

Trustees Under Threat

The downturn in the economy, in particular falling investment returns, means we are starting to see a rise in attacks on trustees by disappointed beneficiaries for the management of the trust funds and, more specifically, the delegation of discretionary investment powers to specialist advisers. In the good years of upwards only investment growth beneficiaries may have had little reason to challenge investment performance but having enjoyed and expected hitherto stable growth and income returns, they now face declining or negative returns, and the challenges to the trustees' actions in earlier years, and in the recent market turmoil are now growing shrill.

Under the Trustee Act 2000 trustees can delegate their asset management functions to third party investment managers. However, trustees cannot wash their hands of their duties to:

- Understand the source of their power of investment;
- Develop appropriate criteria (for suitability and diversification of the investments);
- To act fairly between beneficiaries - to balance the income and the capital growth;
- Obtain expert advice on investments;
- Delegate investment management with a written policy statement to guide the agent's exercise of powers; and
- Supervise their investment managers/adviser (to review the delegation and its operation and the asset management policy statement).

Even if no challenge can be mounted against the trustees directly, there may still be claims against the trust advisers in negligence for their advice and/or failure to monitor investments or comply with the investment scheme prescribed by the trustees.

Of particular concern are those trustees who have not regularly reviewed investments schemes or regularly or adequately supervised their advisers, or where they have over-weighted investments in certain sectors or asset classes (e.g. the Icelandic banks).

For bank-tied or bank-owned trustees and investment managers we are likely to see claims by beneficiaries attacking the cosy relationships between the trust companies and their investment managers on grounds of conflict of interest. Such claims could tie-in with the trustee duty to disclose circumstances which might cause a trustee to exercise

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discretionary trust powers improperly. Whilst it is difficult to prove loss from such a breach of duty it can be used as a 'lever' to negotiate with trustees for their removal. Of course failure to monitor investment performance and the trust's advisers will be a key consideration and the records of trustee meetings, showing whether supervisory duties have been complied with will be relevant. Ultimately any potential for a claim in negligence against advisers may cause some awkward relationship challenges because trustee duties include a duty to sue for recovery of losses to the trust fund if those losses are a result of their investment manager's failures.

Another area for concern may be if banks have lent to trustees - 'the leveraged asset' class of investment. Banks are now calling in their loans and, if trustees sell to realise the borrowing, they may face challenges from the beneficiaries that they failed to act in their best interests. Much will of course depend upon the exact facts.

Of course the courts will not expect trustees to be able to crystal-ball gaze into the future, but when reports in the financial media were circulating well in advance of certain businesses' problems it might be expected that trustees should have taken a more cautious approach to their investments.

In uncertain times one certainty is that more claims of this type will be made.

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