

DISCRETIONARY TRUSTS AND POWERS OF APPOINTMENT : PROGRESSIVE ASSIMILATION

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The distinction between trusts and powers as juridical concepts remains clear. However, during the second half of the twentieth century, the courts have been required to consider those concepts in the context of funds established for the benefit of employees and other large groups. The result has been that, although it is still possible to assert the conceptual distinction between trust and powers, the practical significance of that distinction has been progressively eroded. The purpose of this article is to examine these developments relating to the trust/power dichotomy, culminating in the recent decision in *Mettoy Pension Trustees Ltd v Evans*.¹

I. THE CONCEPTUAL FRAMEWORK : THE GIFT/POWER/TRUST SPECTRUM

1. Primary concepts

When one person transfers property to another person, in the majority of cases, the transferor intends to make, and does make, an outright transfer of the property to the transferee. The transferor does not retain any interest in the property, nor does he purport to tell the transferee how to deal with the property. The transferee has the property to do with as he pleases. However, the present article is concerned with those cases where the transferor transfers the property to the transferee, or more commonly transferees, on terms that the transferees will deal with the property in a particular way – ultimately for the benefit of some other person or persons (the beneficiaries). The nature of the terms on which the transferees hold the property can vary greatly according to what may be termed the “degree of compulsion” imposed upon the transferees; but essentially, the terms will involve, sometimes alone but increasingly in combination, trusts and powers.

For present purposes, a trust involves the situation where the transferor (the “settlor”) transfers property to the transferees (the “trustees”) so that the trustees hold the legal title to the property. However, they are under a duty, enforced by equity, to manage the property so as to produce benefit (which usually means to invest the property so as to produce income); and they are under the further duty to divert that benefit to other persons (the “beneficiaries” of the trust). The essence of the trust is the *duty* on the trustees: the trustees *must* carry out the trust in accordance with the terms imposed by the settlor.

From the point of view of the trustees, the trust, at least in its ultimate form of the fixed trust, is the very antithesis of an outright transfer: the trustees of a fixed trust are subject to the ultimate degree of compulsion. The settlor has fixed the beneficial or equitable interests which the beneficiaries are to receive, or at least the means of calculating those interests.²

* This article is an expanded version of a lecture delivered at the University of Canterbury in September 1992.

1 [1990] 1 WLR 1587, [1991] 2 All ER 513.

2 A fixed trust is created where the settlor provides within the trust instrument itself a complete answer to the questions as to who is entitled to what, and when. For example, “\$100,000 on

The trustees have no part in determining those interests; they have no function other than to distribute the trust property in accordance with the determination of the settlor; they are being used by the settlor simply as a means of diverting the benefit of the property to the true transferees, the beneficiaries.³ The point is further emphasized by the nature of the interests of the beneficiaries under a fixed trust. Each beneficiary is the owner of a specific interest in the trust property; and collectively the beneficiaries own the entire trust property so that, in accordance with the so-called principle in *Saunders v Vautier*,⁴ if those beneficiaries are all adult and under no legal disability, they can combine together to terminate the trust and distribute the trust property among themselves.

Thus, in terms of the degrees of compulsion that can be imposed on transferees of property, outright transfers constitute the limit at one end of the spectrum (because they involve no compulsion at all on the transferees) and fixed trusts constitute the limit at the other end of the spectrum (because they involve the greatest possible degree of compulsion). Between these two extremes of the spectrum, the territory is occupied by powers and trust/power combinations.

Of the primary concepts, the nature of a power remains to be considered. A power is an authorisation given to a person to take certain action affecting property in circumstances where that person is not absolutely entitled to that property or even where that person has no interest at all in that property. The concept of a power in this sense embraces a wide variety of administrative powers;⁵ but the present discussion is concerned rather with the dispositive type of power, namely the power of appointment, which authorises the donee of the power to dispose of the settlor's property by "appointing" it to another person or persons as beneficiaries.⁶ However, in common with the discretionary nature of all powers, the essential feature of a power of appointment is that the donee of the power is merely *authorised* to appoint the property to one or more of the beneficiaries *without being under a duty to do so*.

From the point of view of the donee of a power of appointment, the only restriction *inherent in the power itself* is that, if he decides to exercise the power, he must keep within the terms of the power and appoint only to persons within the specified class of potential beneficiaries.⁷ From the point of view of the potential beneficiaries of a power of appointment, two propositions may be asserted, each of which follows logically from the essential principle that a power does not have to be exercised: first, an individual potential beneficiary owns nothing unless and until an appointment is made in his favour; second (and in contrast with the position under a trust and with the principle in *Saunders v Vautier*), the potential benefi-

trust for A for life, remainder to B" or "\$100,000 on trust for my children in equal shares". Although in the second example the quantum of each child's interest is dependent upon the total number of children (since each child will receive a per capita share of the \$100,000) and the settlor may produce more children, the settlor has fixed the means of calculating those interests.

3 The trustees of a fixed trust may have some discretion but only in the context of their administrative duties and powers, for example in relation to the investment of the trust fund.

4 (1841) 4 Beav 115; affirmed Cr & Ph 240, 10 LJ Ch 354.

5 Examples are the powers of trustees in relation to delegation and investment.

6 For example, "\$100,000 to A for life, remainder to whomsoever A may appoint" (where the donee of the power also has a limited interest in the property); "\$100,000 to such of X's children as A may appoint" (where the donee of the power has no interest in the property).

7 The question whether the donee of a power of appointment is subject to any other duties is discussed below.

ciaries under a power of appointment cannot combine together and claim the property for themselves.⁸

Conceptually, therefore, trusts and powers are clearly distinguishable. Trusts are imperative: the trustees *must* carry out the duties or obligations imposed by the trust; powers are discretionary: the donee of a power *may* exercise the power, or not, as he chooses.

2. Trust/power combinations

The trust/power distinction is blurred by the fact that the terms of a trust may give considerable discretion to the trustees. Most importantly, trustees may be given a discretion to select beneficiaries from a specified class, or to determine the proportions in which specified beneficiaries are to take. This is the basis of the discretionary trust, which combines the characteristics of both trusts and powers. As in the case of a fixed trust, the trustees of a discretionary trust have a duty to distribute the trust property among the specified class of beneficiaries;⁹ but, as in the case of a power of appointment, the trustees of a discretionary trust have a discretion to select which members of the class of potential beneficiaries shall actually benefit. However, the predominant characteristic is the trust element. The discretionary trust is in the final analysis a trust, and the trustees have an obligation to carry out the terms of the trust. Thus, whereas the donees of a power of appointment can choose not to exercise their discretion and not to select beneficiaries, because they have no duty to do so, the trustees under a discretionary trust have no such choice – they do have an obligation to exercise their discretion and to select beneficiaries after proper consideration. For only then have they carried out the trust.¹⁰

It might appear to be possible simply to add discretionary trusts at some appropriate point on the spectrum between powers and trusts; but the position is not quite so straightforward.

(a) *Burrough-type and Baden-type discretionary trusts*¹¹

The term “discretionary trust” does not have a single or exhaustive meaning. First, it is used apparently interchangeably with a number of other terms such as “trust power”, “power in the nature of a trust” and “power coupled with a trust”. Second, each of these terms has been used, without any apparent consistency, to denote two (but it is submitted only two) distinct types of trust/power combination. The difference becomes apparent when the courts are required to remedy the failure on the part of the trustees to carry out their duty to make a selection from among the class of potential beneficiaries. For, where the court is called upon to execute the trust, sometimes the court will order that the trust property be divided equally among all the members of the class of potential beneficiaries and sometimes the court will order some other division of the trust property.

The first approach is exemplified by the case of *Burrough v Philcox*,¹² where a settlor directed that certain property should be held on trust for his two children for life and that, in the events which happened, the survivor of the two children “shall have power to dispose of [the property] amongst

8 These propositions were confirmed by the House of Lords in *Vestey v IRC* (No 2) [1980] AC 1148.

9 Subject to the distinction between exhaustive and non-exhaustive discretionary trusts discussed below.

10 See, for example, *Re Locker's Settlement Trusts* [1977] 1 WLR 1323, [1978] 1 All ER 216, discussed below.

11 The terminology was adopted by Emery (1982) 98 LQR 551.

12 (1840) 5 My & Cr 72, 41 ER 299.

[the settlor's] nephews and nieces or their children, either all to one of them, or to as many of them as [the] surviving child shall think proper". Notwithstanding the apparent terminology of powers, the court inferred a general intention on the part of the settlor to benefit the class of potential beneficiaries as a whole and held that the disposition in favour of the nephews and nieces created a discretionary trust;¹³ and that, since the surviving child, as trustee of that discretionary trust, had failed to carry out the trust, it was for the court to do so. In deciding how to execute the trust, the court again attached particular significance to the general intention of the settlor: in effect the trustee had been directed to distribute to one or some *or all* members of the class; and in default of selection by the trustee it was appropriate to order that the trust property be divided equally among all members of the class. It has been argued that the courts are likely to adopt this first approach to unexecuted discretionary trusts where the class of beneficiaries is small in number, and even more so where the class comprises members of the settlor's family.

On the other hand, there are cases of unexecuted discretionary trusts where equal division of the trust fund would clearly be wholly inappropriate. Equal division is likely to be inappropriate in the case of a company benefit fund, involving a substantial number of potential beneficiaries, as exemplified by *McPhail v Doulton (Re Baden (No 1))*.¹⁴ The settlor transferred property to trustees, to "apply the net income of the fund in making at their absolute discretion grants to or for the benefit of any of the officers and employees or ex-officers or ex-employees of the company or to any relatives or dependants of any such persons in such amounts at such times and on such conditions (if any) as they think fit". In the circumstances of such a discretionary trust,¹⁵ to quote the words of Lord Wilberforce:¹⁶

As a matter of reason, to hold that a principle of equal division applies is certainly paradoxical. Equal division is surely the last thing the settlor ever intended; equal division among all may, probably would, produce a result beneficial to none. Why suppose that the court would lend itself to a whimsical execution?

Thus, if the trustees failed to carry out their duty of selection and distribution, the court would normally infer an intention on the part of the settlor that the trustees should distribute to one or some but *not* all members of the class. Equal division of the trust property would therefore not accord with the settlor's intention and the court would adopt some other means to

13 Where the terms of a disposition are prima facie compatible with either a discretionary trust or a power of appointment, the inclusion of a gift over in default of selection and distribution precludes the characterisation of the disposition as a discretionary trust: see, for example, *Re Hay's Settlement Trusts* [1982] 1 WLR 202, [1981] 3 All ER 786, and below n 49; but there is no "inflexible and artificial rule of construction" in favour of a discretionary trust where there is no gift over in default of selection and distribution: *Re Combe* [1925] Ch 210, 216. Compare *Burrough v Philcox* with *Re Weekes' Settlement* [1897] 1 Ch 289.

14 [1971] AC 424.

15 The first issue in the case was whether the settlor had created a discretionary trust or a power of appointment. In its terms, the deed in this case (rather more than in *Burrough v Philcox*) seemed to point to a discretionary trust. However, both Goff J at first instance ([1967] 1 WLR 1457) and a majority of the Court of Appeal ([1969] 2 Ch 388) held that the provision created a power of appointment. Harman and Karminski LJ based their decision expressly on the basis that, as the law then stood on the requirements as to certainty of objects, such a decision gave the settlor's scheme a chance of survival; by contrast, to have decided that the provision created a discretionary trust would have been to condemn the scheme to certain failure. The House of Lords held that the provision created a discretionary trust but proceeded to re-examine (and alter) the requirements as to certainty of objects: see below.

16 [1971] AC 424, 451.

ensure a more appropriate distribution of the trust property that would accord with the settlor's intention.

(b) Exhaustive and non-exhaustive discretionary trusts

The trust/power distinction is further blurred by the fact that a discretionary trust may be "exhaustive" or "nonexhaustive". An exhaustive discretionary trust requires the trustees to distribute the whole of the income arising in any year (or other period): their duty to exercise their discretion can only be satisfied by making an exhaustive distribution. That is the traditional discretionary trust. However, most modern large-scale discretionary trusts are in fact non-exhaustive in so far as the settlor gives the trustees power not to distribute all of the income arising, where, for example, he gives them a power to accumulate all or part of the income for a certain period. That was in fact the position in *McPhail v Doulton*.¹⁷ This further distinction prompts two questions: first, wherein lies the difference between a non-exhaustive discretionary trust and a power of appointment? and, second, assuming that there is a difference and assuming that a non-exhaustive discretionary trust is properly characterised as a trust, what is the precise duty imposed upon the trustees of a nonexhaustive discretionary trust?

The theoretical answer to those two questions appears to be that, as with exhaustive discretionary trusts, so with nonexhaustive discretionary trusts there is a duty to exercise the discretion and that provides the point of distinction from powers of appointment; but that, in the case of non-exhaustive discretionary trusts, the duty to exercise the discretion may be satisfied by a *positive decision* on the part of the trustees to accumulate rather than distribute income.¹⁸

In practical terms, however, that answer may be less than satisfactory. As Lord Wilberforce commented in *McPhail v Doulton*:¹⁹

It is striking how narrow and in a sense artificial is the distinction, in cases such as the present, between [discretionary trusts]²⁰ and powers. It is only necessary to read the learned judgments in the Court of Appeal to see what to one mind may appear as a power of distribution coupled with a trust to dispose of the undistributed surplus, by accumulation or otherwise, may to another appear as a trust for distribution coupled with a power to withhold a portion and accumulate or otherwise dispose of it. A layman and, I suspect, also a logician would find it hard to understand what difference there is.

Notwithstanding these variations within the discretionary trust concept, the interests of the potential beneficiaries under a discretionary trust are essentially similar. Since the trustees of a discretionary trust have a discretion to select some and not others to benefit from the distribution of the trust property, it must follow that, as in the case of a power of appointment, no individual member of the class has an interest in any part of the trust property unless and until the trustees exercise their discretion in his favour.²¹ On the other hand, the overriding duty on the part of the

¹⁷ It is not suggested that *Burrough*-type and *Baden*-type discretionary trusts are necessarily exhaustive and non-exhaustive respectively; but the desire for maximum flexibility in *Baden*-type discretionary trusts tends to be reflected in the inclusion of a power of accumulation.

¹⁸ Some commentators have taken the view that there is no longer any analytical distinction between discretionary trusts and powers: see Davies (1970) ASCL 187; Grbich (1974) 37 MLR 643. Harris (1971) 87 LQR 31 seeks to resolve the perceived difficulties by characterising the duty of discretionary trustees as a rule-based duty with no necessity for correlative rights in the potential beneficiaries.

¹⁹ [1971] AC 424, 448.

²⁰ Lord Wilberforce used the term "trust powers" throughout his speech.

²¹ It was this factor that prompted the use of discretionary trusts as a potentially effective mechanism for the mitigation of tax liability; but changes in tax policy and legislation in the

trustees to execute the trust by distributing and/or accumulating the trust property means that the class of potential beneficiaries collectively owns the trust property – so that, as in the case of a fixed trust, if they are all adult and not under any legal disability, they may combine together to terminate the trust and distribute the trust property among themselves. However, in identifying the “class of potential beneficiaries” for these purposes it may be necessary to distinguish between exhaustive and non-exhaustive discretionary trusts: in the case of the former the class comprises the range of beneficiaries from whom the trustees must select;²² in the case of the latter the class would presumably include in addition any beneficiaries (potentially) entitled under the accumulation provision.

II. DISCRETIONARY TRUSTS AND POWERS OF APPOINTMENT: RECENT DEVELOPMENTS AND CURRENT PRACTICAL ISSUES

Although the conceptual distinction between trusts and powers remains, in practice the distinction has to a significant extent been obscured as a result of the modern exploitation of the large-scale discretionary trust and the complex combination of trusts and powers within the same trust deed. The legal developments discussed in this article have not taken place exclusively in the commercial context;²³ but it has probably been the increased use of the trust machinery in that context that has provided the catalyst for those developments. In particular, there has been a growing tendency for employers to establish pension funds and other employee benefit schemes, which use the trust machinery but which confer wide discretionary powers of selection and distribution on the trustees.²⁴

However, prior to the decision of the House of Lords in *McPhail v Doulton*, the conceptual distinction between trusts and powers continued to have an impact in the context of discretionary trusts and powers of appointment in two important respects. First, the requirements of certainty of objects (and thus validity) were stricter for trusts (including discretionary trusts) than for powers of appointment. Second, as indicated above, the consequences of the failure to execute a discretionary trust or to exercise a power of appointment were different: the potential beneficiaries under a discretionary trust were entitled to the trust property whereas the potential beneficiaries under a power of appointment were not.

In *McPhail v Doulton* the House of Lords reviewed the requirements of certainty of objects in relation to discretionary trusts. It was well established that, in the case of a *fixed* trust for a class of beneficiaries, the trustees or the court (in the event of the failure on the part of the trustees to execute the trust) required a complete list of all the members of the class: otherwise the trust could not be executed. The imposition of the same “list certainty” requirement in the case of discretionary trusts had been confirmed in *IRC v Broadway Cottages Trust*;²⁵ but almost immediately the courts began to

United Kingdom have to some extent reduced the effectiveness (for that purpose) of large-scale discretionary trusts.

²² *Re Smith* [1928] Ch 915; *Re Nelson* [1928] Ch 926; *Vestey v IRC (No 2)* [1980] AC 1148.

²³ See, for example, *Re Hay's Settlement Trusts* [1982] 1 WLR 202, [1981] 3 All ER 786.

²⁴ *Re Gestetner Settlement* [1953] Ch 672 is usually cited as the first reported case involving consideration of the trust/power distinction in the context of such schemes.

²⁵ [1955] Ch 20. The “list certainty” requirement as applied to discretionary trusts was formulated in *Re Ogden* [1933] Ch 678. In *Re Gestetner Settlement*, Harman J supported its application to *Baden*-type discretionary trusts: [1953] Ch 672, 686; but he later expressed regret for the “absurd and embarrassing result” stemming from that decision: *Re Baden's Deed Trust* [1968] 2 Ch 388, 397.

express misgivings²⁶ and to suggest that discretionary trusts should be subject instead to the less strict “criterion certainty” requirement, which was applicable to powers.²⁷ In *Re Gulbenkian’s Settlements*, Lord Upjohn expressed his support for the “list certainty” requirement in the case of discretionary trusts²⁸ but in *McPhail v Doulton* a bare majority of the House of Lords rejected that requirement and substituted a “criterion certainty” test, “similar” to that formulated for powers of appointment, namely that a discretionary trust is valid “if it can be said with certainty that any given individual is or is not a member of the class”.²⁹

The House of Lords had to deal with two main arguments in favour of the stricter “list certainty” requirement. The first argument, that the court, if called upon to execute the trust, could do so only by equal division of the trust property among all the beneficiaries, has been considered above: Lord Wilberforce effectively said that in the context of *Baden*-type discretionary trusts the court would never order equal division, or indeed any division of the trust property that involved giving something to *all* potential beneficiaries. It followed that a complete list of the potential beneficiaries would be unnecessary.³⁰ According to the second argument, even if not all members of the class are to benefit, all members of the class are entitled to be *considered* and for that purpose the trustees still require a complete list of the potential beneficiaries.³¹ Lord Wilberforce responded:³²

[A] trustee with a duty to distribute, particularly among a very large class, would surely never require the preparation of a complete list of names, which anyhow would tell him little that he needs to know. He would examine the field by class and category; might indeed make diligent and careful inquiries, depending on how much money he had to give away and the means at his disposal, as to the composition and needs of particular categories and of individuals within them; decide upon certain priorities and proportions, and then select individuals according to their needs or qualifications. If he acts in this manner can it really be said that he is not carrying out the trust?

Differences there certainly are between [discretionary trusts] and powers, but as regards validity, should they be so great as that in one case complete, or practically complete, ascertainment is needed, but not in the other? Such distinction as there is would seem to lie in the extent of the survey which the trustee is required to carry out: if he has to distribute the whole of a fund’s income, he must necessarily make a wider and more systematic survey than if his duty is expressed in terms of a power to make grants. But just as, in the case of a power, it is possible to underestimate the fiduciary obligation on the trustee to whom it is given,³³ so, in the case of a [discretionary trust], the danger lies in overstating what the trustee requires to know or to inquire into before he can properly execute his trust. The difference may be one of degree rather than of principle

26 See, for example, *Re Hain’s Settlement* [1961] 1 WLR 440, 447, [1961] 1 All ER 848, 853 per Lord Evershed MR; *Re Saxone Shoe Co Ltd’s Trust Deed* [1962] 1 WLR 943, 955-956, [1962] 2 All ER 904, 914 per Cross J.; *Re Gulbenkian’s Settlements* [1968] Ch 126, 134 per Lord Denning MR.

27 The imposition of different requirements to schemes which are intended to achieve essentially similar purposes but which are artificially distinguished by constructional niceties produces some anomalous results: compare *Re Sayer* [1957] Ch 423 and *Re Saxone Shoe Co Ltd’s Trust Deed* [1962] 1 WLR 943, [1962] 2 All ER 904.

28 [1970] AC 508, 524.

29 [1971] AC 424, 456. For the application of the test to the facts of *McPhail v Doulton*, see *Re Baden’s Deed Trusts (No 2)* [1973] Ch 9. For a detailed analysis of the requirements as to certainty of objects, see Emery (1982) 98 LQR 551.

30 It is generally accepted that a complete list of the beneficiaries is still required in the case of fixed trusts; and it is submitted that the same reasoning is equally applicable to *Burrough*-type discretionary trusts.

31 This seemed to be the view of Lord Upjohn in *Re Gulbenkian’s Settlements* [1970] AC 508, 524.

32 [1971] AC 424, 449.

33 See below.

Since the decision of the House of Lords in *McPhail v Doulton*, there has been a significant shifting of the spotlight, away from the interests of the potential beneficiaries in the event of a failure of selection and distribution, towards the duties of the trustees during the operational period of discretionary trusts and powers of appointment and towards the remedies available to enforce those duties. This examination of the duties of trustees has been prompted both in response to the somewhat inconclusive statement of Lord Wilberforce quoted above (and indeed the whole tenor of the decision in *McPhail v Doulton*) and also in response to the increasing incidence of powers of appointment conferred on trustees. The practical importance of the distinction between Baden-type discretionary trusts and powers of appointment now lies in the duties imposed on the trustees of discretionary trusts as compared with those imposed on trustee-donees of powers of appointment, for example how far they are required to consider the claims of potential beneficiaries; and the importance of the distinction lies also in the remedies available to potential beneficiaries under discretionary trusts as compared with those of potential beneficiaries under powers of appointment.

III. DISCRETIONARY TRUSTS AND POWERS OF APPOINTMENT: DUTIES OF TRUSTEE

1. Discretionary trusts

As suggested above the generic duty of the trustees of discretionary trusts is the duty to exercise their discretion. In the case of exhaustive discretionary trusts, that duty can only be satisfied by making an exhaustive distribution; but, in the case of non-exhaustive discretionary trusts, the duty may be satisfied by the trustees deciding to accumulate rather than distribute income.

The point is illustrated by *Re Locker's Settlement*.³⁴ The terms of a discretionary trust required the trustees to apply the income for charitable purposes or among the class of beneficiaries as the trustees "shall in their absolute discretion determine". In response to the expressed wishes of the settlor, the trustees did not make any distributions of income from 1965 to 1968 and they accumulated the undistributed income. In 1975 the question arose as to what should be done with that income and, in particular, whether the trustees' discretion had expired. Goulding J held that the discretion still continued, and that the duty of the trustees to exercise that discretion still continued, which, in the context of an exhaustive discretionary trust, required the distribution of the accumulated income to persons selected from those persons who were members of the class of potential beneficiaries in the relevant years.³⁵

However, in order to carry out that duty of selection, the trustees have a prior duty to survey the class. The elaboration of that duty by Lord Wilberforce in *McPhail v Doulton* has been quoted above. Lord Wilberforce summarised by referring to the need of trustees "to make such a survey of the range of objects or possible beneficiaries as will enable them to carry out their fiduciary duty".³⁶ In *Re Baden (No 2)*³⁷ Sachs LJ referred to the comments of Lord Wilberforce and said:³⁸

³⁴ [1977] 1 WLR 1323, [1978] 1 All ER 216.

³⁵ *Ibid* at 1325-1326 and 218-219.

³⁶ [1971] AC 424, 457.

³⁷ [1973] Ch 9.

³⁸ *Ibid* at 20.

In modern trusts of the category now under consideration it may be sufficient to know whether the range of potential postulants runs into respectively dozens, hundreds, thousands, tens of thousands or even hundreds of thousands. ... [The passage from the speech of Lord Wilberforce] refers to something quite different to [sic] a need to provide a list of individuals or to provide a closely accurate enumeration of the numbers in the class: it relates to that width of the field from which beneficiaries may be drawn and which the trustees should have in mind so that they can adapt to it their methods of discretionary selection. Assessing in a businesslike way “the size of the problem” is what the trustees are called on to do.

And in *Re Hay's Settlement Trusts*, although the case involved a power of appointment, Megarry V-C ventured a “modest degree of amplification and exegesis”:³⁹

The trustee must not simply proceed to exercise the power in favour of such of the objects as happen to be at hand or claim his attention. He must first consider what persons or classes of persons are objects of the power within the definition in the settlement or will. In doing this, there is no need to compile a complete list of the objects, or even to make an accurate assessment of the number of them: what is needed is an appreciation of the width of the field, and thus whether a selection is to be made merely from a dozen or, instead, from thousands or millions. ... Only when the trustee has applied his mind to “the size of the problem” should he then consider in individual cases whether, in relation to other possible claimants, a particular grant is appropriate.

2. Powers of appointment

It is now clear that, in identifying the duties of the donees of powers of appointment, a distinction must be made between those powers which may be termed bare or personal powers and those which may be termed fiduciary powers.⁴⁰ In the first category the donees of powers of appointment have no other powers or duties in relation to the property in question: for example, a settlor may transfer property to trustees on trust for his grandchildren, but he may make the entitlement of the grandchildren under the trust subject to a power conferred on his brother to appoint the property among a specified class of persons which may or may not include the settlor's grandchildren. In such circumstances, the donee of the power of appointment is an individual who is unfettered by any of the fiduciary duties which attach to trustees. It is submitted that, in respect of such bare or personal powers of appointment, there is support for following propositions:

- (a) As emphasised above, it is in the nature of a power that the donee of the power is under no obligation to exercise that power: he has a discretion to exercise it, or not, as he chooses.
- (b) Moreover, because the power is conferred on the donee in a personal, nonfiduciary capacity, the donee can do with it what he pleases. He is under no obligation even to consider periodically whether to exercise the power: he can determine simply to ignore it. If he does decide to exercise it, he can do so without considering the competing claims as between potential beneficiaries of the power, or, in the context of the above example, as between, on the one hand, potential beneficiaries of the power and, on the other hand, the grandchildren who would take the property under the trust if he failed to exercise his power.

³⁹ [1982] 1 WLR 202, 209-210, [1981] 3 All ER 786, 792-793. Megarry V-C also ventured to correct the punctuation and the syntax of the judgment of Sachs LJ in *Re Baden (No 2)*.

⁴⁰ For express recognition of the distinction, see *Re Wills' Trust Deeds* [1964] Ch 219.

- (c) The only restrictions on the donee appear to be that if he does decide to exercise the power, he must keep within the terms of the power and only appoint to persons within the specified class of potential beneficiaries.⁴¹

Until relatively recently, it was asserted that those same propositions were equally applicable where the donees of powers of appointment were also trustees, for example where trustees of certain property were given a power of appointment which was exercisable in respect of the same property.

The proposition that such trustee-donees might owe any legally enforceable duty to the potential beneficiaries (save that of not appointing to persons outside the specified class) received support from Harman J in *Re Gestetner Settlement*,⁴² from Cross J in *Re Abrahams' Will Trusts*⁴³ and from Lord Reid in *Re Gulbenkian's Settlements*,⁴⁴ but in the latter case Lord Upjohn twice asserted that donees of powers of appointment, *whether trustees or not*, owe no positive duties to the potential beneficiaries of the power.⁴⁵ On the other hand, in *McPhail v Doulton*, Lord Wilberforce characterised as a "complete misdescription" the proposition that the duties of trustee-donees were confined to not appointing to persons outside the specified class; and he intimated, albeit in somewhat guarded terms, that trustee-donees owed the more positive duties of survey and consideration.⁴⁶

These positive duties were more fully explained by Templeman J in *Re Manisty's Settlement*⁴⁷ and by Megarry V-C in *Re Hay's Settlement Trusts*.⁴⁸ In the latter case, the settlement provided that "the trustees shall hold the trust fund on trust for such persons as the trustees shall appoint ... and in default of such appointment in trust for the nieces and nephews of the settlor."⁴⁹

In circumstances such as these, where the donees of the power are also trustees, although the power itself remains merely permissive and discretionary, so that it does not have to be exercised, the donees of the power *because they are trustees* must act in relation to that power in accordance with the fiduciary obligations which are inherent in their trusteeship. The obligations arise not from the power but from the office of trustee.

According to Megarry VC, what may appear to be the paradox of obligations attached to discretions resolves itself in the following way:

That brings me to ... the extent of the fiduciary obligations of trustees who have a mere power vested in them, and how far the court exercises control over them in relation to that power.

41 See *Re Hay's Settlement Trusts* [1982] 1 WLR 202, 209, [1981] 3 All ER 786, 792.

42 [1953] Ch 672, 688.

43 [1969] 1 Ch 463, 474.

44 [1970] AC 508, 518.

45 *Ibid* at 521 and 524-525.

46 [1971] AC 424, 449.

47 [1974] Ch 17, 25-26.

48 [1982] 1 WLR 202, 209-210, [1981] 3 All ER 786, 792-793.

49 The wording of that disposition may appear to be somewhat misleading. Under the first part property is given to trustees expressly *on trust* for such persons as the trustees *shall* select, which words seem to suggest a trust. However, the deed goes on to provide that in default of an appointment under the first part the property is to be held on trust for the nieces and nephews of the settlor. The very existence of that trust in default indicates that the settlor herself contemplated the possibility that the trustees might not make an appointment under the first part of the deed. Since the settlor contemplated and made provision for such a possibility, it is logically inconsistent to say that the first part of the deed created a trust because a trust involves a *duty* to distribute the trust property. Thus the first part of the deed created a discretionary power of appointment.

In the case of a trust, of course, the trustee is bound to execute it, and, if he does not, the court will see to its execution. A mere power is very different. Normally the trustee is not bound to exercise it, and the court will not compel him to do so. That, however, does not mean that he can simply fold his hands and ignore it, for normally he must from time to time consider whether or not to exercise the power, and the court may direct him to do this.

When he does exercise the power, he must of course (as in the case of all trusts and powers) confine himself to what is authorised, and not go beyond it. But that is not the only restriction. Whereas a person who is not in a fiduciary position is free to exercise the power in any way that he wishes, unhampered by an fiduciary duties, a trustee to whom, as such, a power is given is bound by the duties of his office in exercising that power to do so in a responsible manner according to its purpose. It is not enough for him to refrain from acting capriciously; he must do more. He must “make such a survey of the range of objects or possible beneficiaries” as will enable him to carry out his fiduciary duty. He must find out “the permissible area of selection and then consider responsibly, in individual cases, whether a contemplated beneficiary was within the power and whether, in relation to other possible claimants, a particular grant was appropriate”.⁵⁰

...
How is the duty of making a responsible survey and selection to be carried out in the absence of any complete list of objects? This question was considered by the Court of Appeal in *Re Baden (No.2)*. That case was concerned with a discretionary trust and not a mere power; but plainly the requirements for a mere power cannot be more stringent than those for a discretionary trust.⁵¹

Megarry V-C then ventured his “modest degree of amplification and exegesis” quoted above and summarised:

[T]he duties of a trustee which are specific to a mere power seem to be threefold. Apart from the obvious duty of obeying the trust instrument, and in particular of making no appointment that is not authorised by it, the trustee must, first, consider periodically whether or not he should exercise the power; second, consider the range of objects of the power; and third, consider the appropriateness of individual appointments. I do not assert that this list is exhaustive; but as the authorities stand⁵² it seems to me to include the essentials

Thus, although the power remains a power and, as such, the trustees have no duty to exercise it and cannot be compelled to exercise it, the trustees *as trustees* nonetheless have duties in relation to the power – in particular, a positive duty to consider whether or not to exercise it.

The status of these duties of trustees in relation to powers of appointment were further considered in *Turner v Turner*,⁵³ where the court declared invalid the purported exercise of the power in question. The trustees had effectively left all the decision making to the settlor (who was not one of the trustees). The court held that they had failed to consider the exercise of the power and the appropriateness of the appointments made; and, in accordance with the principles laid down by Megarry VC in *Re Hay's Settlement Trusts*, that amounted to a clear breach of their duties as trustees.

It is clear that the intervention of the court was based upon the breach by the trustee-donees of their fiduciary duty, and not upon the entitlement of (any of) the potential beneficiaries under the power of appointment. Nonetheless, in the light of the content of the duties of trustee-donees as identified by Megarry V-C, it is arguable that, in the context of large-scale fiduciary powers of appointment, it would be difficult for the trustee-donees

⁵⁰ *McPhail v Doulton* [1971] AC 424, 457, per Lord Wilberforce.

⁵¹ For the duty to survey in the context of a *Baden*-type discretionary trust, see above. In *McPhail v Doulton* Lord Wilberforce had asserted ([1971] AC 424, 457) that “a wider and more comprehensive range of inquiry is called for in the case of [discretionary trusts] than in the case of powers”.

⁵² The authorities referred to by Megarry V-C included *Re Gestetner Settlement* [1953] Ch 672, *Re Gulbenkian's Settlements* [1970] AC 508, *McPhail v Doulton* [1971] AC 424 and *Re Manisty's Settlement* [1974] Ch 17.

⁵³ [1984] Ch 100.

to justify a total failure to distribute any part of the fund. And such a conclusion might be reinforced if the potential beneficiaries were afforded appropriate remedies to enforce the duties of the trustee-donees.

IV. DISCRETIONARY TRUSTS AND POWERS OF APPOINTMENT: ENFORCEMENT OF DUTIES OF TRUSTEES

1. Discretionary trusts

It is clear that where the trustees of a discretionary trust fail to exercise their discretion by selection and distribution,⁵⁴ and thus fail to perform the generic duty inherent in a discretionary trust, the court will ensure its performance.

In the circumstances of *Re Locker's Settlement*:⁵⁵

[W]here the trustees desire to repair their breach of duty, and to make restitution by doing late what they ought to have done early, and they are in no way disabled from doing so, the court should ... permit and encourage them to take that course. A tardy distribution at the discretion of the trustees is, after all, nearer to prompt distribution at the discretion of the trustees, which is what the settlor intended, than tardy distribution at the discretion of someone else.

However, where the trustees are not willing or able to execute the trust, the court will do so. As Lord Wilberforce explained in *McPhail v Doulton*:⁵⁶

[T]he court, if called upon to execute the [discretionary trust], will do so in the manner best calculated to give effect to the settlor's or testator's intentions. It may do so by appointing new trustees, or by authorising or directing representative persons of the classes of beneficiaries to prepare a scheme of distribution, or even, should the proper basis for distribution appear, by itself directing the trustees so to distribute.

2. Powers of appointment

It has always been possible for the potential beneficiaries of a power of appointment to apply to the court for an order restraining the donee from appointing to a person outside the class of potential beneficiaries.⁵⁷ Beyond that, on the basis that the donee of a power of appointment was subject to no duties (save that of not appointing to persons outside the specified class), the distinction between trusts and powers was evident in the potential role of the court. To quote Megarry V-C in *Re Hay's Settlement Trusts*:⁵⁸

In the case of a trust, of course, the trustee is bound to execute it, and, if he does not, the court will see to its execution. A mere power is very different. Normally the trustee is not bound to exercise it, and the court will not compel him to do so.

On the other hand, in the case of powers of appointment conferred on trustees, once it was recognised that the trustee-donees owed duties of survey and consideration similar to those owed by the trustees of discretionary trusts, remedies were required for the enforcement of those duties by the potential beneficiaries. In *Re Manisty's Settlement* it was asserted that "the only right and only remedy" of the potential beneficiaries was the removal of the defaulting trustees and the appointment of replacement trustees;⁵⁹ in *Re Hay's Settlement Trusts*, Megarry V-C stated that the court

54 Subject to the power of accumulation in the case of a non-exhaustive discretionary trust.

55 [1977] 1 WLR 1323, 1325, [1978] 1 All ER 216, 219. For the facts, see above.

56 [1971] AC 424, 457.

57 See *Re Gulbenkian's Settlements* [1970] AC 508, 525; *McPhail v Doulton* [1971] AC 424, 456.

58 Such a remedy is of course available to the (potential) beneficiaries of all trusts and powers.

59 [1982] 1 WLR 202, 209, [1981] 3 All ER 786, 792.

might direct the trustees to carry out their duties;⁶⁰ and, as indicated above, in *Turner v Turner*⁶¹ the purported exercise of a power of appointment was declared void where the trustee-donees had failed to carry out their duties in relation to that power.

Nonetheless there remained a discrepancy between the remedies for the enforcement of the duties of the trustees of discretionary trusts and the remedies available for the enforcement of the duties of the trustee-donees of powers of appointment. It was that discrepancy that came under the spotlight in *Mettoy Pension Trustees Ltd v Evans*.⁶² Mettoy, a well-known British toy manufacturer, had gone into liquidation. Under the much-amended rules of the contributory pension scheme established for the employees, the trustees of the scheme were required to acquire annuities to satisfy the fixed entitlements of the existing and future beneficiaries. In the event of any surplus remaining in the pension fund, the rules included a power to augment the fixed entitlements of the beneficiaries. That power was exercisable at the absolute discretion of Mettoy itself, not the trustees, and any ultimate balance in the fund was to go to Mettoy. After meeting the fixed entitlements, there was in fact a surplus in excess of £9 million. The trustees issued an originating summons seeking directions from the court as to how the surplus fund ought to be administered. The beneficiaries clearly wished to establish that they were entitled to the surplus funds or at least entitled to have their claim to those funds properly considered. Mettoy (or more precisely Mettoy's liquidators) argued that the power to augment the fixed entitlements was entirely discretionary and that there was no obligation to exercise it; that the power could therefore be released, which in turn would activate the gift over in favour of Mettoy; and that the surplus funds would then be available for Mettoy's creditors.

The first task of Warner J was to characterise the discretion in respect of the surplus funds. He adopted a fourfold classification of discretionary powers:

- (i) a power of appointment conferred on a donee with no obligations in relation to that power, save the obligation not to commit a fraud on the power by appointing to a person outside the class of potential beneficiaries;
- (ii) a power of appointment involving fiduciary duties on the part of the donee of the power (referred to by Warner J as a "fiduciary power in the full sense"⁶³);
- (iii) any discretion which is really a duty to form a judgment as to the existence of particular circumstances giving rise to particular consequences; and
- (iv) a discretionary trust where the trustee has a duty to distribute the trust property among the class of potential beneficiaries, although he has a discretion to select which of those beneficiaries actually receive the property and in what shares.

Leaving aside category (iii), which has no relevance to the issues under consideration, that classification follows the spectrum outlined above.

59 [1974] Ch 17, 25, citing Harman J in *Re Gestetner Settlement* [1953] Ch 672, 688.

60 [1982] 1 WLR 202, 209, [1981] 3 All ER 786, 792.

61 [1984] Ch 100.

62 [1990] 1 WLR 1587, [1991] 2 All ER 513.

63 [1990] 1 WLR 1587, 1613-1614, [1991] 2 All ER 513, 545, following the terminology of Chitty J in *Re Somes* [1896] 1 Ch 250, 255.

Since the discretion in the present case was clearly not within the fourth category, the question was whether the case involved a power of appointment within the first or second category. In the words of Warner J:⁶⁴

That depends upon whether the words by which that discretion is expressed to be conferred on [Mettoy] mean in effect no more than that [Mettoy] is free to make gifts out of property of which it is the absolute beneficial owner or whether those words import that [Mettoy] is under a duty to the objects of the discretion to consider whether and if so how the discretion ought to be exercised.

Warner J decided that the power was properly classified as belonging to category (ii) for two principal reasons. First, its classification within category (i) would have rendered any entitlement of the beneficiaries illusory and its inclusion within the pension scheme rules would have been pointless: since Mettoy was certainly entitled to the surplus in default of appointment, the beneficiaries would have been in precisely the same position if Mettoy had been absolutely entitled to the surplus.⁶⁵ Secondly, Warner J emphasized that the beneficiaries under the pension scheme were not volunteers: by a combination of their contributions to the fund and the performance of their contracts of employment they had purchased not only their fixed entitlements but also the right to be considered for discretionary benefits.⁶⁶

However, on the basis of the existing authorities discussed above, the finding that the power of appointment was fiduciary appeared to be largely academic. Although certain duties owed by trustee-donees had been identified, the remedies available for the potential beneficiaries of fiduciary powers of appointment to secure performance of those duties were limited and, in the absence of the appointment of new trustees, were apparently confined to a direction to the existing trustees to carry out their duties.

In the circumstances of *Mettoy* that would have provided an illusory remedy for the beneficiaries because the existing trustees were the Mettoy liquidators. As trustee-donees of the power of appointment, they would have been under a duty to consider exercising the power in favour of the beneficiaries; but, as liquidators, they would have owed a duty to Mettoy's creditors, which would have required them not to exercise the power of appointment with the result that the entitlement of Mettoy in default took effect.

It was in these circumstances that Warner J further assimilated the practical operation of discretionary trusts and powers of appointment conferred on trustees. He cited the passage from Lord Wilberforce in *McPhail v Doulton*:⁶⁷

As to powers, I agree with my noble and learned friend Lord Upjohn in *Re Gulbenkian's Settlements* that although the trustees may, and normally will, be under a fiduciary duty to consider whether or in what way they should exercise their power, the court will not normally compel its exercise. It will intervene if the trustees exceed their powers, and possibly if they

64 [1990] 1 WLR 1587, 1614, [1991] 2 All ER 513, 546.

65 [1990] 1 WLR 1587, 1615-1616, [1991] 2 All ER 513, 547. Warner J referred, with obvious approval, to *Re Courage Group's Pension Schemes* ([1987] 1 WLR 495, [1987] 1 All ER 528), where the classification of an analogous power within category (ii) precluded a "take-over raider" from asset-stripping the pension fund of the target company.

66 [1990] 1 WLR 1587, 1618-1620, [1991] 2 All ER 513, 549-551. Warner J disagreed with the view of Millett J in *Re Courage Group's Pension Schemes* ([1987] 1 WLR 495, 514-515, [1987] 1 All ER 528, 545-546) that any surplus in such pension funds arises from overfunding by the employer and thus belongs morally to the employer.

67 [1971] AC 424, 457.

are proved to have exercised it capriciously. But in the case of a [discretionary trust], if the trustees do not exercise it, the court will I would venture to amplify this by saying that the court, if called upon to execute the [discretionary trust], will do so in the manner best calculated to give effect to the settlor's or testator's intentions. It may do so by appointing new trustees, or by authorising or directing representative persons of the classes of beneficiaries to prepare a scheme of distribution, or even, should the proper basis for distribution appear, by itself directing the trustees so to distribute. The books give many instances where this has been done and I see no reason in principle why they should not do so in the modern field of discretionary trusts

Despite the clear distinction that Lord Wilberforce draws between the remedies available in the context of powers of appointment and discretionary trusts respectively, Warner J concluded that all the remedies available to the potential beneficiaries in the context of discretionary trusts should also be available in the context of fiduciary powers of appointment. In the absence of a request for the appointment of new trustees, he took the view that he was entitled to approve a proposed scheme or even dictate a scheme himself and to that end he invited further argument as to the possible content of such a scheme.

More generally, it is arguably implicit in the approach of Warner J that, as tentatively suggested above, the availability of remedies to enforce the duties of trustee-donees may lead to a greater incidence of distribution among the potential beneficiaries of fiduciary powers of appointment.

V. DISCRETIONARY TRUSTS AND POWERS OF APPOINTMENT: FURTHER IMPLICATIONS

This assimilation in respect of the remedies available in the contexts of discretionary trusts and powers of appointment may have further implications. It is arguable that this development may also involve assimilation between discretionary trusts and powers of appointment in relation to the requirements of certainty of objects. In accordance with what has been termed the "cardinal principle",⁶⁸ the objects of a trust or power must be sufficiently certain to enable the trustees (or, if necessary, the court) to execute the trust in accordance with the settlor's intention. As a result of *McPhail v Doulton*, the same "criterion certainty" requirement for certainty of objects applies to both powers of appointment and *Baden*-type discretionary trusts;⁶⁹ "list certainty" has never been required for powers of appointment and is now no longer required for *Baden*-type discretionary trusts; but discretionary trusts do have to satisfy the additional requirement of administrative workability. In the words of Lord Wilberforce in *McPhail v Doulton*:⁷⁰

There may be a third case where the meaning of the words is clear but the definition of beneficiaries is so hopelessly wide as not to form "anything like a class", so that the trust is administratively unworkable...

Lord Wilberforce suggested, albeit somewhat hesitantly, that a discretionary trust for "all the residents of Greater London" would be void on this ground, but he did not expand on the substance of the requirement of administrative workability.⁷¹ Moreover, even though the decision in *R v*

⁶⁸ Emery (1982) 98 LQR 551.

⁶⁹ Namely, that it must be possible to say with certainty whether any given individual is or is not a member of the class.

⁷⁰ [1971] AC 424, 457.

⁷¹ In *Re Hay's Settlement Trusts* Megarry VC tentatively expressed the view ([1982] 1 WLR 202, 213, [1981] 3 All ER 786, 796) that a discretionary trust for such persons (except a named few)

*District Auditor, ex parte West Yorkshire Metropolitan County Council*⁷² was based on administrative unworkability, that case provides virtually no clarification.⁷³

It has been suggested that the notion relates to the practicability of the execution of the trustees' duties; and that administrative unworkability exists where the settlor has in effect set the trustees an impossible task because the class is so defined that there are no discernible criteria according to which the selection procedure should be approached. Accordingly it is argued that the duty apparently imposed on the trustees is in its nature incapable of enforcement and control by the courts; and that the discretionary trust is therefore void. If this is indeed the substance of administrative unworkability, then in the light of the post-*McPhail v Doulton* developments in relation to fiduciary powers of appointment – the recognition of the duties of trustee-donees and, more particularly, the provision of remedies for the enforcement of those duties – it is arguable that administrative unworkability is, in principle, no less a problem for fiduciary powers of appointment than for discretionary trusts.⁷⁴

VI. CONCLUSION

Trusts and powers remain conceptually distinct; and in their simplest forms – fixed trusts and personal powers of appointment – the imperative/discretionary distinction may also have significant practical importance. However, more recently, the greater incidence of trust/power combinations – particularly Baden-type discretionary trusts and fiduciary powers of appointment – has led to a dramatic reduction in the practical significance of the distinction. First, the requirements as to certainty of objects (and thus initial validity) for Baden-type discretionary trusts and powers of appointment were assimilated in *McPhail v Doulton* (except in relation to the issue of administrative workability); and it is arguable that the decision in *Mettoy* must inevitably result in complete assimilation. Second, although the interests of the potential beneficiaries in the event of a failure of selection and distribution remains a point of distinction, that distinction has, to some considerable extent, been sidelined by the assimilation of the duties of trustees of Baden-type discretionary trusts and of trustee-donees of powers of appointment during the operational period of the trust or power and by the assimilation of the remedies available to enforce those duties. It is submitted that the consequential strengthening of the position of potential beneficiaries under fiduciary powers of appointment and the reiteration of the position of potential beneficiaries under Baden-type discretionary trusts is likely to lead to closer continuing scrutiny of trustees throughout the operational period

as the trustees may select might fail on the same ground, although he too failed to offer any real explanation for that view. See McKay [1974] Conveyancer 269 for a detailed but predictably inconclusive analysis of the notion of administrative unworkability.

⁷² [1986] 26 RVR 24; and see Harpum (1986) 45 CLJ 391.

⁷³ Lloyd LJ asserted that a trust with 2.5 million potential beneficiaries "is quite simply unworkable. The class is far too large". However, the case was heard under the Crown Office List, the point was not fully argued and the relevant authorities were not fully considered.

⁷⁴ Prior to the post-*McPhail v Doulton* developments, in *Blausten v IRC* ([1972] Ch 256) Buckley LJ assumed obiter that the notion of administrative unworkability did apply to powers of appointment, while in *Re Manisty's Settlement* ([1974] Ch 17) Templeman J questioned that conclusion. In *Re Hay's Settlement Trusts* ([1982] 1 WLR 202, [1981] 3 All ER 786) Megarry V-C preferred the latter view. Even if administrative unworkability could invalidate a fiduciary power of appointment, since it did not invalidate the discretionary trust in *McPhail v Doulton*, it is suggested that it would not have posed problems on the facts of *Mettoy*.

of the trust or power; and it has been suggested that that in turn may significantly reduce the incidence of disputes over the entitlement to funds at the end of the operational period. If there is indeed a reduction in the incidence of such disputes, which arguably provide the only remaining context for the application of the strict conceptual trust/power dichotomy, then it may be possible to assert that the courts have acknowledged and addressed the artificial distinction between Baden-type discretionary trusts and fiduciary powers of appointment — a distinction which, according to Lord Wilberforce,⁷⁵ has probably never commended itself to laymen or logicians.

⁷⁵ *McPhail v Doulton* [1971] AC 424, 448.