within the meaning of the trust deed. Importantly, the reasons for the trustee’s decision were revealed in its answers to interrogatories. Essentially, the trustee had relied upon four medical reports. Applying \textit{Karger v Paul},\textsuperscript{424} Bryson J examined the decision of the trustee for evidence of “real and genuine consideration”, and held that:\textsuperscript{425}

\begin{quote}

it was impossible for the defendant’s directors to have come to the conclusion expressed in their resolution if they gave reasonable consideration to the medical reports which were before them with a view to coming to a conclusion on the existence of total and permanent disablement as defined in the trust deed. Their resolution was for that reason not an effectual exercise of their power to determine the plaintiff’s claim.

\end{quote}

In concluding that the trustees had not given “reasonable consideration of the medical reports” the court’s examination of the trustee’s reasons appears to go further than the traditional mere questioning of the honesty and integrity with which the deliberation was conducted. If in this case the trustee had in fact volunteered its reasons, so that the court could assess their soundness, the outcome would arguably have been the same. In assessing the\textit{bona fide} exercise of discretion, the court examined the substance of the trustee’s reasons outlined in the answers to the

\begin{footnotes}
\textsuperscript{422} \textit{Karger v Paul} [1984] VR 161 at 166 per McGarvie J.

\textsuperscript{423} (Unreported, Bryson J, Supreme Court of New South Wales, 3 March 1993).

\textsuperscript{424} [1984] VR 161.

\textsuperscript{425} \textit{Vidovic v Email Superannuation Pty Ltd} (Unreported, Bryson J, Supreme Court of New South Wales, 3 March 1993) at 20.
\end{footnotes}
interrogatories. Had reasons been voluntarily proffered the scope of the review would have been effectively the same. In both scenarios the court examined the substance of the trustee's reasons.

That the court does in practice examine the substance of a decision is further substantiated by the converse situation. It is said that the mala fides rule is somewhat self-perpetuating as the lack of reasons itself renders it more difficult to establish whether the trustee has acted in good faith and with real and genuine consideration. This was certainly the case in *Esso Australia Ltd v Australian Petroleum Agents' and Distributors' Association*, where Hayne J found it necessary to deny the plaintiff's claim that the decision of the trustee (the defendant) be overturned. The trustee had not stated its reasons and therefore it was not possible for Hayne J to conclude whether it had taken account of irrelevant considerations.

As the final aspect, it is relevant to compare the courts' approach to the review function when reasons have been voluntarily provided. In *Meat Industry Employers Superannuation Fund Pty Ltd v Petrucelli* Nathan J outlined the review function in these circumstances as being delineated by the following six points:

1. Whether the reasons relate to or are relevant to the discretion to be exercised.
2. Whether the reasons were arrived at in good faith and without an ulterior purpose (see *Karger* [1984] VR 161 and *Re Beloved Wilkes's Charity* (1851) 3 Mac & G 440; 42 ER 330).
3. Whether the reasons reasonably support the conclusion.
4. It is open to the court to look at evidence of the enquiries made by the trustees, the information they had and the manner of the exercise of their discretion, but only so far as to assess the viability of the exercise, not to impugn or replace it.
5. It is not open to the Court to examine the reasons for the purposes of exercising its own discretion. It is not open to the Court to examine the factual situation for the purposes of substituting its own discretion for that of the trustee because the Court might consider the trustee unwise or imprudent (see also *Dundee Hospital v Walker* [1952] 1 All ER 896). (6) It follows as a compelling matter of logic that the reviewable discretion is that which was exercised by the trustees at the time.

*Prima facie* the review outlined in points (1) and (3) is broader than that enunciated in *Karger v Paul*. Added to the review function is whether or not the reasons stated justify the conclusion. Yet this is not appreciably different from an investigation into whether there has been a real and genuine consideration, or has taken into account

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427 [1999] 3 VR 642.
428 *Esso Australia Ltd v Australian Petroleum Agents' & Distributors' Association* [1999] 3 VR 642 at 655-656.
429 (Unreported, Supreme Court of Victoria, Nathan J, 28 February 1992) at 7-8.
irrelevant considerations. A failure on this basis would also generate the conclusion that the reasons do not justify the decision. Similarly, it is difficult to imagine that the court could so conclude, and yet not also conclude that there had been some other failure such as taking account of irrelevant considerations or not giving a real and genuine consideration.

Even more compelling is the identified objective of the courts' review function. Nathan J expressly characterised the review function at point (5) as not being for the purposes of substituting its own discretion for that of the trustee because the Court might consider the trustee unwise or imprudent. Thus, even where soundness of reasons is liable to investigation, the court does not conduct a hearing de novo as to how the trustee should have exercised its discretion. On this basis the courts' objective in reviewing a trustee's discretion remains constant regardless of the disclosure of reasons or otherwise. In neither case does the court subjugate the function of the trustee or act as an appeal from the trustee's decision. Accordingly, the standard of review does not alter but evidentially the challenge becomes easier. This view is supported by Lord Normand who, in responding to an argument that the court has a greater liberty to examine and correct a decision if the trustees give reasons, stated:

In my opinion, that is erroneous. The principles on which the courts must proceed are the same whether the reasons for the trustees' decision are disclosed or not, but, or course, it becomes easier to examine a decision if the reasons for it have been disclosed. Lord Truro's judgment in Re Wilkes's Beloved Charity ought not be construed as going beyond that.

Robert Walker J has also been a strong proponent of this view, expressly approving the statement of Lord Normand, and arguing extra-curially that:

It would certainly be odd if the court were more ready to intervene against trustees who are careful enough to obtain full written advice and keep full written minutes, and candid enough to disclose them to their members' scrutiny.

Austin J in the Supreme Court of New South Wales has more recently approved these views.

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431 *Dundee General Hospitals Board of Management v Walker* [1952] 1 All ER 896 at 900 (HL). The remaining Law Lords did not comment on this submission.

432 *Scott v National Trust for Places of Historic Interest or Natural Beauty* [1988] 2 All ER 705 at 718-719 (EWHC).

In review, that the court draws an adverse inference on the failure to proffer reasons, finds it difficult to assess the bona fides of a decision without reasons, and utilises reasons where available, demonstrates that the provision of reasons supports rather than hinders the review process. Moreover, in that the standard of review remains constant regardless of the availability of reasons, the objection to the provision of reasons as offending against the mala fides rule lacks substance. The relaxation of the "no reasons" rule simply broadens the evidential material before the court. Even on the assumption that the voluntary provision of reasons will enliven a broader review function, given the courts will presume there are no reasons where reasons are not proffered, there is in practice only a very fine line between the two review functions.

Even if the above argument cannot be sustained, the distinction between the scope of review permitted when reasons are disclosed out of litigious necessity, as opposed to where they are voluntarily disclosed, is arguably misplaced and illogical. Trustees are effectively encouraged to deny any request for reasons, reasonable or otherwise. In the event of a denied request, a beneficiary wishing to challenge a trustee's decision-making must litigate the matter. If reasons are then disclosed in the context of litigation, the beneficiary is not entitled to rely on those reasons for the purpose of substantive review. The general law serves to protect the trustee at every level, hindering every effort of beneficiaries seeking due administration of a trust. The illogically of this approach is substantiated by the words of Sir Robert Walker cited directly above.435

A further ramification of the creation of an environment of secrecy is that it can lead to speculative actions for breach of trust.436 If a trustee is not forthcoming with reasons for a decision, the secrecy itself can foster a suspicion that the trust has been maladministered. A policy of openness guards against the consequential waste of economic resources, not only of the litigant beneficiary but of all the other

434 Knudsen v Kara Kar Holdings Pty Ltd [2000] NSWSC 715 at [61]. Austin J also considered that Young J's approach in Maciejewski v Telstra Super Pty Ltd (1998) 44 NSWLR 601 of drawing an adverse inference from the trustee's failure to provide any reasons for the decision represented an implicit acceptance on Lord Normand's approach.


beneficiaries of the trust. The comments of Young J in the *Maciejewski* case should be noted in this regard:437

It must also be remembered that it costs thousands of dollars for a person to approach this Court for relief. That may not be very much in the eyes of the defendant, but it does mean that because it is so difficult and expensive for a worker who challenges decisions of this nature that those who are given the job of acting fairly under superannuation schemes must be scrupulously professional, careful and assisting. If they are not, then this Court will need to step in.

(ii) *Embitter Family Feelings*

In *Re Londonderry's Settlement*438 the English Court of Appeal did not allow beneficiaries access to agendas and minutes of trustee meetings that disclosed the reasons for discretionary decisions because it could cause "infinite trouble in the family". For similar reasons, the beneficiary in *Hartigan Nominees Pty Ltd v Rydge*439 was denied access to a memorandum of the settlor's wishes that was created specifically for use of the trustees in exercising their discretionary powers. Within the sphere of the traditional family trust a concern for the maintenance of harmonious relationships between family members may be a valid consideration. Yet even in this context it has been argued that although the "plain truth might sometime hurt a beneficiary...nothing can excite more suspicion and ill-feeling than an unreasoned and apparently arbitrary decision of trustees".440 In any event, when one moves into the commercial sphere of superannuation a concern not to embitter family feelings or relationships as a rationale for the "no reasons" principle holds far less weight and is arguably irrelevant. A superannuation fund is generally constituted in the context of the employment relationship. Consequently, the relationship between the members of the superannuation fund is one of employment. Moreover, the relationship between trustees and members is professional, not familial, in nature.

It may well be that small self-managed funds – "Mum and Dad" type funds – are established on a more familial basis. Trustees of larger funds may also confront difficult family situations in the distribution of death benefits, such as distributing to an illegitimate child, the existence of which may be unknown to the deceased's spouse. Yet such situations can be managed upon a confidentiality basis. To heighten


438 [1965] 1 Ch 918 at 935 per Danckwerts LJ.


440 Samuels, "Disclosure of Trust Documents" (1965) 28 MLR 220 at 228.
the barrier of effective review on the basis that the trustee may occasionally face embarrassing situations somewhat overcompensates especially given that the beneficiaries in a superannuation trust are not mere volunteers. It also reinforces the traditional paternalistic role of trustees and assumes that beneficiaries would prefer to be shielded from embarrassing situations than have an effective ability to seek review.

(iii) Onerous Obligations of Trustees

It is true to state that trustees are subject to onerous obligations. However, trustees of superannuation trusts are somewhat removed from the position of the traditional family trustee. No longer the devout clergyman found in Re Beloved Wilkes's Charity, superannuation trustees professionally manage millions of dollars on behalf of the beneficiaries. Moreover, unlike trustees of traditional family trusts, superannuation trustees are invariably (and generously) remunerated for their services. If not directly remunerated, as may be case with employer and employee representatives, trusteeship will often be a part of the "paid" employment function. Adding a further obligation is therefore a remunerative and cost issue, not one which alone can dictate that trustees need not provide reasons.

It must be remembered that what is being suggested is not a widening of the review function, but the provision of reasons to facilitate that review function. The proposed relaxation for the "no reasons" rule does not contemplate trustees performing an additional duty but rather the disclosure of reasons for a decision that has already been made. It is recognised that at times the settling of reasons by the trustee may be difficult. This is particularly so in the case of a corporate trustee constituted by a number of directors. Yet in the face of litigation it seems that trustees have experienced no real difficulty “settling” reasons in defence of the exercise of their discretion. Moreover, the requirement to settle collective reasons for a decision can lead only to a better and more considered decision-making process. It would be a curious state of affairs to permit trustees (or directors thereof) to manage

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442 Kingsford Smith, “Who Knows Best? Review of Discretionary Powers in Superannuation Funds” (2000) 28 ABLR 418 at 436. Kingsford-Smith argues further that even when trustees of a fund are truly volunteers and receive no extra remuneration or leave from employer, that such trustees nevertheless “have the protection the court from harassing and vexatious beneficiaries” (Harrigan Nominees Pty Ltd v Kyde (1993) 29 NSWLR 405 at 420 per Kirby P) and up to a point legislation permits trust deeds to limit the liability of trustees: at 436.
multi-million dollar funds and yet exempt them from settling reasons for decisions in respect of that fund because the process is too difficult.443

As a corollary to this point it must also be borne in mind that in all of the jurisdictions canvassed by this thesis the general statutory trend is towards greater disclosure and greater accountability to members.444 Moreover, in the Australian context provision of information to members has been expressed to be a fundamental tenet of the SIS Act and SIS Regulations.445 Access by beneficiaries to trustees' reasons is entirely consistent with this trend.

6.5.1.2 ARGUMENTS AGAINST RELAXATION OF THE “NO REASONS” RULE

Two arguments are generally raised in opposition to relaxing the “no reasons” rule in superannuation trusts. The first, that the “no reasons” principle is inconsistent with the courts' jurisdiction to review the discretionary decisions of trustees, has been addressed above.446 The second argument is that all trusts should be subject to the same rules, including in this case, the “no reasons” rule. Though this argument was also mentioned earlier, it merits further comment in view of the decision in Wilson v Law Debenture Trust Corp plc.447

The facts of this case concerned a request by a number of beneficiaries of a company superannuation fund for the provision of reasons in relation to a surplus distribution decision. The plaintiff beneficiaries, as a result of a part sale of the original company, had been transferred to the purchaser's superannuation scheme. The trustee of the original scheme transferred an amount in respect of the transferred employees to the purchaser's scheme. Although at the time of sale a substantial actuarial surplus remained

443 Davis argues although it may pose a challenge to a court or tribunal if the recorded reasoning of each trustee is different, it is nevertheless open for the court or tribunal to decide that the different reasons of each trustee are all defective: Davis, The Law of Superannuation in Australia (2nd ed, Butterworths, Looseleaf), at §4.65.
445 Commonwealth of Australia, Department of Treasury, Strengthening Super Security, Statement by the Honourable John Dawkins MP Treasurer of the Commonwealth of Australia, 1992. In this statement John Dawkins (the then Treasurer), in explaining the current superannuation regulatory regime, made the following comment in respect of the provision of information to members: “The disclosure of adequate and appropriate information to members is a critical element in the prudential arrangements if members are to be in a position to exercise influence over the direction their fund takes” (at 13).
446 See the heading “(g) Offends against the “Mala Fides” Principle” in 6.5.1.1.
447 [1995] 2 All ER 337 (EWHC).
in the original scheme, the trustees determined not to transfer any part of the surplus to the purchaser's scheme. The plaintiff beneficiaries sought reasons for this decision.

Counsel for the plaintiffs argued that trustees of superannuation funds were bound to give reasons for the exercise of discretions conferred by the relevant trust instrument as it was unreasonable that members who have purchased their interests should not be able to see that the trustee had exercised its discretion properly. After a lengthy examination of the various authorities, Rattee J held that the traditional principles as to the exercise by trustees of discretion applied to pension schemes.\(^{448}\) His Lordship recognised that a pension scheme is different to a private trust, but considered that the relevant issue turned on the nature of the interest purchased. Although a beneficiary of a superannuation fund provides consideration, the interest purchased remains a mere expectancy and therefore the rights that flow from this interest are limited to those at general law.\(^{449}\)

Although it is correct to state that a beneficiary of a superannuation fund holds a mere expectancy, this does not necessitate a conclusion that established trust principles are appropriate merely because traditionally this has been the case. Instead, a better approach is to examine the underlying rationale for the relevant principle to determine if it holds true in the modern context. This point was not argued before his Lordship and so was not addressed in his judgment. In this context the words of Lord Browne-Wilkinson in Target Holdings Ltd v Redfern are apt:\(^{450}\)

> It is important, if the trust is not to be rendered commercially useless, to distinguish between the basic principles of trust law and those specialist rules developed in relation to traditional trusts, which are applicable only to such trusts and the rationale of which has no application to trusts of quite a different kind.

The so-called distinctive nature of superannuation trusts may also be called upon as a basis upon which to depart from traditional principle. That members are said to have earned their rights is arguably a basis upon which to require the giving of reasons. Consistent with the Wilson case, though this factor in and of itself may be insufficient to support this conclusion, when combined with the fact that the traditional rationale for "no reasons" rule does not hold true, the proposed departure is justified in terms of the inapplicability limb of the SRF. Further justification can also be found on the basis of

\(^{448}\) *Wilson v Law Debenture Trust Corp plc* [1995] 2 All ER 337 at 348 (EWHC).


\(^{450}\) [1995] 3 WLR 352 at 362 (HL).
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the protective limb. The very heart of trust is its protective attributes. Even if a beneficiary holds a mere expectancy, the rights flowing from that expectancy should be protected. At general law all beneficiaries have a right to due administration of the trust. As such, beneficiaries have the right to ensure that the trustee carries out the terms of the trust and exercises any powers and discretions conferred bona fide for the purposes of the trust. As is highlighted earlier, logically, it is very difficult for a beneficiary to assess due administration of the trust without some form of evidence. Access to reasons for the exercise of discretionary decisions provides information upon which an assessment can be made. How can a proper assessment otherwise be made? It was thought in Re Londonderry that this difficulty could be averted through disclosure at the discovery stage.

Yet the fallacy in this approach is demonstrated by its consequence: it requires beneficiaries to undertake actions alleging bad faith without first being in a position to determine if such an action is feasible. On the one hand, the practical ramification is that the costs associated with commencing actions will deter beneficiaries. On the other hand, as noted earlier, the creation of an environment of secrecy can lead to speculative actions for breach of trust. A policy of openness guards against the consequential waste of economic resources of not only the litigant beneficiary but all other beneficiaries the trustee represents. Even if a beneficiary chooses this course, the path to disclosure is nevertheless fraught with uncertainty and difficulty. As is argued by Nobles:

The rights to discovery, and to serve interrogatories, can themselves be nullified through a successful application to strike out proceedings on the basis that they reveal no cause of action. If members have no evidence of impropriety, then their action may not survive such an application.

In view of these considerations there is very little that protects, and secures to beneficiaries, their right of due administration. Thus, notions of protection in

451 Re Coram (1992) 109 ALR 353 at 356-357 per O'Loughlin J.
452 See 6.5.1.1.
453 See Re Londonderry's Settlement [1965] 1 Ch 918 at 938 where Salmon LJ stated: "The position is quite different where the beneficiary seeks disclosure of documents from the trustee in the air, as in this case, from the position where the beneficiary seeks discovery of documents in an action in which allegations are being made against the bona fides of the trustees. If the documents in question are in the position or power of the trustees and are relevant to the issues in the action, they must be disclosed whether or not they are trust documents." See also Megarry, "The Ambit of a Trustee's Duty of Disclosure" (1965) 81 LQR 192 at 196-197.
conjunction with the redundancy the “no reasons” rationale justifies, and can be argued to necessitate, a relaxation of the “no reasons” principle.

Though traditionally the courts have unquestioningly and uncritically applied the “no reasons” rule, there are small signs of turning tides in the superannuation waters. Following Kirby P’s dissatisfaction in his dissenting judgment in Hartigan Nominees with the Re Londonderry decision, Young J of the Supreme Court of New South Wales expressed sympathy with the plight of superannuation beneficiaries:

It must also be remembered that it costs thousands of dollars for a person to approach this Court for relief. That may not be very much in the eyes of the defendant, but it does mean that because it is so difficult and expensive for a worker who challenges decisions of this nature that those who are given the job of acting fairly under superannuation schemes must be scrupulously professional, careful and assisting. If they are not, then this Court will need to step in.

This sympathy led him to draw an adverse inference from the trustee’s failure to proffer reasons. In somewhat stronger terms, the comments of Bryson J in the Vidovic case may be argued to foreshadow a change in principle. Focusing upon the factual matrix in which a superannuation scheme is placed, his Honour opined that:

It is a marked anomaly to use mechanisms drawn from fields of law remote from employment and relating to trusts for bounty or charity to administer important entitlements in an employment relationship. I find it difficult to understand why the entrenchment of such important rights against review is so usual, and why this kind of arrangement is so commonly found acceptable to employees in view of the economic significance of such decisions and the economic function of superannuation... In an arrangement with a contractual character in which value is given in the expectation that a benefit will be available in stated circumstances a construction in which one party has an entire and unreviewable power to determine whether that party will pay a sum of money to the other or retain it in its own funds has an element of absurdity.

455 See Kingsford Smith, “Who Knows Best? Review of Discretionary Powers in Superannuation Funds” (2000) 28 ABLR 418, who argues that there are signs that the courts are impatient with the tardy and shabby treatment received by some fund members in the exercise of trustee discretions. To this end, she maintains that “in subtle but discernable ways, in the superannuation area of trust law, there are suggestions that the standards and techniques of administrative review are influencing the language and the thinking of judges” (at 436-437).


458 See 6.5.1.1.

459 Vidovic v Email Superannuation Pty Ltd (Unreported, Bryson J, Supreme Court of New South Wales, 3 March 1995).

460 Vidovic v Email Superannuation Pty Ltd (Unreported, Bryson J, Supreme Court of New South Wales, 3 March 1995) at 11. These comments were approved by Gallop ACJ in Minehan v AGL Employees Superannuation Pty Ltd (1998) 134 ACTR 1 at 10-11.
That the “no reasons” rule is not of such resolute standing in the superannuation context is also evident from statements in *Telstra Super Pty Ltd v Flegeltaub*, where counsel for the superannuation scheme member proposed that, in the situation where a fiduciary is obliged to form an opinion on a question fact, there might also be a duty to give reasons. Callaway JA noted that this would entail introducing a radical difference between trustees deciding a question of fact and trustees exercising a *Karger v Paul* discretion. However, rather than dismissing the argument out of hand, his Honour considered that the case was “not a suitable vehicle to decide the point”. Although he also stated that he did not wish to give any encouragement to the argument, it has nevertheless left the door ajar for a more detailed crucial examination. Opening the door even wider are the comments of Austin J that the court will in the review of an exercise of discretion “take into account reasons given by the trustee”. This led his Honour to comment that the “no reasons” formulation “has been revised” and is no longer “a safe formulation of orthodox principles”.

These views are not stated for the purpose of establishing that there has been a progression in the traditional doctrine, but to indicate a level of judicial support for the proposed view. A recent decision of the Privy Council, though not directly on point (as it focused on the source of the right to trust documents), is nonetheless also in line with this judicial trend.

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464 *Knudsen v Kara Kar Holdings Pty Ltd* [2000] NSWSC 715 at [61].
465 *Knudsen v Kara Kar Holdings Pty Ltd* [2000] NSWSC 715 at [61].
466 *Schmidt v Rosewood Trust Ltd* [2003] 2 WLR 1442. The case concerned a claim against the trustees of a discretionary trust for the disclosure of trust documents. The fund, worth millions of dollars, appears to have been derived from the Russian oil industry. The petitioner's late father was a co-settlor and, like all directors of Russia's largest oil company (Lukoil), was named as an object of the settlement. The petitioner claimed both on his behalf (as a beneficiary of his father's estate) and as the administrator of the estate. The trustees opposed the disclosure on the basis that the father, as no more than an object of the power, had no entitlement to trust documents or information. Their Lordships considered that a beneficiary's right to the disclosure of trust documents was not premised upon the notion of there being a proprietary right to such disclosure. Instead, “it is best approached as an aspect of the court's inherent jurisdiction to supervise, and where appropriate intervene in, the administration of trusts” (at 1463). It found no reason to “draw any bright dividing line” between the rights of an object of a discretionary trust and those of the object of a mere power” (at 1463). Although the case did not directly concern the giving of reasons, their Lordships approach to disclosure, as a aspect of “court's inherent jurisdiction to supervise” may represent an inroad into the “no reasons” principle – ie that the court could, in the appropriate circumstances, permit disclosure contrary to the traditional “no reasons” rule. See Arthur and Sargant, “About Schmidt: Vadium Schmidt v Rosewood Trust Limited”, presented at APL Castelaw Forum, May 2003, Association of Pensions Lawyers (see www.apl.org.uk).
Ultimately the issue concerns prioritising either the interests of the beneficiaries or those of the trustee. As has been recognised by Steele, "[t]he tension...is between ensuring an acceptable level of protection of trustees in their discretionary decision-making (and thus ensuring continued supply of willing trustees) and securing protection for and advancement of, the best interests of the beneficiaries".467 Professor Waters similarly characterises the issue as follows:468

The inevitable question then is whether the modern trustee, whose essential role is to manage property for others, should be in the patriarchal position of not only being excused from giving reasons for his discretionary decisions, but of being able to withhold from the beneficiaries any document, whether or not originated by third parties, which was involved in the process of the decision that were made. Different generations give different answers to that question...

This thesis argues that, in this generation – the age of superannuation – the answer should indeed change. The protection of trustees is currently at a level that denies the basic right of a beneficiary to effectively determine whether or not there has been due administration of the trust. This is most concerning where those functions of due administration impact directly upon the beneficiary, such as in decisions regarding benefits. As a medium for assessing change within the generation, the principles of SRF justify if not compel a relaxation of the "no reasons" principle

6.5.1.3 IMPLEMENTATION

Acceptance of the proposed departure from traditional principle, namely that beneficiaries should be entitled to reasons in respect of the exercise of a discretionary power of a superannuation trustee, necessitates examination of the most effective method of implementation. There are two options: reform of the general law or statutory intervention. The former option suffers two deficiencies. First, it is not a timely option. If a decision was made at lower court level not to follow Re Londonderry in the superannuation context, the decision would undoubtedly be appealed. As a result, it could take years, if not decades, to reform the law. Secondly, even if the right to reasons principle gained acceptance at general law, it could be excluded by express provision in the trust instrument, thereby negating the effect of the reform.

Given the inherent deficiencies of reform at general law, the most effective method of implementation is statutory intervention. In this context, it is interesting to note that the trustee legislation in Queensland, Western Australia and New Zealand contains a

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provision that overrides the general law position in respect to the disclosure of reasons.\textsuperscript{469} The Queensland provision, the \textit{Trusts Act} 1973 (Qld), s 8(i) reads as follows:

Any person who has, directly or indirectly, an interest, whether vested or contingent, in any trust property or who has a right of due administration in respect of any trust, and who is aggrieved by any act, omission or decision of a trustee or other person in the exercise of any power conferred by this Act or by law or by the instrument (if any) creating the trust, or who has reasonable grounds to apprehend any such act, omission or decision by which the person will be aggrieved, may apply to the court to review the act, omission or decision, or to give directions in respect of the apprehended act, omission or decision; and the court may require the trustee or other person to appear before it and to substantiate and uphold the grounds of the act, omission or decision which is being reviewed and may make such order in the premises (including such order as to costs) as the circumstances require.

The general effect of this provision is to grant jurisdiction to the court to order "a trustee to give reasons for what it has done, or not done".\textsuperscript{470} This section has been interpreted in accord with the general law reluctance to interfere with the discretionary acts of private trustees.\textsuperscript{471} Before the court will exercise its power, an applicant must show that the relevant decision of the trustee is of real significance in the affairs of the trust and that there are real and substantial grounds for questioning its correctness. Where a challenge is made on the basis that there has been an absence of prudence and wisdom in the trustee's decision, a far heavier onus is said to rest upon the applicant.\textsuperscript{472} The power conferred upon the court is, in practice, therefore more limited than a literal reading of the statute suggests. In any event, the Western Australian and New Zealand counterparts are available only to beneficiaries who have an interest in the trust. As such, they have no practical application to superannuation trusts whose beneficiaries usually have a mere expectancy rather than an interest in the trust. Moreover, the legislation in each of these jurisdictions requires an application to the court, which necessarily involves cost. For these reasons, it is not suggested that this statutory initiative be adopted in other jurisdictions to effect a reform of the general law.

\textsuperscript{469} \textit{Trusts Act} 1973 (Qld) s 8; \textit{Trustees Act} 1962 (WA) s 94; \textit{Trustee Act} 1956 (NZ) s 68.

\textsuperscript{470} \textit{Re Koczorowski} [1974] Qd R 177 at 183 per Dunn J. The provision was enacted out of a concern of the limitations imposed by the general law in respect of the disclosure of reasons. See QLRC, \textit{A Report of the Law Reform Commission on the Law Relating to Trusts, Trustees, Settled Land and Charities}, No 8, 1971, at 11-13. In this report it was stated by the Commission that: "it is, we think, preferable that trustees should occasionally experience some embarrassment in publicly justifying their decisions than that beneficiaries should be left quite ignorant as to the reasons which have determined disposition of what is, after all, beneficially their property and that of the trustee" (at 11). For a more comprehensive treatment of the \textit{Trusts Act} 1973 (Qld) s 8 and the \textit{Trustees Act} 1962 (WA) s 94 see Hardingham and Baxt, \textit{Discretionary Trusts} (2nd ed, Butterworths, 1984), pp 116-118.

\textsuperscript{471} \textit{Re Whitehouse} [1982] Qd R 196 at 204 per Macrossan J.

\textsuperscript{472} \textit{Re Koczorowski} [1974] Qd R 177 at 185 per Dunn J; \textit{Re Whitehouse} [1982] Qd R 196 at 204 per Macrossan J.
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A better approach is to confer a direct right on beneficiaries to access the reasons for trustees' discretionary decisions. This may be effected through an amendment to the SIS Act s 52, which sets out a number of trustee covenants, ranging from a duty to act honestly to a requirement to formulate and implement investment and reserving strategies. The covenants are implied into the governing rules of all superannuation entities. Therefore, to the extent that the trustee covenants differ from general law, the effect of s 52 is to exclude the application of the general law by the express terms of the trust deed of the superannuation entity. The proposed reform could be achieved by including an additional trustee covenant that has the effect of requiring trustees to:

(a) record reasons for the exercise of discretion; and
(b) subject to confidentiality restraints, make such reasons available, upon request, to interested beneficiaries.

The purpose of the interested beneficiary requirement is to limit the access of reasons to those beneficiaries: (a) in respect of whom the decision was made; and/or (b) who suffer direct financial detriment as a result of the trustee's decision. The right to reasons should not apply in respect of the general management of the fund, for this could severely hinder the trustees' ability to manage the fund. Instead, the right to reasons would be limited to situations where beneficiaries are directly affected by the outcome, for example, in respect of decisions concerning disability payments, death benefits and surplus distributions. On the confidentiality point, as the information that a trustee considers in the process of making a decision will invariably consist of personal and financial details of the relevant beneficiaries, it is important that the confidentiality of that information be maintained. Therefore, where the reasons for a trustee's decision contain confidential details, beneficiaries should not, without the requisite consents, be able to access such information in respect of other beneficiaries.

The suggested approach has two main advantages. First, as the effect of s 52 is to statutorily modify the trust instrument, the proposed reform is effected by the express terms of the relevant trust deed. Consequently, the effect of the general law principle that beneficiaries cannot rely on reasons disclosed out of litigious necessity is negated. The disclosure of reasons is required by the trust deed, not by litigious necessity. Secondly, the reform is consistent with the review jurisdiction of the Superannuation Complaints Tribunal ("SCT"). The SCT has jurisdiction to hear complaints in relation

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to the decisions and conduct of trustees, insurers or RSA providers. There are specific grounds of complaint listed in the Superannuation (Resolution of Complaints) Act 1993 (Cth), all of which are based upon the relevant decision or conduct being unfair or unreasonable. In particular, s 14 provides that if the trustee of a fund has made a decision in relation to a particular member or former member of a regulated superannuation fund, a person may make a complaint to the SCT that the decision is or was unfair or unreasonable. Importantly, however, complaints must be defined with specificity and not relate to the general management of the fund. The proposed reform would assist the SCT in determining whether a decision is fair and reasonable. Limiting access to interested beneficiaries is compatible with the SCT's scope of review. Thus consistency is achieved across the spectrum of regulation.

Conclusion

A distinctive feature of the superannuation trust is its intrinsic link to the employment relationship. The private relationship of the trust is the mechanism used to make provision for retirement, yet the funding for that provision is an incident of the remuneration received by the employee in return for his or her services. The involvement of the employer may run deeper than the simple payment of contributions; the employer itself may choose to initiate a scheme on behalf of his or her employees, and the trust deed may contemplate employer participation in the administration and management of the fund. This interaction yields two main tensions, which are most conveniently phrased as questions.

The term “decision” is given a wide meaning and includes the failure to make a decision: Superannuation (Resolution of Complaints) Act 1993 (Cth) s 4. An example is a decision relating to the payment of a benefit or some other matter affecting the member or beneficiary. The term “conduct” includes acts, omissions and representations: s 30. The term “RSA provider” refers to any person who is the provider of a Retirement Savings Account (“RSA”): Retirement Savings Accounts Act 1997 (Cth) s 12. An RSA is a non-trust structure directed principally to providing benefits on retirement and death. Certain financial institutions and life insurance companies may offer such accounts.

The SCT does not have the power to require reasons from trustees. However, the SCT has encouraged trustees to record their reasons so that they are available for review, indicating that where such reasons are not available an adverse inference will be drawn: Edstein, “More Reasons for Not Recording Reasons” (1996) 191 Superfunds 36 at 36. The proposed reform will assist the SCT in determining whether or not a trustee's decision is fair and reasonable.
First, what is the influence of the contract of employment on the structure of the trust and the interests arising therefrom? Secondly, what is the proper role of the employer and trustee within that structure? The SRF has been utilised as a structure for analysis of the general law in light of these tensions and questions, and to assist in assessing statutory intervention in this context.

**Influence of the Contractual Relationship**

The interaction of the trust with the employment relationship has led some commentators to argue that a distinctive set of principles is applicable to the superannuation trust. Indeed some characterise the underlying interests of the parties as contractual, which naturally leads to assumptions and assertions regarding the true ownership of the trust fund. However, putting aside for one moment the implied duty of good faith, consistent with the first limb of the SRF there is little evidence of departure from general trust principle in the judicial interpretation of the superannuation trust instrument. Judgments, almost without exception, address the issues at hand by referencing two hallowed principles: that the courts' approach should be practical and purposive; and that the constituent documents should be construed against their factual matrix. The latter in turn requires consideration of the fact that superannuation funds are established against the background of employment and so must be interpreted against that background; beneficiaries are not volunteers, their rights have contractual and commercial origins and have been earned by their service under contracts of employment.

Yet the contract of employment has, in practice, had little impact upon general principles of interpretation and their application to the issues of surplus and amendment. First, it cannot be said that the "factual matrix" principles represent a contractual approach to interpretation. There are "no special rules of construction"; the principles utilised are those applicable generally to trusts. Moreover, they are universally relevant as determinants of intention.

Secondly, the courts have not employed the factual matrix approach to import contractual notions of ownership. Counsel have repeatedly urged the judiciary to characterise the

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477  Mettoy Pension Trustees Ltd v Evans [1990] 1 WLR 1587 at 1610 per Warner J.
478  Imperial Group Pension Trust Ltd v Imperial Tobacco Ltd [1991] 2 All ER 597 at 605 per Browne-Wilkinson VC.
479  Mettoy Pension Trustees Ltd v Evans [1990] 1 WLR 1587 at 1610 per Warner J.
480  Re Courage Group's Pension Schemes [1987] 1 All ER 528 at 537 per Millett J.
rights and interests underlying the superannuation trust as flowing from contractual underpinnings, in order to support claims, albeit conflicting, to respect of the trust fund. However, the courts have time and time again resorted to the words of the trust instrument, preferring to adopt a solution that lies within the terms of the scheme itself, not within a world populated by competing philosophies of ownership. The application of this approach is particularly evident in respect of the surplus issue. In determining whether or not an actuarial surplus can be reduced by a contribution holidays or payment to the employer, the words of the trust instrument have been determinative. An investigation as to the nature of the employer’s funding obligation and the role of the actuary in determining the appropriate contribution rate determines the availability of a contribution holiday, whereas payment out to the employer requires an express power to that effect.

In the context of realised surplus, the courts have utilised the general law presumption of resulting trust to fill any gaps in beneficial ownership. Contenders for a share of surplus have generally deferred to competing contractual notions of ownership to support their claim. Again the courts have eschewed these notions, preferring instead to prioritise the nature of the particular trust at hand by tracing not only source of the contributions but the use of those contributions within the scheme. Although traces of contractual bargain theory are evident from the Privy Council’s recent decision in *Air Jamaica Ltd v Charlton*, it is doubtful that this case can be relied upon as affirming the contractual ownership approach. Their Lordships seemed to be influenced by the justice of outcome; the contractual analysis conveniently provided the means to the end sought. Moreover, Lord Millett in giving the judgment of the court disavowed general support for the ownership approach by stating that it was “not obvious”, when employees have contributed more than was needed to fund benefits, that they should not receive a return based simply on the argument that they had received all that they had bargained for.

*Finally*, the courts have not generally utilised the practical and purposive approach of interpretation as a guise for the adoption of contractual notions of ownership. A consistent theme in the interpretation of superannuation trusts, particularly regarding amendment, has been the use of the purposive approach. At a superficial level it can easily be argued that the purpose of the trust is to provide benefits, and so any amendment inconsistent with that purpose is invalid. Proponents of the contractual view argue that this is consistent with the notion that benefits are deferred pay and thus the deed should be

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482 *Air Jamaica Ltd v Charlton* [1999] 1 WLR 1399 at 1412.
interpreted on this basis. While it is true to state that superannuation and pension funds are held generally for the benefit of employees, the extent of that holding and the precise substratum of a trust will be defined by reference to the specific provisions of the trust, for it is these that reveal the intent of the settlor.

These conclusions are not intended to indicate that an entirely uniform approach has been taken or that theories of ownership have never influenced the judiciary. Indeed, the views of Lord Browne-Wilkinson are a prominent exception. Instead, these comments represent that the trend of juridical views and considerations has been to promote the terms of the trust instrument, thereby prioritising the principles of the general law of trusts.

**The Role of the Employer and Trustee**

**The Employer**

The glaring exception to the above conclusions is the recognition of an implied obligation of good faith to control the exercise of any power conferred on the employer. Emanating from general principles of contract law, this implied obligation not only arises in contract but operates to modify the powers and discretions conferred on the employer by the trust instrument. Thus, regardless of the intent of the settlor to confer absolute power on the employer, the implied contractual obligation will fetter and limit the employer's actions. Specifically, it will prevent the exercise of a power for collateral and improper purposes, will compel the employer to consider the exercise of its powers, and will restrain a unilateral pursuit of its own interests without regard to the employees' "legitimate expectations". This elevation of contractual principle over and above the settlor's freedom to frame the terms of the trust as he or she sees fit can in part be justified upon the basis of the protective limb of the SRF. It protects against the removal of existing rights and expectations, and prevents the employer from exercising its power for a collateral purpose. But to the extent that the legitimate expectation concept has the potential to transform a mere expectancy into something more akin to a right, it falls outside of the parameters of the SRF.

Despite this justifiable departure from trust principle, it is recommended that the general law eschew these notions of contract law in favour of a broad application of the equitable doctrine of fraud on power. This doctrine likewise restrains employers' actions, but has the added advantage of being a more consistent, and less complex, approach that preserves and promotes trust principle.
Trustee

The ongoing participation of the employer within a superannuation scheme has in turn emphasised the role of the trustee; it has been suggested that the trustee's role and duty be formulated by reference to the tripartite nature of the superannuation arrangement. In short, this would require the trustee to act fairly with respect to the participants in the scheme, including the employer. The principles underlying the SRF preclude any development in the law that lessens the absolute nature of the trustee's duty to beneficiaries. The duty to act in the best interests of the beneficiaries marshals duties of loyalty to their service and economic well being. Any reformulation of the trustee's role in this respect is fundamentally inconsistent with the juristic nature of this "best interests duty" and ultimately undermines the protective features of the trust. This is not to say that employers' interests can never be considered or that the trustee should seek to frustrate the reasonable objectives of the employer, but that such consideration is qualified and bounded by the best interests of the beneficiaries.

Although the best interests duty is fundamental to the protective nature of the trust, there is little that assists beneficiaries in the review of trustee action. Trustees, though under a duty to account to beneficiaries, are protected in the exercise of their discretion by not being bound to disclose the reasons actuating their decisions. Principally on the basis on the inapplicability limb of the SRF, this chapter concludes that the "no reasons" rule should be relaxed. The justifications for its imposition expounded in Re Londonderry's Settlement do not apply in the superannuation context, or even in the general commercial sphere. Moreover, its relaxation would assist to protect and secure to beneficiaries their right of due administration of the trust. To this end, it is suggested that the most effective manner of implementation is statutory intervention. As such, it is tentatively recommended that the implied trustee covenants in SIS Act s 52(2) be modified to confer a direct right on beneficiaries to access the reasons for trustees' discretionary decisions relating to them.

Statutory Initiatives

In respect of the interaction of trust and contract, legislatures have exhibited concern regarding the role of the employer. All jurisdictions canvassed in this thesis seek to limit and control the employer's influence via statutory intervention. Controls have been placed

484 [1965] 1 Ch 918.
upon the unilateral exercise of employer discretions and powers, the ability of the employer to unilaterally manage the fund, and the ability to effect a repatriation of surplus to the employer. The Australian regime, like that of Hong Kong, is particularly strong in this regard. The position of the trustee is protected and promoted by prohibiting the employer (and any other person) from directing the trustee. Moreover, the exercise of any discretion by the employer requires the consent of the trustee. Finally, safeguards are implemented as to the repayment of surplus to the employer.

Although these provisions limit the settlor's general freedom, all are necessitated by the protective limb of the SRF. Unbounded employer control and influence generates significant agency risk; the interests of the employer are not aligned with those of beneficiaries, creating a risk that the employer's interests will be preferred.

Despite the existing protections, three aspects would further strengthen the Australian regime. *First*, the approach adopted in Ontario of requiring the trust deed to specifically address the issue of surplus, and the specification of accompanying rules of construction, would add greater certainty to the interpretation of trust provisions.

*Secondly*, specific regulator involvement in the process of repatriation of surplus to the employer could be considered as a further safeguard. In this respect, Australia is the only regime that permits payment of surplus without regulatory consent.

*Finally*, to the extent, if any, that the surplus repayment provision (SIS Act s 117(5)) can be interpreted to require the trustee to balance the interests of the employer and the members, it represents an unjustifiable departure from general trust principle. A better approach is that in the United Kingdom, where the trustee's duty to act in the best interests of the beneficiaries is statutorily reinforced specifically in relation to the payment of surplus out to the employer.

Weaknesses are also evident in other jurisdictions. Ontario is particularly susceptible to risk arising from conflicts of interest with the employer permitted to unilaterally manage the pension plan. The United Kingdom regime would arguably benefit from provisions, similar to those in Australia, that further promote the role of the trustee. However, as these jurisdictions do not embrace the compulsory collection of contributions, it is recognised that further shifting control in favour of trustees is difficult. Where superannuation and pension provision is provided at the discretion of the employer, to shift the balance of control further away from the employer may have the undesired result of decreasing the attractiveness of making provision for employees in their retirement.
In conclusion, excepting the implied obligation of good faith, the general law prioritises general trust principle in the resolution of tensions and disputes between trust and contract within superannuation law. Although premised upon contract principle and not the preferred vehicle for its task, the implied obligation has protective underpinnings and assists to protect beneficiaries' interests against undue employer influence and control. The role of trustees is likewise promoted as guardians and protectors who act solely and exclusively in the interests of beneficiaries. It is these principles that underlie the general law and statutory governance of trust and contract relations.
CHAPTER 7

CONCLUSION

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7.1 **OVERVIEW**

The real problem is that pension law is an emerging field and there is no framework for development. Pension law is the intersection of competing interests of employees and employers. It is the intersection of competing systems of law: contract law and trust law. It is a matter of huge public concern and the response of the legal system will be a major factor in determining whether private pensions thrive and flourish or die...

It is up to the legal profession, the legal academics and the judiciary to forge the way ahead and to develop a framework in which problems can be resolved without recourse to the courts. Development of a coherent set of flexible principles and their meaningful application is a challenge that will span the next decade at least.

**Eileen E Gillespie (now Justice Gillespie)**  

In this, the age of superannuation, this thesis strives to achieve two objectives. The first is to contribute a flexible set of principles to assess and guide the development of superannuation law – the superannuation relationship framework ("SRF"). The second is to demonstrate the meaningful application of the SRF to the tensions and conflicts that arise in the regulation of superannuation and its underlying legal relationships.

To these ends, this thesis first outlines the regulation of superannuation in Australia and in four comparator jurisdictions: the United Kingdom, Ontario, New Zealand and Hong Kong. In each jurisdiction the focus is upon the bodies of law that interact together to provide a core basis of regulation: trust, statute and contract. **First** addressed were the basic components of each legislative regime. **Secondly**, attention turned to the legislative impact of each regime on the constituent features of the trust relationship. **Finally**, the tripartite interaction between the statute, trust and employment was considered.

The following chapter proposed the SRF and considered justifications for its two core features: preference of trust principle, and structured flexibility. A prominent feature of this chapter was the adoption of a process of regulatory analysis. The results of this process justified not only the preference for trust principle; it ultimately gave substance to the second limb exceptions of the SRF.

Finally, the proposed framework was applied to a selection of areas where the interaction between the foundational bodies of law gives rise to friction. In the interaction of legislative regimes with trust principle, the position of the trustee was of primary interest. To this end, the capacity and constitution of trustees was discussed with particular focus on the proposed universal licensing regime. Analysis was then directed to the fundamental
duties of trustees. Regarding the interaction of trust with the employment relationship, first addressed was the pervasive notion of interpretation and its application to the areas of surplus and amendment. Finally, attention turned to the proper role of employer and trustee.

7.2 SYNTHESIS AND CONCLUSIONS

7.2.1 SUPERANNUATION RELATIONSHIP FRAMEWORK – FOUNDATIONS

Priority of the Trust and Preference of Trust Principle

At the heart of the SRF is the priority of the trust and preference of trust principles. The first limb of the SRF directs the use of trust principles in priority to all other principles of law for the settlement of any issues arising in the context of a superannuation fund. The justification for this preference rests upon the results of a process of regulatory analysis. This process is premised upon the notion that the success of a system of regulation is a function of the suitability of the mechanism chosen to achieve the regulatory objectives. Both in a legislative context, and at general law, the purpose of superannuation provision is ultimately the delivery of benefits upon retirement and probably also in the event of death or disability. Fundamental to this purpose is security and protection of the relevant fund.

It follows that the protective attributes ingrained in the trust relationship justifies its choice and preference. The very structure of the trust relationship – the duality of ownership – creates a shield against insolvency protection. Moreover, the trustee as legal owner is invested with the role of protector requiring the trustee to act in the best and exclusive interests of the beneficiaries. Finally, the trust’s hybrid in personam and in rem characteristics dictates that not only can the trustee be held responsible for breaches of trust but the property of the trust itself can be followed into the hand of anyone except a bona fide purchaser for value without notice. The alternative mechanisms of contract and company are fundamentally directed towards different ends. Each embraces the pursuance of profit and self-interest. Also, in the absence of a segregated fund there is no insolvency protection, the remedy of tracing may not attach, and there is no designated protector or guardian.
This regulatory analysis outcome is further confirmed by the expressed industry preference for the trust mechanism, and the choice of the trust as the superannuation vehicle in each of jurisdictions canvassed by this thesis.

**Structured Flexibility – The Exception Limbs**

In view of the trust being the *preferred* rather than the *perfect* vehicle, the SRF permits the relegation of trust principle when either of the exceptions constituting the second limb apply: (i) that the use of trust principles denies the fulfilment of a main objective of superannuation; or (ii) that the rationale underlying the relevant trust principle is redundant in the context of superannuation.

The concept of protection and security not only dictates the choice of the trust but also gives substance to these exceptions. The process of regulatory analysis identifies prudential security as the justification for regulatory intervention in the marketplace. In other words, an unregulated market fails to achieve what the government views as an important superannuation policy objective, namely, the prudential security of funds. Moreover, independently of legislation, in the fulfilment of the stated purpose of superannuation and pension trusts – to provide superannuation and related benefits to beneficiaries – security and protection is essential. The main objective of the first exception is thus prudential security or protection. It must be understood, however, that security and protection is not an absolute concept; it does not embody a form of guarantee. Instead, its essence is that of minimising risk: systemic risk, agency risk, operational risk and investment risk.

Regarding the inapplicability exception, logic dictates that, where the rationale for a rule does not apply, nor does the rule itself. Once that conclusion is drawn, the concepts of prudential security and protection inform the choice of replacement or alternative principles.

**7.2.2 SUPERANNUATION RELATIONSHIP FRAMEWORK – APPLICATION**

The utility of the SRF is that it provides a framework for analysis against which current statutory provisions, new legislative initiatives and the reasoning of the judiciary can be analysed in areas where the interaction of the underlying bodies of law produces tension or conflict. Also, as the trust is argued to be the most suitable vehicle but not the perfect vehicle, the SRF also directs attention to the suitability of various trust principles in their application to superannuation.
In this thesis the SRF was applied to issues arising from the two principal interactions underlying superannuation law: that between trust and legislation; and that between trust and the employment relationship. The first inquiry was whether or not the relevant statutory or general law principles, or proposed principles, are those applied generally in respect of trusts. If so, the first limb was satisfied. If not, an assessment followed as to whether or not the variation in principle could be justified on the basis of either the protective (or prudential security) limb, or the inapplicability limb, of the SRF.

Three themes emerged from the foregoing assessment: the ownership of the trust fund; the role of the trustee; and the role of the employer.

**Ownership: Interpretation, Distributions of Surplus and Amendment**

*General Law*

That the superannuation trust arises against the background of a contractual (employment) relationship has led some to characterise the underlying interests of the stakeholders according to what are perceived to be contractual foundations. The argument is that because contributions arise from the contractual relationship, ownership of the fund should be adjudged according to contractual foundations. This issue has surfaced particularly in the context of the interpretation of trust instruments, the amendment of trust instruments, and the management of surplus funds.

Consistent with the first limb of the SRF, there is little evidence of departure from general trust principle in the judicial interpretation of the superannuation trust instrument. Courts have specifically eschewed general notions of contractual ownership, preferring instead “to construe the document without any predisposition as to the correct philosophical approach”. Two prominent principles of interpretation have emerged for construing the words of the instrument: that the courts’ approach should be practical and purposive; and that the constituent documents should be construed against their factual matrix. The latter in turn requires consideration of the fact that superannuation funds are established against the background of employment and so must be interpreted against that background; beneficiaries are not volunteers, their rights have contractual and commercial origins, and have been earned by their service under contracts of employment. However, the judiciary

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has warned that these principles are not to be regarded as special rules of construction. This warning is particularly apposite in respect of the factual matrix approach. Although it appears overtly contractual, the principle applies to trusts as it does to other documents the intention behind which is sought.

Nor can it be said that the two main principles of construction have been employed as a de facto means of importing contractual notions of ownership. For example:

- **Actuarial Surplus**: In determining whether or not an actuarial surplus can be reduced by contribution holidays or payment to the employer, the words of the trust instrument have proven conclusive. An investigation of the nature of the employer's funding obligation and the role of the actuary in calculating the appropriate contribution rate determines the availability of a contribution holiday, whereas payment out to the employer requires an express power to that effect.

- **Realised Surplus**: In this context the courts have utilised the general law presumption of resulting trust to fill any gaps in beneficial ownership. Rather than deferring to competing contractual notions of ownership to determine the source of contributions, judges have prioritised the nature of the particular trust at hand by tracing the source(s) and use of contributions within the fund.

- **Amendment**: A consistent theme in the interpretation of amendment powers has been the use of the purposive approach. At a superficial level it can easily be argued that, as the purpose of the trust is to provide benefits, any amendment inconsistent with that purpose is invalid. Proponents of the contractual view argue that this is in line with the notion that benefits are deferred pay and thus the deed should be interpreted on this basis. While it is true to state that superannuation and pension funds are held generally for the benefit of employees, the judiciary has indicated that the extent of that holding and the precise substratum of a trust will be defined by reference to the specific provisions of the trust, for it is these that reveal the intent of the settlor.

**Role of the Trustee**

The trustee as legal owner of the superannuation trust fund is the central responsible entity in the trust relationship. Equity ascribes its strictest obligations in respect of this role. Indeed, the duty of trustees to act entirely and exclusively in the interests of beneficiaries without regard to their own (or other) interests is a core protective feature of the trust.

**Interaction of Trust and Statute**

A particular strength of the *Superannuation Industry (Supervision) Act 1993* (Cth) ("SIS Act"), in its interaction with trust principles, is that it reinforces the position and role of trustee. In the pursuit of this purpose, the SIS Act departs from general principles by circumscribing the freedom of the creator of the trust, thereby limiting the flexibility of the trust. Yet such departure is, generally speaking, not only justified but necessitated on the basis of the prudential security and protection limb of the SRF. Examples canvassed in this thesis include:
Disqualified Persons: The disqualified person provisions of the SIS Act expressly limit the general law eligibility for trusteeship. The prudential security limb justifies this limitation on the basis that these provisions reduce the risk of fraud and mismanagement by disqualifying persons who have shown themselves to be dishonest, incapable of managing their financial affairs, or who have previously committed a sufficiently serious breach of the SIS Act.

Representative Trusteeship: In requiring equal representation in employer-sponsored funds, the SIS Act limits the general law freedom of the settlor to constitute the trustee as he or she thinks fit. Described as a potent force of prudential supervision, this departure from the general law is justified in that it seeks to foster prudential security through the minimisation of agency risk. In preventing the employer from unilaterally acting as trustee, the rules provide a direct control on the actions of the employer and its representatives, and alleviate the risk that the interests of the employer will be preferred to those of the members.

Universal Licensing Regime: The proposed universal licensing regime anticipates that the Australian Prudential Regulation Authority ("APRA") will license all trustees. This is turn requires trustees to comply with the criteria for obtaining a licence and any conditions accompanying approval. As a significant departure from general law principles, the proposed regime has the potential to facilitate greater prudential security than presently achieved under the SIS Act. The interests of prudential security, and therefore the SRF, will be served if trustees are assessed for their capacity, capability and suitability for the trustee function. Moreover, its risk-dominated framework encapsulates the very essence of prudential security. However, the ability to achieve these prudential security objectives rests upon successful implementation and effective regulatory supervision.

Covenants: The SIS Act s 52 covenants seek, with the exception of the standard of care, to reinforce the fundamental duties of trustees. As the covenants are implied into the governing rules of every superannuation entity without modification, the SIS Act curbs the settlor's freedom at general law to modify such duties. Justified on the basis of the prudential security limb of the SRF, the risk that general law standards could be lowered is negated.

Despite these advances for the cause of prudential security, two weaknesses surfaced. First, a consistent theme throughout Chapter 5 was the need for specialised education and training of trustees. This is not to say that the present system is at grave risk but that the introduction of compulsory specialist training would add to the prudential strength of the universal licensing regime and the system of representative trusteeship. Secondly, neither the prudential security nor inapplicability limbs of the SRF justify a lowering of the standard of care applicable to trustees. Covenant (f) of the SIS Act s 52(2) requires trustees to exercise their powers and duties in accordance with standards of ordinary prudence rather than the general law standard of the ordinary prudent business person. Instead, the SRF necessitates a standard, similar to that implemented Hong Kong and currently under review in the United Kingdom, that: (i) is specifically directed towards persons familiar with the operation of superannuation schemes; and (ii) holds professional trustees to a higher standard, namely the knowledge and skill that they have or ought reasonably to be expected to have because of their profession or business.
Interaction of Trust and the Employment Relationship

In light of the distinctive nature of a superannuation scheme, particularly the ongoing involvement of the employer in the typical defined benefit scheme, it has been suggested that the trustee's role and duty be modified at general law by reference to the tripartite nature of the superannuation arrangement. In short, this would require the trustee to act fairly with respect to the participants in the scheme, including the employer. It was concluded that the principles underlying the SRF preclude any development in the law that lessens the absolute nature of the trustee's duty to beneficiaries. Any reformulation of the trustee's role in this respect is fundamentally inconsistent with the juristic nature of this "best interests duty" and ultimately undermines the protective features of the trust. This is not to say that employers' interests can never be considered or that the trustee should seek to frustrate the reasonable objectives of the employer, but that such consideration is qualified and bounded by the best interests of the beneficiaries.

Application to Existing Trust Principle

Trustees, though under a duty to account to beneficiaries, are protected in the exercise of their discretion by not being bound to disclose the reasons actuating their decisions. Principally on the basis of the inapplicability limb of the SRF, the thesis maintains that the general law "no reasons" rule should be relaxed in the superannuation context, if not if the general commercial context. This is because the justifications for its imposition expounded in Re Londonderry's Settlement do not apply in the superannuation context, or even in the general commercial sphere. Its relaxation would also assist to protect and secure to beneficiaries their right of due administration of the trust; currently there is little that assists beneficiaries in the review of trustee action. The most effective manner of implementation is statutory intervention. As such, it is tentatively recommended that the implied trustee covenants in SIS Act s 52(2) be modified to confer a direct right on beneficiaries to access the reasons for trustees' discretionary decisions relating to them.

Role of the Employer

As the employer's role in the superannuation context is ongoing, the proper role of the employer in relation to both trustees and beneficiaries must be addressed. Tension in this respect may particularly be apparent when a trust deed confers wide powers upon the

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2 [1965] 1 Ch 918.
sponsoring employer, permitting effective control of the trust. Concerned with undue influence and control, the judiciary has sought to fetter any power conferred on the employer, in this context via an implied obligation of good faith. Emanating from general principles of contract law, this implied obligation arises not only in contract but operates to modify the powers and discretions conferred on the employer by the trust instrument. Thus, regardless of the intent of the settlor to confer absolute power on the employer, the implied contractual obligation may fetter and limit the employer's actions. Specifically, it prevents the exercise of a power for collateral and improper purposes, compels the employer to consider the exercise of its powers, and restrains a unilateral pursuit of the employer's own interests without regard to the employees' "legitimate expectations". This elevation of contractual principle over and above the settlor's freedom to frame the terms of the trust as he or she sees fit can in part be justified under the protective limb of the SRF. It protects against the removal of existing rights and expectations, and prevents the employer from exercising its power for a collateral purpose. But to the extent that the legitimate expectation concept has the potential to transform a mere expectancy into something more akin to a right, it falls outside the parameters of the SRF.

Despite this justifiable departure from trust principle, it is recommended that the general law eschew these contract law notions in favour of the equitable doctrine of fraud on power. This doctrine likewise restrains employers' actions, but has the added advantage of being based in a well-established area of equity jurisprudence traditionally applied to trusts, and thus preserves and promotes trust principle.

The role of the employer has also come to the attention of all legislatures canvassed by this thesis. In Australia, the power of the employer has been expressly limited by:

- requiring equal representation of employer and employee representatives;
- mandating that the trustee consent to the exercise of an employer's discretion conferred by the trust instrument;
- prohibiting the employer from directing the trustee; and
- imposing conditions for the repatriation of surplus to the employer.

Although these provisions limit the settlor's general freedom, all are necessitated by the protective limb of the SRF. Unbounded employer control and influence generates significant agency risk: that the interests of the employer are not aligned with those of beneficiaries, creating a risk that the employer's interests will be preferred.

Despite the existing protections, three aspects would further strengthen the Australian regime. First, although not specifically related to the role of the employer, the approach adopted in Ontario of requiring the trust deed to specifically address the issue of surplus,
and the specification of accompanying rules of construction, would add certainty to the interpretation of trust provisions. This has the advantage of reinforcing the general law principle that for payment to be made out to the employer, an express power is required.

Secondly, specific regulator involvement in the process of repatriation of surplus to the employer could be considered as a further safeguard. In this respect, Australia is the only regime that permits payment out of surplus without express regulatory consent.

Finally, to the extent, if any, that the surplus repayment provision (SIS Act s 117(5)) can be interpreted to require the trustee to balance the interests of the employer and the members, for the reasons discussed above in respect of the role of the trustee, it represents an unjustifiable departure from general trust principle. A better approach is that in the United Kingdom, where the trustee’s duty to act in the best interests of the beneficiaries is statutorily reinforced specifically in relation to the payment of surplus out to the employer.

7.3 **SPECIFIC RECOMMENDATIONS**

In addition to justifying the role and basis of the SRF and demonstrating its application, the foregoing synthesis not only highlights legislative initiatives and general law principles and trends that are consistent with the SRF, but also identifies areas that could be prudentially enhanced. To further strengthen the prudential foundations of the superannuation regime in Australia, the following specific recommendations flow from the above conclusions.

**Recommendation No 1**

It is recommended that the standard of care incorporated in the SIS s 52(2)(f) be modified to incorporate a standard similar to that applicable under the *Managed Investments Act* 1998 (Cth) and the MPF regime in Hong Kong, and under review in the United Kingdom. This would require:

- trustees to exercise that care, skill, diligence and prudence to be reasonably expected of a person administering a superannuation scheme and who is familiar with the operation of such a scheme; and
- trustees to use in the administration of the scheme all knowledge and skill that they have, or ought reasonably to be expected to have, because of their profession or business.
Recommendation No 2

It is recommended that the SIS Act require trustees (and their directors) to undertake accredited specialised trustee training. This could be implemented through the “fitness and propriety standard” of the current universal licensing regime proposal.

Recommendation No 3

It is recommended that an additional covenant be included in the SIS Act s 52(a) requiring trustees to:

- record reasons for their exercise of discretion; and
- subject to confidentiality restraints, make such reasons available, upon request, to interested beneficiaries.

The purpose of the term “interested beneficiaries” is to limit access to reasons to those beneficiaries: (i) in respect of whom the decision was made; or (ii) who suffer direct financial detriment as a result of the decision.

Recommendation No 4

It is recommended that, for the purpose controlling the exercise of any power conferred on the employer, the general law eschew the implied obligation of good faith in favour of the equitable doctrine of fraud on a power.

Recommendation No 5

It is recommended that the governing rules of all superannuation schemes be required to expressly address the management of actuarial and realised surpluses. Concomitantly, it is also recommended that consideration be given to statutorily prescribing rules of construction regarding the powers to repatriate surplus. For example, in Ontario, where a fund’s governing rules do not provide for the withdrawal of surplus money while it continues in existence, it is statutorily required that the plan be construed to prohibit any such withdrawal.

Recommendation No 6

It is recommended that consideration be given to prescribing specific regulator involvement in the process of repatriation of surplus to the employer. Of those regimes the subject of this thesis, Australia is presently the only one that permits payment out of surplus without express regulatory consent.

Recommendation No 7

It is recommended that, in respect of the decision to repatriate surplus to the employer, the SIS Act s 257(3)(e)(ii) be amended to expressly require trustees to act in the best interests of beneficiaries rather than requiring the trustee to balance the interests of the employer and the beneficiaries.
7.4 **OTHER JURISDICTIONS**

A strength of the Australian superannuation regime is the extent to which it promotes and protects the role of the trustee. It is tentatively suggested that the other jurisdictions canvassed in this thesis could benefit from Australia's experience in this respect. To this end, it is suggested:

- **Equal Representation:** That: (i) New Zealand and Hong Kong consider the implementation of member representation at trustee level; (ii) the United Kingdom and Ontario (in respect of the latter's pension committees) consider increasing member representation to 50 per cent; and (iii) in conjunction with member representation, Ontario, New Zealand and Hong Kong consider provisions that protect member representatives from employer victimisation.

- **Barriers to Entry – Disqualified Persons:** That New Zealand and Ontario consider the enactment of provisions that disqualify undesirable persons from acting as trustees (or directors of trustees).

- **Employer control:** That each of the jurisdictions in question consider limiting the role of the employer by prohibiting employer direction of the trustee and requiring trustee consent to the exercise of employer discretion in relation to the superannuation scheme. The Ontario regulatory regime, in permitting the employer to unilaterally manage the pension plan, is particularly susceptible to risk arising from conflicts of interest. Compulsory member representation could provide an antidote.

These recommendations must be viewed against the constraint of the local culture of regulation in each respective jurisdiction. This may be so particularly in those jurisdictions that do not embrace the compulsory collection of superannuation contributions. Where superannuation and pension provision is at the employer's discretion, to shift the balance of control further away from the employer may generate the undesired result of decreasing the attractiveness of making provision for employees in their retirement.
7.5 THE FUTURE

This thesis makes no attempt to be exhaustive within its general topic area. Rather, it may provide a springboard for future research and the application of the SRF to various other areas of friction. These may include trustee conflicts of interest, the duty of impartiality, the underlying general basis for the review of trustee decisions, the appropriateness of importing the concept of legitimate expectations, the scope of trustee exculpation clauses, and the selection of avenues for fund investment, to name a few. The SRF may also apply outside of the parameters of this thesis in respect of other bodies of law that impact upon trust principles and the trust relationship in the superannuation context. The impact of corporations law and taxation law may, to this end, present areas for research. Finally, the superannuation area is one in which detailed empirical research into the effectiveness of prudential controls is lacking. Such research would further inform the application of the SRF and ultimately assist legislatures and regulators.

7.6 CONCLUDING REMARK

The Australian superannuation regulatory regime, in both its statutory and general law aspects, is a strong proponent of the trust. Yet most statutorily imposed modifications of trust principle serve to curb the trust's inherent flexibility and to reinforce the ideals of equity. In the interests of prudential security this is entirely appropriate and, to borrow a phrase coined by Lord Millett, it avoids the danger of letting the "pension scheme tail wag the trust law dog".3