VICTORIAM LAW REFORM COMMISSION

TRADING TRUSTS – OPPRESSION REMEDIES

SUBMISSION ON CONSULTATION PAPER OF JUNE 2014

1 I am a member of the Victorian Bar. I practise in commercial disputes and insolvency matters. I am also an accredited mediator.

2 I have been involved in many disputes in which the parties were conducting business through trading trusts.

3 In this submission I make the following points:

(a) There is need for reform because lawyers and accountants are recommending trading trusts when they are not appropriate structures, especially when there is a dispute.

(b) The description in the consultation paper of the fundamental issue is not accurate. Oppression occurs not at the hand of the corporation or the trustee but at the hand of others within the trading entity.

(c) The terms of reference should be widened to encompass deadlock at board level, regardless of the reason for the deadlock.

(d) The *Trustee Act 1958* should be amended to include provisions similar to the buyout provisions in section 233 of the *Corporations Act 2001*.

(e) The court should also be given an express power to wind up a trust.

4 In my experience business people usually rely on their lawyers and accountants to recommend appropriate structures for their businesses. It is often the tax accountants that recommend a trading trust with a corporate trustee, usually a unit trust with discretionary trusts to own the units. So the founding documents are a company constitution and one or more trust deeds.

5 In a perfect world there would also be agreements between the shareholders and the unit holders dealing with issues like the ability to compel the purchase of units and an agreed basis for the valuation of the units – as there would be in a partnership agreement. In practice it is rare to see competently drawn agreements of this kind in place. In many cases there are no such agreements at all.

6 The result is that when there is a dispute between the persons in business they are caught in a web of uncertainty. Their rights and obligations are determined by corporations law and trust law. It is rare for the directors of the corporate trustee (who are often also shareholders of the trustee company and beneficiaries of the discretionary trusts that own the units in the unit trust) to fully understand their structures. There is no point telling them later that they have chosen those structures, and that they have left themselves without an obvious remedy when they argue.

7 The issues referred to in the preface to the consultation paper and in the introduction are not accurately stated. The consultation paper refers to oppressive conduct by a corporation, also to oppressive behaviour by trustees. The oppression is usually effected by fellow travellers - by shareholders against other shareholders, or by beneficiaries against other beneficiaries. The oppression is not by the corporation itself or the trustee (which is the same thing where there is a corporate trustee.)

8 Consider for example a case in which the founder of a succesful business takes in a "partner" and the accountant recommends a unit trust structure. The new partner happily takes the profits but does no work, contrary to the previous understanding between them. How does the founder expel the newcomer, and how much is the newcomer entitled to for the units in the trust?

9 The Commission's consultation paper contains a thorough and helpful summary of the law as it stands at present and of some of the issues requiring attention.

10 In my opinion it is not a realistic option to leave things as they are.

11 The late professor Harold Ford referred to the unhappy union between corporations law and trust law. He described the trading trust as a "commercial monstrosity" ("Trading Trusts and Creditors' Rights", (1981) 13 MULR 1.) He was right. Something needs to be done to guide the parties out of the maze.

12 Getting back to the example of the problem with the newcomer, under the present law there is a real difficulty on two levels if the founder wants to expel the newcomer.

13 The first difficulty is that the gateway to a buyout order under section 233 of the *Corporations Act 2001* is the requirement to show, under section 232, oppression or conduct contrary to the interests of the members. Oppression by the delinquent "partner" in particular would be hard to show.

14 Indeed, if there is oppression it might well be the working partner oppressing the lazy partner out of frustration. Can the working partner then claim that there has been oppression generally, thereby enabling it to invoke the buy out provisions in section 233 of the *Corporations Act 2001*? Further, would the working partner then be exposed for the costs of the proceeding because of its own conduct?

15 The second difficulty is that the court may not have power to order a buyout of the units in the trust (if, as the New South Wales courts suggest, the decision in *Viglioroni* is wrong.)

16 My basic point is that a court should have power to order a buyout of units where there is deadlock at board level for any reason at all. That could be done by enlarging the powers in the *Trustee Act 1958* to include buy out provisions like those in section 233 of the *Corporations Act 2001*.

17 Incidentally, that would provide a broader remedy than that in the *Corporations Act 2001*. There is no present basis under that Act for the court to order a buy out based on deadlock. Perhaps that could be considered in the next round of amendments to that Act. The *Trustee Act 1958* can lead the way.

18 I also recommend that the court be given express power to wind up a trust, just as it can wind up a company on the just and equitable ground (section 461 of the *Corporations Act 2001*.) If the court considers that the relationship is finished it could order that the trust be wound up and give directions about appropriate distributions.

19 The number of cases brought to court for decision does not reflect the size of the problem in the commercial community. Not all cases get to court, and most of those are settled and are not reported. Discussions with lawyers and accountants would reveal the scale of the problem.

20 I do not support the implicit suggestion, at paragraph 5.6 on page 55 of the discussion paper, that there is no real demand for change in the commercial community. Many of the entities that encounter these problems are family businesses and other small to medium enterprises. They cannot afford the costs and distress of litigation.

Thankfully, where common sense prevails, many of the disputes are resolved at early mediation. But that does not mean that the problem does not need to be fixed.

21 A trust is not an entity. It is a relationship. But with common usage it has come to be treated as an entity. Accountants prepare financial accounts for the trust. The Australian Taxation Office requires a trust to lodge its own tax return, thereby promoting the fiction that a trust is a separate entity. Accordingly, given that practical reality, it would be sensible to provide for beneficiaries and unit holders remedies similar to those available to shareholders in a company.

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