

Executor and trustee investment duties

As fiduciaries, executors and trustees owe numerous duties to both the estate and to its beneficiaries. CI's Tax, Retirement and Estate Planning team website, <http://trep.ci.com/> contains a checklist for executors outlining over 40 distinct duties, and no less onerous are the duties of a trustee. This article addresses a particular trustee duty, namely the duty to invest the trust property.

A trustee is limited by three legal rules when investing:

1. A trustee is required to obey the trust deed

Often, a trust deed will contain a specific term limiting the trustee's investment authority. Recently, the British Columbia court provided a clear message to settlors and testators to carefully consider the words chosen in a trust deed, as those words may greatly limit the trust investments. In *Dunn v. TD Canada Trust* (2016), a trust created upon the death of the testator in 1957 contained a clause directing the trustee to "retain in the form in which they are at the time of my death all my investments in bonds and stocks, and to sell, call in and convert into money all the rest and remainder of my estate." Between 1957 and 1973 the trustee sold most of the original investments, including the stocks and bonds. Most of the cash realized from these sales was distributed to the beneficiaries. What remained in the trust was invested in blue chip stocks and various bonds.

However, despite the fact the beneficiaries had received most of the cash and the remaining investments were prudent, the court found the trustee had breached its duty to obey the trust deed. Clearly, a trustee and a trust's investment advisor must carefully read and adhere to the words used in the deed.

In 2017, the Court of Appeal reversed the trial court's decision based on an interpretation of the clause in the will. However, the principles set out by the trial court are still applicable.

2. A trustee is obligated to invest as would a prudent investor

In order to ensure the investments of a trust are "prudent," a trustee is required to consider, among other factors, the following:

- General economic conditions
- The possible effect of inflation or deflation
- The expected tax implications of investment decisions on the overall investment strategy
- The role each investment plays in the trust's portfolio
- The expected total return from income and appreciated capital
- The need for liquidity, any required income payments and the preservation or appreciation of capital
- Any assets of special value to the beneficiaries.

In addition, case law is clear that a trustee has an obligation to diversify the trust's portfolio to the extent it is appropriate, even in those provinces where the legislation does not require diversification.

In most instances, a trustee is required to establish and follow an investment plan assessing the risks and returns associated with the investment portfolio. Trustees should ensure they obtain advice from an advisor and review this plan on an annual basis or when circumstances change. Failure to establish and follow a plan may result in personal liability for the trustee.

In all provinces, a trustee is permitted to delegate investment authority to an investment advisor, so long as the choice of advisor is prudent. A clause in a trust deed or will that is becoming more common provides a direction to the trustee to retain a specific advisor so long as that choice is prudent when retained. This ensures some continuity, as the advisor named is often the individual who provided services to the testator or the settlor before the trust was created.

Where the trustee delegates authority to an advisor, a written agreement between the trustee and the advisor, in addition to the investment plan, is required.

Given the requirement for diversification, the use of mutual funds are ideal for investing in trusts. Provincial legislation specifically authorizes a trustee to use mutual funds when investing in a trust. However, an investment advisor retained by the trustee will want to see specific authorization to use funds in the trust deed. In the 1994 Ontario case of **Haslam v. Haslam**, the court held that although delegation by a trustee to an investment advisor was authorized, this did not authorize the investment advisor to sub-delegate to anyone else, including a mutual fund management company without specific authorization in the deed. In order to remove any uncertainty a well-drafted trust deed usually specifically authorizes an investment advisor, when retained by a trust, to use mutual funds when investing.

It is also important for a settlor or testator to ensure that the terms of the trust deed are broad enough to allow for the type of investments they feel would be most beneficial. For instance, if the settlor or trustee contemplates the use of a mutual fund with a return of capital component, it is advantageous to allow the income beneficiary some ability to encroach upon capital; otherwise additional steps will be required in the trust accounting.

3. A trustee is obligated to maintain an even hand between the beneficiaries

A trust will often have two different classes of beneficiaries with competing interests. An income beneficiary is the person or persons who have the right to access the income produced by the trust.

Often the income beneficiary may encroach upon the capital in some circumstances. Capital beneficiaries are the persons who will inherit the capital of the trust when the trust is terminated.

In some trusts the settlor or testator will include a specific clause directing the trustee to prefer one class of beneficiary or even to ignore the interests of one class of beneficiary, thereby freeing the trustee from the confines of the “even hand” rule. However, in the absence of such a clause a trustee must ensure that the interests of all beneficiaries, both income and capital, are considered when investing.

These legal rules should be kept in mind both when creating and when administering a trust. Failure to consider these rules when drafting a trust will inhibit the trust’s investment advisor. Failure to consider these rules during the trust’s administration will lead to potential liability.

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