

In charity we trust:

Charities as potential

beneficiaries of failed

commercial trusts^{*}

The Hon. Justice Clyde Croft¹
Supreme Court of Victoria

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Introduction

Commercial trust instruments, which are not primarily established for charitable purposes, are often drafted to include charities amongst the class of potential beneficiaries. At first glance, this may seem inconsistent with the commercial purpose of these trusts.² Nevertheless, it is not uncommon to find provisions in commercial trusts reserving a power to select amongst charities within the pool of potential beneficiaries, either in the usual course, or upon termination or failure of the trust. In the commercial sphere, this power might be expected to be conferred upon an entity associated with the corporate entity utilising the trust for its own commercial purposes.

The fact that charities are among the class of potential beneficiaries does not change the nature of the trust. The purpose of such a trust is primarily commercial. Nevertheless, this does not mean that the cases concerned with the validity of so called charitable purpose trusts are not relevant. Consequently, regard must be had to Lord Macnaghten's oft-repeated statement in *Pemsel's case* that "charity in its legal sense comprises four principle divisions: trusts for the relief of poverty; trusts for the advancement of education; trusts for the advancement of religion; and trusts for other purposes beneficial to the community, not falling under any of the previous heads".³ Critically, in addition to the requirement that the purpose be

² References to the "commercial purpose" of a trust or a trust for commercial purposes are references to a trust with identifiable beneficiaries, with a commercial function, and not a trust for a purpose, which, of course, must generally be for a charitable purpose; and, consequently, issues do not arise with respect to "mixed" charitable and non-charitable purposes (as to which, see KJ Hardingham, "Trusts including charitable and non-charitable purposes - special statutory provisions" (1973) 47 *ALJ* 698).

³ *Income Tax Special Purposes Commissioner's v Pemsel* [1891] AC 531 (HL) at 572; and see *Royal National and Agricultural and Industrial Association v Chester* (1974) 48 *ALJR* 304 (HL); *Aid/Watch Incorporated v Commissioner of Taxation* [2010] HCA 42 at [13].

charitable, the trust must also serve the “public purpose”.⁴ Thus, for example, a trust to educate employees’ children is invalid, as it is not a valid charitable purpose that serves the public.⁵ It would also follow that a charitable trust for a limited class of individuals, for example, employees of a particular company, would fail as a charitable trust.⁶ In the present context, it should be noted that a gift “to such charitable institutions and objects as my said trustees may determine” has been upheld as a good charitable trust.⁷ So provisions for charity may be specific or non-specific as to the charitable institutions or purposes to which they are directed – provided, of course, they

⁴ There is some debate, and exceptions, to this general principle. For further discussion, see J.D. Heydon and M.J. Leeming, *Jacobs’ Law of Trust in Australia* (LexisNexis Butterworths, 7th ed, 2006) (“Jacobs”) at 142 ([1006]).

⁵ *Oppenheim v Tobacco Securities Trust Co Ltd* [1951] AC 297 (HL) applying *Re Compton* [1945] Ch 123; and see *Thompson v FCT* (1959) 102 CLR 315.

⁶ Thus Ford and Lee commented:

“The *Compton/Oppenheim* rule generated its own problems. It meant that employee benefit funds could not be characterised as charitable trusts; and often they could not be characterised as private trusts because they lacked certainty of beneficiaries under the strict rules for the ascertainment of beneficiaries of private trusts before *McPhail v Doulton*; *Re Baden’s Deed Trusts* [1971] AC 424; [1970] 2 All ER 228; 2 WLR 1110: see [5.8210] ff. They could therefore be without any legal foundation within the law of trusts and as such possibly void with the consequence that their funds would have to be returned to the persons who furnished them. At best they were valid as mere powers, but not enforceable as trusts. It is arguable that one of the consequences of *Compton/Oppenheim* was that it rendered necessary the decision in *McPhail v Doulton*; *Re Baden’s Deed Trusts* [1971] AC 424; [1970] 2 All ER 228; 2 WLR 1110, which modified the rule of certainty of beneficiaries in the case of private trusts, so that employee benefit trusts might be recognised as being within the private trust mechanism and so capable of enforcement. This decision has relieved the law of any necessity to undertake a reconsideration of the *Compton/Oppenheim* rule.

The *Compton/Oppenheim* rule has attracted some judicial misgivings, eg in *Dingle v Turner* [1972] AC 601; 1 All ER 878 per Lord Cross at 623-624 and per Zelling J in *Public Trustee’s Young* (1980) 24 SASR 407 at 414, but it is submitted that it has become embedded” (Thomson Reuters, *Principles of the Law of Trusts*, vol 2 (at 82) [19.650]): see *Dingle v Turner* [1972] AC 601, where a trust for “paying pensions to poor employees” of a company was upheld; thus standing for the proposition that where the trust is for the purpose of the relief of poverty, it is unlikely that a “public” purpose will be required for its validity.

⁷ See *Re Percy* [1898] 1 Ch 565; and see Jacobs at 142 [1062].

are charitable. It may be that the more specific are the provisions of the trust, the less it might be said to indicate a general charitable intention.⁸

The inclusion of charities as potential beneficiaries in commercial trusts is predominantly to avoid the trust failing for want of beneficiaries as, generally, a trust with no beneficiaries, or one expressed to be for a non-charitable purpose, as opposed to being for beneficiaries, will fail.⁹ This “device” may also be used in limited circumstances to avoid the rule against perpetuities in certain jurisdictions; also known as the rule against “remoteness of vesting”. A trustee with a power to appoint could, for example, determine, in the exercise of the trustee’s discretion, to make a distribution to a charitable body if the trust would otherwise fail due to lack of beneficiaries or would otherwise infringe the rule against perpetuities.¹⁰ Nevertheless, the rule against perpetuities will still apply if the trustee exercises the discretion to appoint at a time beyond the period allowed for vesting by the rule. It should, of course, be mentioned that South Australia is a notable exception, as the only jurisdiction in Australia to have abolished this rule.¹¹ Remoteness issues are, of course, more likely to arise with respect to the appointment of capital or residual beneficiaries, rather than with respect to income beneficiaries.

The power to nominate beneficiaries, including charitable beneficiaries, is a fiduciary one, which is properly described as a “power in the nature of a

⁸ See Jacobs at 142 [1068]; a matter which may be relevant to the question whether the court should approve a scheme, general or *cy-près* (see below pp 22 - 26).

⁹ See PW Young, C Croft and ML Smith, *On Equity* (Lawbook Co, 2009) [6.310], 405 (“Young Croft and Smith”); and Ford and Lee, Thomson Reuters, *Principles of the Law of Trusts*, vol 2 (at 78) [19.080]) that “A charitable trust cannot fail for uncertainty of objects or administrative unworkability: the Court will always assist; whereas a private trust may: see, for example, *Commissioner of Stamp Duties (NSW) v Way* (1951) 83 CLR 570 ...”.

¹⁰ NB: Particular classes or types of trusts are excepted by statute from this rule: see for example the *Superannuation Industry (Supervision) Act 1993* (Cth) . Certain trusts for the benefit of employees are also exempted (see Ford & Lee (at 77) [7-10510]).

¹¹ *Law of Property Act 1936* (SA), s 61; and see also section 62 of the *Law of Property Act* which allows applications to be made to courts to vary the terms of a disposition so that unvested interests may vest immediately.

trust”, or a “discretionary trust”.¹² Subject to powers of accumulation, powers such as this impose upon the donee of the power a duty to select from among a class of beneficiaries which of them is to receive a distribution; and, where appropriate, the proportions in which they are to receive the income or capital of the trust.¹³ Where the donee of the power does not exercise that power, or is “absent”, courts will ensure, by one means or another, that the trust is carried into effect; including by exercising the discretion of the donee.¹⁴

The purpose of this paper is to consider these, in a sense, “mixed” commercial purpose and charitable trusts, to which reference has been made, and the consequences of a failure of their commercial purpose. These consequences, in turn, depend very much on the terms of the trust deed or instrument. Broadly, the effect of failure of the commercial purpose may be to provide for a distribution of trust property to charity which can take effect according to the terms of the trust (with or without court assistance, depending on the circumstances). Alternatively, the provision for charity may fail because it is not “charitable” in the technical legal sense or the charitable purpose is clear but for various reasons it can only be implemented by utilizing a “scheme” approved by the court. Finally, there may be no provision made in the trust deed or instrument in the event of the failure of the trust as a result of the failure of its commercial purposes, in which case charity will not figure in the picture.

¹² Dr Geraint Thomas, *Thomas on Powers* (Sweet & Maxwell, 1998), [2-76]ff, citing *Brown v Higgs* (1803) 8 Ves Jr 561, at 570-571.

¹³ *Mettoy Pension Trustees v Evans* [1990] 1 WLR 1587, at 1614.

¹⁴ *In re Baden's Deed Trusts* [1971] AC 424, at 456-457 (Lord Wilberforce); *Mettoy Pension Trustees v Evans* [1990] 1 WLR 1587, at 1617.

Construing the trust instrument

The approach of the courts in construing trust deeds or instruments is epitomized by the statement of Parker J in *Boranga v Flintoff* that:¹⁵

“[i]t is trite that the primary task of construction is to endeavour to discover the intention of the parties from the words of the instrument. If the words used are unambiguous the Court must give effect to them: *Australian Broadcasting Commission v Australian Performing Right Association Ltd* (1973) 129 CLR 99 at 109. The general rule is that evidence of surrounding circumstances is admissible to assist in the interpretation of a deed if the language is ambiguous. But evidence of surrounding circumstances is not admissible to contradict the language when it has a plain meaning: *Codelfa Construction Pty Ltd v State Rail Authority of NSW* (1982) 149 CLR 337 per Mason J at 347; *Southern Resources Ltd v Technomin Australia NL* [1990] WAR 72. This rule is not absolute. Extrinsic evidence is admissible to identify the meaning of a word: *Life Insurance Co of Australia Ltd v Phillips* (1925) 36 CLR 60 at 78; *Southern Resources v Technomin Australia NL* at 84. In particular, evidence of mutually known facts is always admissible even where there is no apparent ambiguity – to prove the meaning of a descriptive term in a written instrument: *Homestate Australia Ltd v Metana Mineral NL* (1994) 11 WAR 435 at 447 and cases cited therein.”

Thus, the primary task of courts is to discern the intention of the settlor from the words of the relevant trust deed or instrument. The relevant time for construing the settlor’s intention is “at the time the deed or instrument was entered into”.¹⁶ Additionally, in construing a trust deed or instrument, its provisions must, like any other deed or instrument, be construed as a whole and an interpretation which does not render provisions or parts of provisions in a written instrument redundant is to be preferred to one which has this result.¹⁷ If the words used are unambiguous, they must be given effect. However, where the words used are ambiguous, evidence of surrounding circumstances is admissible to assist in the interpretation of the trust deed or instrument. If there is such a level of ambiguity that the words cannot be

¹⁵ (1997) 19 WAR 1; having cited and applied the decision of the Full Court of Western Australia in *Clay v Clay* (unreported, Supreme Court Western Australia, 27 March 1996), per Ipp J (Walsh and Anderson JJ concurring) at 5-6, where the authorities were reviewed; and see *Fell v Fell* (1922) 31 CLR 268 at 272-3 (Isaacs J); and *Re Gulbenkian’s Settlement Trusts* [1970] AC 5081 at 522 (Lord Upjohn) (HL).

¹⁶ (1997) 19 WAR 1 at 6.

¹⁷ See Lewison, *The Interpretation of Contracts* (4th ed, 2007), [7.02] and [7.03].

given a meaning, even with reference to such evidence, it may be that the trust will fail for uncertainty at this point.

Employee incentive plans

Perhaps one of the most prominent examples of trusts which name charities or charity, more broadly, as a potential beneficiary or beneficiaries are those utilised in employee incentive schemes. As is no doubt apparent, schemes in which some form of benefit such as shares, rights, securities or cash vests in employees are highly significant commercially. Use of this type of scheme allows employers to guarantee the provision of both short and long-term incentive programs for employees; intended to encourage them to “work harder and stay longer”. This also allows employers to make better strategic management and resourcing decisions, and to influence staffing outcomes in their favour, whilst simultaneously maximising employee performance and return. Employees stand to benefit financially from these schemes, which, if effective, will provide greater incentives for good work performance, and reward longer periods of service to the one employer. As a result, employers also gain through attracting and, particularly, retaining, talented employees, and all the benefits which flow from this.

There is little in the way of case law specifically relating to employee incentive schemes in the present context. This is probably because, unlike the very regulated position applying to employee pension or superannuation schemes, there are generally no special rules applying to employee incentive plans. Instead, the trusts supporting these plans are treated in the same manner as any other trust deed or instrument.

In a case that I recently decided, *Australian Incentive Plan Pty Ltd v Babcock & Brown International Pty Ltd (“Babcock”)*,¹⁸ the focus was on the construction of a

¹⁸ [2010] VSC 564.

trust instrument establishing an employee incentive scheme. The purpose of the trust was to provide incentive arrangements, namely shares or options, as part of employees' overall "compensation" (or remuneration) packages. In furtherance of this purpose, the trustee, a company styled Australian Incentive Plan Pty Ltd, purchased shares in the settlor of the trust, the holding company of the Babcock & Brown group of companies across the globe. The entitlement of employees to such shares under this scheme typically did not vest for at least four years. The trust deed made clear that the employees under this scheme held no beneficial interest unless and until the minimum term of employment was completed. The purpose of the trust, to provide incentive options to employees employed for a defined period of time, was said to have failed when the settlor of the trust, Babcock & Brown International Pty Ltd was placed into liquidation and ceased trading. As a result, the minimum term of employment required for a disbursement under this trust could never be reached by any employee. I make illustrative reference to this set of facts in the remainder of this paper.

Has the commercial purpose of the trust failed?

For the most part, commercial trusts are effected without difficulty and in accordance with their stated terms. Nevertheless, in certain circumstances, the purpose of the trust may fail before this occurs: for example, where the commercial purpose for which the trust was established can no longer be fulfilled.

The commercial purpose of a trust will usually be apparent from the recitals and operative clauses describing or providing for the purpose of the trust. The specific machinery by which this purpose is intended to be achieved must be discerned from the trust deed as a whole. In some circumstances it will be clear that the commercial purpose has failed. In *Babcock* the commercial purpose, to provide incentives to employees, was no longer achievable as

insolvency had overtaken the Babcock & Brown group and there were no longer employees of the relevant beneficiary class or classes.

Settlor's intention: the presumption of resulting trust

Where a trust as a whole fails for any reason, the beneficial interest or interests the subject of the failed trust must pass to someone as equity abhors, and will not tolerate, a vacuum in the equitable ownership.¹⁹ Thus, once it is established to the court's satisfaction that a trust has failed, the court may be asked to determine the fate of the trust property.

The settlor of an apparently failed trust may argue that although there has been a total failure of the trust there was, in any event, an incomplete disposal of the beneficial interest under the trust, thus giving rise to a resulting trust of the beneficial interest in his, her or its favour.²⁰ Resulting trusts of this kind, which arise by operation of law, are, like other resulting trusts, based upon intention presumed from the circumstances.²¹ The following statement in Jacobs is illustrative:²²

“A resulting trust may be presumed upon a disposition of the legal estate without any disposition of the beneficial interest, arising by reason of a mistake or an oversight in the drafting of a document evidencing an express trust or a failure to make provision for the particular contingency which has later occurred. ... [T]he law presumes that, in so far as the settlor or testator has not disposed of the beneficial interest, he or she intended to retain it.”

The settlor may also argue that the inclusion of a discretionary power of appointment in favour of charities in the trust instrument was employed purely to avoid any failure of purpose of the trust for want of beneficiaries or to avoid the rule against perpetuities; consistent with the real purpose of the

¹⁹ Thomas and Hudson, *The Law of Trusts*, 2nd ed (2010), [26.27]. See also Jacobs at 236, [1205]; *James Miller Holdings Ltd. v Graham* (1978) 3 ACLR 604, at 613-614.

²⁰ As to which see Young, Croft and Smith at [6.940]-[6.950], [6.10000]; GE Dal Pont & DRC Chalmers, *Equity and Trusts in Australia* (Fourth Edition, Lawbook Co., 2007) (“Dal Pont”) at [26.15]; Jacobs at [1201]-[1202].

²¹ Ibid.

²² Jacobs at [1202].

trust being entirely commercial, with no intention that it should be charitable. This argument will no doubt be strengthened where part of the beneficial interest has been retained by the settlor, and provide a firmer basis for finding a resulting trust in the settlor's favour. This would tend to suggest that in the case of failure, the settlor would have intended that the trust property revert back. By the same token, where the settlor retains no continuing interest, such a construction is less likely. Nevertheless, a resulting trust will not arise where the settlor has made a clear alternative provision for the "destination" of the whole of the beneficial interest in an express trust in these type of circumstances; a provision which will be given effect to by the courts.²³ It must be noted, however, that an intention to "abandon" the beneficial interest is not lightly to be inferred;²⁴ and that this is particularly the case in the commercial context.

In other words, where the trust can still be carried out and the whole of the trust fund applied to some, or a class of, the potential beneficiaries, it cannot be said that there has been an incomplete disposal of the settlor's interest. For example, again in the employee incentive scheme context, where the trust deed evinces an intention to benefit employees through the incentive scheme, and also an intention to benefit charity in the event of a surplus under the scheme, and there are employees or a charity or charities eligible and able to receive the trust funds, there will be a complete disposition of the beneficial interest originally settled.²⁵ There is no interest remaining to result, beneficially, back to the settlor. The remainder of this paper will explore the manner in which the trust is administered after the failure of the commercial purpose.

²³ Dal Pont at [26.15], [26.35]. *Re Trusts of the Abbott Fund* [1900] 2 Ch 326.

²⁴ Young, Croft and Smith at [6.940], citing *Air Jamaica Ltd v Charlton* [1999] 1 WLR 1399. See also Dal Pont at [28.155].

²⁵ *Babcock* at [32].

Has provision for failure been made?

The recent global financial crisis showed that the conventional wisdom that some corporate entities were 'too big to fail' was deeply flawed. However, the effect of this thinking was that many of the events that led to the failure of corporate entities and trusts associated with them were simply never contemplated. Consequently, there are, in hindsight, many significant drafting "omissions and ambiguities" in trust instruments and other contractual documents as a result of this crisis. The unexpected insolvency of these corporate entities was an event so "unthinkable" that no provision was made to deal with such a contingency. Rather like negotiating dispute resolution provisions at the conclusion of a commercial "deal", it may seem ridiculous, in "poor taste", negative or unenthusiastic for an advising lawyer to raise such a seemingly unlikely spectre. Thus, in many cases no provision for negative contingencies of this nature was made. As a result, it may be necessary for the trustee, the settlor, or any prospective or actual beneficiaries, to seek definitive guidance, including intervention and orders, from the courts.

Where the court determines that the trust, or at least its machinery, has failed, something must be done with the trust assets. If no, or inadequate, provision for failure has been made in the trust deed, the court must decide where the assets are to be distributed. In doing so, it will consider the provisions of the trust deed or instrument, properly construed, the intention of the settlor, and any equitable rights or interests that beneficiaries, whether present or future, may have. The court may then proceed on the basis of its statutory, general law or inherent powers to vary or amend trusts or, in certain circumstances, by approving a scheme under its general jurisdiction or ordering a *cy-près* scheme.

It must be recalled that the type of trusts under consideration in this paper are not primarily charitable trusts. Rather, they are primarily commercial trusts,

with provision for a potential discretionary selection of a charity or charities to receive trust property; either in the usual course or, on the triggering of certain events, the remaining trust property, including the corpus. Consequently, concepts such as charitable “schemes”,²⁶ which apply solely to charitable trusts, are likely to have little utility in the present context except where the provision for charity has failed in itself, as being insufficiently expressed or being specific with respect to a charitable institution which is no longer able to receive the trust property because, for example, it has ceased to exist.

Gift to charity takes effect according to the terms of the trust

On the failure of the commercial purpose of the trust, where it is found that the settlor has no prospect of any beneficial interest arising under a resulting trust, the court must next look to distribution of the trust property. The court is then faced with the difficult task of resolving the issue of proper construction of the trust deed and the distribution of the trust fund; either in favour of one group of beneficiaries over another, or perhaps even in the proportion of distribution between, and within, different classes of beneficiaries. Beneficiaries may include charities.

If the circumstances of failure are the subject of an express stipulation in the provisions of the trust deed or instrument (e.g. “on the liquidation of the company” or “if no beneficiaries remain”, “the residual monies will be distributed equally” or “donated to charity”), the provisions should be able to be applied by the trustee – barring, of course, illegality, or the application of rules such as the rule against perpetuities. On the other hand, where any entitlement is subject to the trustee’s discretion, and the class of potential beneficiaries includes both charities and another class of beneficiaries, both of

²⁶ See, for example, Jacobs at [1068]; and see below pp 22 – 26.

which are still unascertained, there may be potential for argument in relation to the exercise of the power of selection.

Charities as potential beneficiaries under a discretionary trust, or discretionary appointment provisions, may be on equal footing, so to speak, with other potential beneficiaries with respect to trust property in situations such as a failed employee incentive program. This is particularly the case where employees have not contributed to the program in monetary terms and thus have no basis upon which to assert a claim to any interest in the trust property; nor any “entitlement” to any award or payment under such a program – though, of course, they may have “put in the time and effort” as diligent employees. *Babcock* is an example of circumstances such as this. Thus, if, for example, provision is made for a payment to be made to an employee after “5 years of service”, with no beneficial interest arising before then, and the employer company becomes insolvent within that period and so the purpose of the trust cannot be achieved, the then-employee cannot be said to have accrued any entitlement. Consequently, although the trust deed or instrument may provide that the trust was established for the benefit of employees (and the employer), they are in these circumstances placed on an “equal footing” with all other potential beneficiaries, including charities. In circumstances where the members of the employee class cannot be ascertained, for example, if the employer company has become insolvent and no longer has any employees or employees of the relevant class, it may be appropriate to exercise any power of appointment which has been provided for in favour of charity for the benefit of a charitable institution or institutions, rather than see the complete failure of the trust.

Gift to charity, but administrative machinery of the trust has failed

In circumstances where there is an absence of any or a comprehensive and clear provision for the fate of trust property on termination of the trust, courts will endeavour to give the trust deed or instrument efficacy in this respect,

construing it consistently with the settlor's intention insofar as possible; and as far as this can be discerned. In *Babcock*, charities were provided for as a potential beneficiary or beneficiaries on the termination of the trust, but the machinery of the trust did not anticipate the liquidation of the relevant company. In this situation, where there was a clear provision for charity as a potential beneficial purpose on the termination of the trust, the settlor's intention would be defeated if the trust were to be allowed to fail because of an unexpected contingency not catered for in the trust's machinery.

Where the nominating entity cannot act

Where the trust fails or terminates where there are no or inadequate provisions for distribution of the trust property or the nominated person or entity empowered to determine and administer distribution no longer exists or is incapable of acting, the position is more complicated. Where there are potential beneficiaries in these circumstances and the person or entity nominated to exercise the discretion or any power of distribution does not exist, or cannot be constituted in some way (for example, if the trust deed or instrument provides that the nominee is to be the directors of a company that subsequently ceases trading, becomes insolvent and is placed in liquidation), the exercise of this power may depend solely on the exercise of the powers of the court, as a court of equity – stemming from its inherent jurisdiction or pursuant to statute.

The impact of liquidation

As foreshadowed, a problem may arise if the settlor or the donee of the power to select from the class or classes of potential beneficiaries and to administer distribution, is unable to exercise the power as a result of insolvency and consequent liquidation. There is no general principle that all powers formerly exercisable by particular officers of a company are, on the commencement of

its liquidation, transferred to the liquidator.²⁷ It is necessary to look to the terms of the trust deed or instrument and, where relevant, the *Corporations Act* 2001 (Cth) to determine whether the liquidator is able to exercise a particular power. If the trust deed or instrument provides, expressly or impliedly, that on winding up of the company the power is exercisable by the liquidator, this will enable the liquidator to act.²⁸ However, if no such provision is made, it is unlikely a liquidator will be able to exercise such a power. The power is not an asset of the company, and it is not necessary for the liquidator to exercise it in winding up the affairs of the insolvent corporate entity and distributing its property.²⁹

In *Babcock*, for example, it was suggested that it would be open to the liquidator of the insolvent Babcock & Brown entity to exercise the powers of the donee of the power; either to appoint a fresh donee or to act, in effect, in that capacity as the donee of this power. Although a liquidator, in general terms, stands in the shoes of the board of directors of the company of which he or she is liquidator, it does not follow that the liquidator necessarily has capacity to exercise all the powers of the board of directors, in whatever capacity. This was made clear in the judgment of McLelland CJ in Eq in *Butterell v Docker Smith Pty Ltd*³⁰ where his Honour reviewed a number of authorities which establish matters of principle with respect to the differing functions and capacity of a board of directors and a liquidator:³¹

“However, in my opinion there are two reasons why such a term cannot properly be implied in the rules (and in the contracts of insurance incorporating the rules) in the present case. The first is that the winding up of the Society did not render impossible the exercise by the Board of its powers.

²⁷ *Butterell v Docker Smith Pty. Ltd.* (1997) 41 NSWLR 129, at 137; *IACS Pty. Ltd. v Australian Flower Exports Pty Ltd* (1993) 10 ACSR 769, at 772.

²⁸ *Butterell v Docker Smith Pty Ltd* (1997) 41 NSWLR 129, at 136.

²⁹ *Corporations Act* 2001 (Cth), ss. 477(2)(m), 506(1)(b); *Mettoy Pension Trustees v Evans* [1990] 1 WLR 1587, at 1616 (Warner J); *Re William Makin & Sons Ltd.* [1993] BCC 453, at 458-460 (Vinelott J).

³⁰ (1997) 41 NSWLR 129.

³¹ (1997) 41 NSWLR 129 at 137-8.

What it did do was, relevantly, to make the continuance (and therefore the exercise) of any of those powers conditional upon the approval of the committee of inspection (or if there were no such committee, the approval of the creditors) - see s499(4) and cf *Austral Brick Co Pty Ltd v Falgat Constructions Pty Ltd* (1990) 21 NSWLR 389). The second reason is that it is far from obvious that insured members who were willing to subject themselves to the exercise of discretionary powers to impose liabilities on them by the Board, an elected collegiate body the members of which had to have special qualifications (see r4(2)), while the Society was a going concern, would have been willing that, in the event of the liquidation and insolvency of the Society, they be subject to equivalent powers vested in a liquidator, particularly where the funds to be raised by Supplementary Subscription are not necessarily confined to the payment of insurance claims made by insured members, but might extend to 'other expenses or outgoings which in the opinion of [the liquidator] necessarily and properly fall upon the Society in respect of [the relevant] Policy Year' (see r13(1)(A)). These might include liabilities of the Society unrelated to the Scheme.

Reliance was placed by counsel for the liquidator on the decision of Beach J in *Pyramid Building Society v Howell* (1994) 14 ACSR 633. In that case it was held that s 477(2)(d) of the *Corporations Law* empowered a delegate of the liquidator of a building society (to which the relevant provisions of the *Corporations Law* were made applicable) to sign a certificate so as to constitute prima facie evidence of the amount recoverable by the Society under a contract of guarantee for the purposes of a clause in that contract which was expressed to give such an effect to a certificate 'signed under the hand of any Director or Commercial Lending Manager or Loan Administration Manager of the [Society]'. If that decision is to be understood as propounding a general or prima facie principle of the transfer to a liquidator of all powers formerly exercisable by particular officers of a company, then with great respect I am unable to agree with it. Although to say that in a winding up the powers formerly exercisable by company officers are transferred to the liquidator is in a general sense loosely descriptive of what occurs, it is conceptually inaccurate. The office of liquidator is a statutory office, and the liquidator's powers derive solely from the relevant statute, in this case the *Corporations Law*. As Sackville J observed in *Dallhold Investments* at 342:

'Of course the fact that the directors cannot

exercise any powers on behalf of the company does not, of itself, mean that all such powers have vested in the liquidator. The extent of the liquidator's powers must depend upon the powers conferred by the *Corporations Law*.³²

Consequently, where the trust deed or instrument, properly construed, is silent on the effect of insolvency in these circumstances, the discretionary power to distribute to beneficiaries within the class of potential beneficiaries, including any charities, can only be exercised by the court.

Variation of trust deeds or instruments

A trust deed or instrument may itself make a provision for a variation of the trust; but in some circumstances the courts have a power of variation. The power of courts in this respect differs between the States and Territories; although the relevant legislation is, in many respects, similar.³² It must be remembered that whilst courts may vary provisions for the administration or management of a trust, the power to vary beneficial interests is generally quite constrained and exercised sparingly. Indeed, as the authorities highlight, the original statutory provisions for variation were too limited, requiring further amendments to the legislation to increase the court powers

³² *Trusts Act 1973 (Qld)*, s 95(5); *Trustee Act 1936 (SA)*, s 59C; *Variation of Trusts Act 1994 (Tas)*; *Trustee Act 1958 (Vic)*, s 63A; *Trustees Act 1962 (WA)*, s 90(3); *Administration Act 1903 (WA)*. Section 59C of the *Trustee Act 1936 (SA)* is broader than the Victorian provision. In this respect, Ford and Lee [15.230] comment (at p 15-1067):

“The general language of the provision is in far broader terms than the English precedent, which was tailored to the highly particular need to break certain kinds of trusts when it was enacted. The jurisdiction to vary or revoke may be exercised not only on the application of a person who has a vested future or contingent interest in property held on trust, but also on the application of “a trustee”. There is therefore no limitation on the persons upon whose behalf a trustee may apply. The awkward language of the “arrangement” and the “approval of an arrangement” has been dispensed with and insistence on benefit is less precise”

See, also, section 35B of *Trustee Act 1936 (SA)* which allows amendment of a employee benefits fund if the consent of three-fourths of those present at the relevant meeting is obtained.

of variation with respect to beneficial interests.³³ These provisions authorise the court to approve, on behalf of the beneficiaries, “any arrangement (by whomsoever proposed and whether or not there is any other person beneficially interested who is capable of assenting thereto) varying or revoking all or any of the trusts, or enlarging the powers of the trustees of managing or administering any of the property subject to the trust”.³⁴

Section 63A(1)(b) of the Victorian *Trustee Act* confers a power to vary trusts, in the following terms:

“63A. *Power of Court to vary trusts*

(1) Where property, whether real or personal, is held on trusts arising, whether before or after the commencement of this Act, under any will settlement or other disposition, the Court may if it thinks fit by order approve on behalf of-

...

(b) any person (whether ascertained or not) who may become entitled, directly or indirectly, to an interest under the trusts as being at a future date or on the happening of a future event a person of any specified description or a member of any specified class of persons, so however that this paragraph shall not include any person who would be of that description, or a member of that class (as the case may be) if the said date had fallen or the said event had happened at the date of the application to the Court;

...

any arrangement (by whomsoever proposed and whether or not there is any other person beneficially interested who is capable of assenting thereto) varying or revoking all or any of the trusts, or enlarging the powers of the trustees or managing or administering any of the property subject to the trusts: Provided that except by virtue of paragraph (d) of this subsection the Court shall not approve an arrangement on behalf of any person unless the carrying out thereof would be for the benefit of that person.”

³³ See s 63 *Trustee Act* 1958 (Vic); provisions which proved to be too limited and which had been thought, wrongly, to authorise the alteration of the interests of beneficiaries: see *Chapman v Chapman* [1954] AC 429 (HL); and see Jacobs at [1705] [1706] and Ford and Lee [15.050] and [15.060].

³⁴ See s 63A of the *Trustee Act* 1958 (Vic).

In *Babcock*, these provisions were relied upon on behalf of all persons who might be determined to be employees for the purposes of the trust deed for the purpose of an application to vary the termination date of the trust – with the effect of producing an immediate distribution of the trust property. In support of this application, it was submitted that such persons may become entitled to an interest under the trust on the termination of the trust. It was further submitted that the amendment sought was for the benefit of those persons because it would bring forward the termination date of the Trust and thus the date on which distributions may be made to such persons, as the “Residual Beneficiaries”.³⁵

The authorities indicate that the power conferred on the court by s 63A of the Victorian *Trustee Act* and its equivalents is discretionary.³⁶ In considering an application under s 63A of the *Trustee Act*, it is important to keep in mind the nature of the discretionary power conferred upon the court by its provisions.³⁷ This is made very clear in the speech of Lord Reid in *In re Holmden’s Settlement Trusts; Inland Revenue Commissioners v Holmden*³⁸ where, referring to the English *Variation of Trusts Act* 1958 from which the Victorian provisions³⁹ were derived, his Lordship said:⁴⁰

“Under the Variation of Trusts Act the court does not itself amend or vary the trusts of the original settlement. The beneficiaries are not bound by variations because the court has made the variation. Each beneficiary is bound because he has consented to the variation. If he was not of full age when the arrangement was made he is bound because the court was authorised by the Act to approve of it on his behalf and did so by making an order. If he was of full age and did not in fact consent he is not affected by the order of the court and he is

³⁵ The trust deed the subject of *Babcock* defined “residual Beneficiaries” as meaning “Employees and/or charities nominated by the Remuneration Committee from time to time”.

³⁶ *In re Oakes’ Settlement Trusts* [1959] 1 WLR 502; Thomas and Hudson, *The Law of Trusts*, 2nd ed (2010), [24.24].

³⁷ See Ford and Lee, [15.070] to [15.090].

³⁸ [1968] AC 685 (HL); and see *Muhling v Perpetual Trustees WA Ltd* [2001] WASC 225 at [25] (Hasluck J).

³⁹ Ford and Lee, [15.060].

⁴⁰ [1965] AC 685 at 701.

not bound. So the arrangement must be regarded as an arrangement made by the beneficiaries themselves. The court merely acted on behalf of or as representing those beneficiaries who were not in a position to give their own consent and approval.”

There are, however, situations where it has been found appropriate that the trustee or trustees, where there are more than one of them, make application to the court for approval under this variation of trusts legislation. Again in relation to the equivalent English provisions, Russell J said in *In re Druce's Settlement Trusts*:⁴¹

“The application was made not by a beneficiary but by the trustees. This is a disadvantage, particularly in a case such as the present, where the interests of the persons for whom the court is concerned are not exactly the same as those of some respondent. It means that there is no counsel whose sole task is to protect and support those interests. Where the trustees make the application their counsel is there to argue for the acceptance of the scheme: but at the same time his duty and that of the trustees is to be the watchdog for (for example) unborn interests. Let me say at once that Mr Brightman for the trustees, while recognising the disadvantage, overcame admirably the duality of his position. To change the metaphor, his performance as touch judge was not marred by the fact that he started in the line-out, and I was grateful for his assistance. Nevertheless, the disadvantages of this duality exist. Counsel for the applicant trustees must have an instinctive reaction against a criticism from the bench, designed to safeguard or benefit those unborn interests, which would be lacking in a respondent trustee, an instinctive tendency to be against alteration of the scheme for the approval of which he is applying. Moreover, if the criticism be in fact unsound, it is likely to take longer for the judge to be dissuaded from it because of that very duality. There are, of course, cases of applications to vary beneficial interests where it is necessary and proper that the trustees should make the application, notwithstanding the disadvantage I have mentioned. This case was one of them, the trustees being satisfied that the scheme was beneficial to their beneficiaries and no beneficiary being willing to make the application. But, in general, the trustees should not be the applicants in applications to vary beneficial trusts, unless they are satisfied that the proposals are beneficial to the persons interested and have a good prospect of being approved by the court, and further, that if they do not make the application no one will. In particular, it would not be right if it became the general practice for such applications to be made by the trustees upon the supposition that should the application fail it will be more probable (though not, of course, certain) that the costs of all parties will be directed to be met

⁴¹ [1962] 1 WLR 363 at 370-371; and see Ford and Lee, [15.090].

out of the trust funds.”

In the circumstances of *Babcock*, the application under s 63A of the *Trustee Act* was properly brought by the trustee because the persons who might be determined to be entitled as “Residual Beneficiaries” on termination of the trust were not ascertained. They were not ascertained because of the requirement that “Residual Beneficiaries” be nominated by the “Remuneration Committee”, a committee not in existence as a result of the insolvency of Babcock & Brown International Pty Ltd.

The plaintiff submitted that the court must be concerned in considering the exercise of the discretionary power under s 63A of the *Trustee Act* whether the arrangement as a whole is, in all the circumstances, such that it is proper to approve it. In the circumstances of *Babcock*, it was submitted that the proposed variation was for the benefit of all persons and charities who might be appointed as “Residual Beneficiaries”.⁴² In this respect, it was submitted that it was important to distinguish between the amendment proposed, which accelerated the date for termination of the trust, and the power of appointment of “Residual Beneficiaries”. It was submitted that the amendment was plainly for the “benefit” of the whole class, whether considered as a class or as individual beneficiaries, by reason of the bringing forward of the termination date.⁴³ Further, it was submitted that the effect of the proposed variation was not to deprive any member of the class, or any individual of a beneficial interest.⁴⁴ It was said that the court was being asked to make a bargain on behalf of the beneficiaries which was reasonable and (where the class of beneficiaries includes infants) one that an adult would be prepared to make.⁴⁵ The defendants, on the other hand, argued against the

⁴² The variation proposed was, in effect, to add a provision for termination of the trust on the commencement of the winding up of Babcock & Brown Ltd – which marked the insolvency of the Babcock & Brown group and the end of its carrying on business.

⁴³ See Thomas and Hudson, *The Law of Trusts*, 2nd ed (2010), [24.27]ff.

⁴⁴ cf *In re Cohen's Settlements* [1965] 1 WLR 1229.

⁴⁵ *In re Cohen's Settlements* [1965] 1 WLR 1229, at 1236 (Stamp J); *Re Blocksidge* [1997] 1 Qd R 234, at 237-238 (Williams J).

approval of the proposed amendment to the trust deed on the basis, as indicated, that the trust had failed in circumstances where there had not been complete disposal of the beneficial interest. Consequently, it was argued that there was a resulting trust, by operation of law, in favour of the settlor.⁴⁶

It was common ground that the parties did not and would not have anticipated the corporate death of Babcock & Brown group entities and the failure of the extensive businesses conducted by these entities. Consequently, it was said that, in all the circumstances, it would not have been anticipated by the settlor that the situation would ever arise that there was no Remuneration Committee in existence as the donee of the power to nominate “Residual Beneficiaries” or that there would not be a Board of Directors of Babcock & Brown Ltd in existence to act in the place of the Remuneration Committee or to appoint a Remuneration Committee as contemplated under the provisions of the Trust Deed.⁴⁷

Once it was decided that no resulting trust arose, the position was that without an amendment to the trust deed as proposed, the trust fund would be held until the trust terminated under its then existing provisions, in 2084. Evidence was given that, although the trust had been able to be administered at minimal cost as part of the Babcock & Brown group administrative services, this would change as a result of the demise of that enterprise. This would mean that, unless the trust was terminated, the trust fund would need to be managed “externally” at greater expense, with the result that it would likely be extinguished in paying administrative charges prior to its termination in 2084, as a result of effluxion of a great deal of time. Clearly, this situation was not in the interests of any of the potential “Residual Beneficiaries” and, consequently, I was of the opinion that this was an

⁴⁶ The settlor was Babcock & Brown International Pty Ltd.

⁴⁷ See clause 1.1 of the Trust Deed: “Remuneration Committee - means the sub-committee by that name of the board of [Babcock & Brown Ltd] as constituted from time to time and if there is no such sub-committee, then the Board of [Babcock & Brown Ltd]”.

appropriate circumstance to exercise the court's discretion under s 63A of the *Trustee Act* to approve the amendment to the Trust Deed as sought by the plaintiff.

No gift to charity capable of implementation

On the failure of the commercial purpose of the trust, and in the absence of any resulting trust in the settlor's favour, the trust property remains to be distributed or otherwise dealt with. If there are no "residual beneficiaries" provided for and there is no general charitable intent expressed with respect to this residue, the trust will, in all probability, fail utterly. In these circumstances, where all possibilities of finding or conferring beneficial entitlement are exhausted, the trust property will, in most jurisdictions, revert to the Crown as *bona vacantia*; "vacant goods" or ownerless property which passes to the Crown.⁴⁸ In South Australia, however, *The Trustee Act 1936* goes a step further and expressly departs from the general law. Consequently, where a charitable purpose fails the trust property does not become *bona vacantia* as might otherwise be the case; and instead, the *cy-près* doctrine is applicable.⁴⁹ On the other hand, if a charitable purpose is established with respect to the "residue", the court will consider whether effect can be given to this purpose by means of a scheme under its general jurisdiction or by means of a *cy-près* scheme. In the present context, it is not necessary to consider either type of scheme in any detail, beyond their general nature and purpose.

General schemes

As discussed by Jacobs, the court may approve a scheme in the exercise of powers within its general jurisdiction where:⁵⁰

⁴⁸ See *Re Wells* [1933] Ch 29 at 49 (Lawrence LJ); *Re Producers' Defence Fund* [1954] VLR 246 (Smith J); and *Ford and Lee*[21.035].

⁴⁹ See *Trustee Act 1936* (SA) s 69B.

⁵⁰ Jacobs at [1069].

“(1) the mode of executing a charitable gift is originally undefined;

(2) the machinery for ascertaining the objects of a charitable intention fails; or

(3) the machinery for effectuating a charitable intention does not exist or fails.

If the donor has appointed trustees but has merely exhibited a general charitable intention and has omitted to specify any particular purpose, the court will nominate the objects for which the gift is to be applied. In doing so it may have regard to evidence as to the donor’s intentions ...”.

Babcock is an illustration of the application of this jurisdiction in circumstances where the machinery for ascertaining the object or objects of the charitable intention failed as a result of insolvency and commencement of winding up of Babcock & Brown Ltd. Consequently, the entity designated to determine the “Residuary Beneficiaries” had ceased to exist.

Cy-près schemes

A *cy-près* scheme may be appropriate where it is not possible to give effect to the charitable trust according to its terms other than with respect to matters that may be dealt with under a general scheme. This may be due to initial or supervening impossibility. In other words, the charitable purpose provided for may have been uncertain, non-existent or illegal initially, or have become so. Alternatively, the charitable purpose of the trust may have been satisfied or exhausted, leaving a residue of trust property.

In *Corish v Attorney-General’s Department of NSW*,⁵¹ Campbell J described the difference between an administrative scheme and a *cy-près* scheme in the following terms:⁵²

⁵¹ [2006] NSWSC 1219.

⁵² [2006] NSWSC 1219, at [9].

“9. There is a clear conceptual difference between a *cy-près* scheme and an administrative scheme for a charitable trust. It is the difference between ends and means. A *cy-près* scheme ... can be directed when it is impossible or impractical to carry out the objects of the trust in all the details the settlor stipulated. An administrative scheme supplements and/or clarifies any provisions the settlor has stipulated concerning the manner in which the objects of the trust are to be pursued, when practical circumstances show that the settlor’s stipulation (if any) of the means is inadequate or impractical.”

The circumstances in which a *cy-près* scheme may be applied are set out by Jacobs, as follows:⁵³

“In other words, in order for the court to order a *cy-près* scheme, one of the following has to occur:

- (1) there is
 - (a) a case of initial impossibility, and
 - (b) either an out-and-out intention to benefit charity or a general charitable intention plus a possible mode of effectuating that intention; or
- (2) there is a case of supervening impossibility (whether the intention be general or merely particular); or
- (3) there is a case where a trust has exhausted its original purpose (whether the original purpose be particular or general in intent) and a surplus remains. Each of these situations will be dealt with in turn.⁵⁴”

The relevant legislation in South Australia is:⁵⁵

“69B – *Alteration of purposes of charitable trust*

- (1) The purposes for which property is required or permitted to be applied in pursuance of a charitable trust may be altered by a scheme (a *trust variation scheme*) approved under this section in any of the following circumstances:
 - (a) where the original purposes, in whole or in part –
 - (i) have been as far as possible fulfilled; or
 - (ii) cannot be carried out, or not according to the directions given and to the spirit of the gift; or

⁵³ Jacobs at [1070]; referring to Sheridan and Delaney, *The Cy-près Doctrine* [?].

⁵⁴ See generally Sheridan and Delaney, *The Cy-près Doctrine*.

⁵⁵ This provision is reflected in other jurisdictions. See, for example, *Charities Act 1978* (Vic), Part I.

- (b) where the original purposes provide a use for part only of the trust property; or
 - (c) where the trust property could be more effectively used if combined with other property applicable for similar purposes and administered jointly with that property; or
 - (d) where it is not reasonably practicable having regard to—
 - (i) the value of the trust property; or
 - (ii) changes in circumstances that have taken place since the constitution of the trust; or
 - (iii) any other relevant factor,
 to apply the trust property in accordance with the original purposes; or
 - (e) where the original purposes, in whole or in part—
 - (i) have been adequately provided for by other means; or
 - (ii) have ceased to be charitable purposes; or
 - (iii) have ceased to provide a suitable and effective method of using the trust property.
- (2) References in this section to the original purposes of a charitable trust shall be construed, where the purposes for which the trust property is required or permitted to be applied have been altered or regulated by a scheme or otherwise, as referring to the purposes for which the property is for the time being required or permitted to be applied.
- (3) A trust variation scheme may be approved, on the application of the trustee, by—
- (a) the Supreme Court; or
 - (b) if the value of the trust property does not exceed \$300 000 or another limit prescribed by regulation—the Attorney-General.
- (3a) The authority to which the application is made (ie the Supreme Court or the Attorney-General) is referred to in this section as the *relevant authority*.
- ...
- (6) If the relevant authority is satisfied, on application under this section, that the variation of the terms of a trust proposed in a trust variation scheme—
- (a) accords, as far as reasonably practicable, with the spirit of the trust; and
 - (b) is justified in the circumstances of the particular case,

the relevant authority may approve the trust variation scheme and the approved scheme prevails over inconsistent provisions of a relevant instrument or declaration of trust.

- (7) The reasonable costs of an application under this section are payable at the direction of the relevant authority from the trust property.

...”

The general equitable jurisdiction is, however, not displaced, as the specific matters set out in s 69B(1)(a) to (e) are not exhaustive. Nonetheless, the statutory grounds are very broad; consequently, there is little benefit in relying upon the general law.⁵⁶ Nevertheless, under both the general law and these statutory provisions, neither expediency, nor the fact that the trust funds could be applied for a purpose more beneficial to the community is a sufficient basis for a *cy-près* scheme.⁵⁷

Having regard to the definition of “Residual Beneficiaries” in the trust deed the subject of *Babcock*, it was not necessary to resort to a *cy-près* scheme. Nevertheless, there may be circumstances, arising out of the provisions of a trust deed or instrument in a “mixed” commercial purpose and charitable trust where the provisions for charity are specific, rather than the subject of a general discretion. Where more specific provisions of this nature “fail” in the sense described above, a *cy-près* scheme may be appropriate; but always provided there is a clear intention to benefit charity, a generable charitable intent.⁵⁸

⁵⁶ See the comments of Duggan J in *Re Estate of Pitt (deceased)* (2002) 84 SASR 109 at [43] and [44].

⁵⁷ *Trustees of the Kean Memorial Trust Fund v Attorney-General (SA)* (2003) 86 SASR 449 at 463, [55]-[56].

⁵⁸ *Royal North Shore Hospital of Sydney v AG (NSW)* (1938) 60 CLR 396 at 428 (Dixon J); and *AG (NSW) v Perpetual Trustee Co Ltd* (1940) 63 CLR 209 at 216-7 (Latham CJ) and 227-8 (Dixon and Evatt JJ)

Conclusion

The device of specifying charitable bodies as potential beneficiaries is a useful one in trusts law to ensure continuity of the trust. Its use, however, requires particular attention to the broader purpose sought to be achieved and careful, detailed, and comprehensive drafting of clauses in trust deeds or instruments. Drafters should ensure that the settlor's intention is clearly expressed, and the commercial purpose and any other purposes of the trust are fully and clearly expressed. Where provision has been made for termination in the event of the commercial purpose of the trust failing, trust property may be distributed according to some residual or fall-back mechanism. This may involve the trust property reverting back to the settlor by way of an express or resulting trust. Alternatively, or additionally, provision might be made for an orderly distribution to specified beneficiaries or to a specified "remainder" or "residual" entity; perhaps a charity or another corporate beneficiary. Whatever the desired outcome, clear, comprehensive and thoughtful drafting will avoid the need for the trustee or others to make application to or seek directions from the court. It will make clear and certain the way in which the trust is to be administered, and its property distributed; both during the life of the primary purpose of the trust, and subsequently, even in the face of an "unthinkable" event.

Where no, or inadequate, provision has been made for the failure of the commercial purpose of the trust, the question becomes more complicated. It may be that the settlor's intention was for a resulting trust to arise in the settlor's favour. It may, alternatively or additionally, have been intended that the trust property pass to a particular class of beneficiaries. If there are no named or ascertainable beneficiaries, further problems arise. If the trust instrument contains provisions that indicate a gift to a charity or a charitable purpose, it may be that court intervention can save the trust from total failure. In the extreme, and outside of South Australia, the trust properly may revert to the Crown *bona vacantia*. Consequently, to avoid such a situation, the full

extent and consequences of a failure of the commercial purpose should be canvassed in the trust instrument - particularly the "unthinkable" - the failure of the enterprise the trust was intended to serve. What seems like a "sure thing" often is not! Corporations that seem stable and permanent can fail; and do. The law reports in all jurisdictions bear testimony to this commercial reality - from at least the South Sea Bubble to the most recent crisis.
