Australian Government

Corporations and Markets Advisory Committee

Administration of charitable trusts

Report

May 2013

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10 May 2013

The Hon. Bernie Ripoll MP
Parliamentary Secretary to the Treasurer
Parliament House
CANBERRA ACT 2600

Dear Mr Rippoll

I am pleased to present the report by CAMAC on the administration of charitable trusts managed by licensed trustee companies.

In responding to the matters raised in your request for advice, CAMAC puts forward recommendations that seek to ensure that the administrative arrangements for these charitable trusts continue to promote the benevolent and philanthropic objectives for which they were established.

Yours sincerely

Joanne Rees
Convenor

Contents

1 Introduction

This chapter provides background information on the reference, explains the review process, sets out the CAMAC approach, including in relation to the particular questions in the terms of reference, and summarises CAMAC's recommendations concerning this segment of the charities sector.

1.1 Overview

This report deals with administrative arrangements concerning one segment of the charities sector, namely charitable trusts managed by licensed trustee companies (LTCs). The terms of reference do not include charitable trusts administered by other persons, or other types of charitable entities.

The issues and conflicting points of view that have emerged during the course of this review are by no means new. Many have been articulated long before a national approach to the regulation of charitable trusts administered by LTCs was introduced in May 2010. These long-standing areas of contention have involved specific issues concerning the fees and tenure of LTCs acting as trustees of charitable trusts as well as more general matters related to the governance and accountability aspects of charitable trusts managed by LTCs.

One approach in the submissions to CAMAC during the review involved proposals for immediate and sometimes fundamental change to the regulation of charitable trusts operated by LTCs, on the basis that this is needed to ensure the focus remains on the public interest objectives of these trusts. The contrary perspective put forward in submissions was that LTCs (and their officers and employees) are already subject to a range of fiduciary duties and regulatory controls and that calls for change may be based on a misunderstanding of how LTCs manage charitable trusts pursuant to the intentions of the creators of those trusts.

CAMAC's starting point in considering these competing perspectives has been to ask why donors set up charitable trusts in the first place. It considers that the primary intent of each donor is to achieve the philanthropic or benevolent purposes or objectives for which the donor established and funded the charitable trust, within the time frame of the trust, and in an effective and efficient manner. This primary intent should be the policy cornerstone which underpins the regulation of charitable trusts generally.

From this policy standpoint, administrative arrangements for operating a charitable trust, whether sought or agreed to by the donor of the trust, should be assessed according to the extent to which they advance or promote the primary intent of the donor. Administrative arrangements are a means to this end, not ends in themselves.

For the purpose of ensuring that the legislative regime for administering charitable trusts promotes the primary intent of the donor, CAMAC proposes a two-stage reform process.

Stage 1 essentially comprises three measures:

- the conducting of Stewardship audits of a cross-section of charitable trusts administered by LTCs, to address the present deficit of relevant and indisputable information on the state of administration of charitable trusts

- the introduction of a 'fair and reasonable' requirement for all fees and costs charged against a charitable trust

- changes to the judicial dispute resolution procedures to enhance access to the court and to broaden its remedial powers, including in regard to whether fees and costs charged against a charitable trust are excessive or whether an LTC should be replaced as the trustee of a charitable trust.

As well as responding to perceived difficulties or shortcomings in the current legal regime, these proposals are designed to promote a more open market by providing opportunities, where appropriate, to alter administrative arrangements in order to achieve the primary intent of the donor.

Stage 2 would build on the information gathered from the Stewardship audits and any preliminary indications from the enhanced judicial dispute resolution procedure. It would focus on what, if any, additional changes to the regulation of administrative arrangements for charitable trusts are required to promote the primary intent of the donor.

1.2 Terms of reference

By letter of 20 September 2012, the Parliamentary Secretary to the Treasurer, the Hon. Bernie Ripoll MP, requested CAMAC to consider various matters concerning fees, and replacement of trustees, for those charitable trusts that are administered by LTCs, as well as other issues that impact on the charitable purposes of trusts. CAMAC was asked to report to the Government in May 2013.

The terms of reference contain six questions for the consideration of CAMAC. The first four questions deal with various aspects of the fees charged by LTCs for administering charitable trusts. The fifth question deals with replacing the trustee of a charitable trust. The final question asks CAMAC to consider other issues that impact on the objectives of Part 5D of the Corporations Act or the charitable purposes of trusts. The full terms of reference are set out in the Appendix to this report.

1.3 Ambit of the review

The terms of reference focus on various administrative matters concerning charitable trusts administered by LTCs. The reference does not extend to administrative matters concerning other entities in the charities sector, which may take the form of public ancillary funds (PuAFs), private ancillary funds (PAFs),[1] not-for–profit companies or charitable trusts and foundations administered by unlicensed trustees, such as individual accountants and lawyers. It appears, for instance, that more than 1000 PAFs have been established in the last decade, of which 80% are managed by parties other than LTCs.[2] Also, Public Trust offices, being State and Territory government entities, are not within the ambit of this review.

What is common to all charitable entities, including charitable trusts administered by LTCs, is the requirement that they provide a public benefit to preserve a beneficial

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1 All PuAFs and PAFs are subject to specific Commonwealth reporting and other guidelines, in the form of regulations made under the *Taxation Administration Act 1953*. Many trusts and foundations are deductible gift recipients (DRGs), which must lodge information with the Australian Taxation Office.

2 This information on PAFs was provided by the Financial Services Council.

taxation status, for instance income tax exemptions for charities that receive income distributions from the charitable entity.

One consequence for the broader charities context in which this review has taken place is that, in some respects, CAMAC's proposals relating to charitable trusts administered by LTCs could have a broader application. CAMAC refers, for instance, to its proposals in chapter 5 of this report concerning an enhanced dispute resolution role for the court. Arguably, this enhanced procedure, if introduced, could be made applicable throughout the charities sector, not just for charitable trusts administered by LTCs.

This review also took place during the period in which the recently created Australian Charities and Not-for-profits Commission (ACNC) has been developing its regulatory role, including through governance standards and external conduct standards. Some aspects of this ongoing process, including the development of various disclosure or periodic reporting requirements pertaining to administrative functions, have a bearing on the matters discussed in this review. The CAMAC report has been prepared within this context but does not seek to cover transparency matters already under consideration by the ACNC. Also, other relevant disclosure issues for consideration by the ACNC, such as the level of information to be publicly available about the identity and nature of particular charitable entities, are not covered in this review.[3]

1.4 Background

LTCs are professional trustee companies that hold an Australian financial services licence issued by the Australian Securities and Investments Commission (ASIC).[4] LTCs manage a range of legal arrangements, including charitable trusts.

A charitable trust is established by an individual or entity (the donor, alternatively described as the settlor) donating assets under a deed of trust (when the donor is alive) or by will, for a charitable purpose or purposes. The trustee holds the donated assets in trust, and administers the trust, which includes managing its assets and making distributions to other entities or persons (donees), according to the philanthropic or benevolent objectives or purposes identified in the deed or will.

The concept of donees has sometimes been extended to persons, or classes of persons, eligible to receive distributions under the terms of the trust, even when no distribution to them has taken place. However, the terms of the trust may preclude any particular individual or entity claiming an entitlement to a distribution in the same manner as a named beneficiary under some other forms of trust.

The donor may choose one of a number of entities, not just an LTC, as the trustee or one of the trustees of the charitable trust. The terms of reference cover only those charitable trusts where an LTC is the sole trustee (sole trustee trusts) or is a co-trustee (co-trustee trusts).

For the purpose of this review, a distinction needs to be made between two types of charitable trust administered by LTCs:

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3 For instance, some donors may wish to avoid the identity or nature of a charitable entity being made public for various reasons, including to maintain the anonymity of the donor or to avoid undue numbers of requests being made by outside parties for funds from the trust.

4 See s 766A(1A).

- those sole trustee trusts and co-trustee trusts that were established before 6 May 2010. They are referred to in the legislation,[5] and in this report, as existing client charitable trusts

- those sole trustee trusts and co-trustee trusts that were established on or after 6 May 2010. They are referred to in the legislation,[6] and in this report, as new client charitable trusts.

Currently, there are eleven LTC corporate groups. Most LTCs are members of the Financial Services Council (FSC). All LTCs are regulated under Chapter 5D of the Corporations Act, which came into force in May 2010. Prior to that date, matters now within Chapter 5D came within the exclusive jurisdiction of the States and Territories. Chapter 5D was the outcome of an agreement reached by the Council of Australian Governments (COAG) in 2008 that the Commonwealth assume responsibility for the uniform regulation in Australia of LTCs, including their management of charitable trusts.

1.5 The review process

CAMAC invited written submissions from interested persons on any aspect of the matters set out in the terms of reference.

Responses on the policy questions raised in this review were received from:

- the Charitable Alliance, and a number of its members

- the Financial Services Council, and a number of its LTC members

- Philanthropy Australia

- RBS Morgans

- others.

CAMAC also conducted a Roundtable in Melbourne on 11 April 2013 which involved representatives from these respondents.

CAMAC was greatly assisted in its consideration of the issues related to the administration of charitable trusts by the information and views provided by respondents. The Committee expresses its thanks to all those who participated in this consultation process.

CAMAC also acknowledges, with appreciation, the work of the CAMAC charitable trusts sub-committee (Greg Vickery (chair), Rosey Batt, Damian Egan, David Gomez, Kate Hamilton (ASIC), Rachel Webber) on this review.

5 s 601TDG.
6 s 601TDA.

1.5.1 Submissions on trustee fees and replacement of trustees

The submissions on trustee fees and the replacement of trustees pointed to what appear to be some fundamental differences of view on these matters. These issues are not of recent origin.[7]

For instance, some respondents asserted that, in some instances, LTCs of existing client charitable trusts have relied on the 'letter of the law' to increase their fees in an unreasonable and unjustified manner over recent years. The relevant provision in the Corporations Act, s 601TDH, permits LTCs post-May 2010 to charge the fees that they 'could' have charged, not what they actually charged as at May 2010. These assertions of undue fee increases pursuant to s 601TDH were denied by LTCs, with supporting data.

Various respondents also asserted that the terms of some charitable trusts have, in effect, entrenched various LTCs, and this lack of ability to replace a trustee, other than in limited circumstances, has excluded the operation of market forces, with negative consequences for the services provided compared with the fees charged. These assertions were, in turn, challenged by LTCs, who pointed to the express terms of trust instruments to have the trust administered by the LTC, asserting that some of the calls for greater ability to replace an LTC as trustee of a charitable trust may be motivated by a desire to change the philanthropic or benevolent purposes or objectives of the trust, contrary to the intention of the donor.

As a result, respondents differed, sometimes sharply, in their proposals for policy change. For instance, LTCs expressed the view that the current arrangements regulating fees under Part 5D.3 are largely satisfactory, as also are the rights of trustees under relevant trust instruments to remain in that role and the role of the court in dispute resolution. Any change, it was submitted, should focus on removing fee caps for new client charitable trusts, to allow for competitive market forces on fees and servicing. Also, an investment management fee for implementing any chosen investment strategy should be allowed in relation to all investments, not just investments in common funds.

Other respondents proposed a range of measures to regulate fees charged by LTCs more closely and to facilitate the replacement of trustees, with differing types and degrees of regulatory intervention being proposed.

1.5.2 Submissions on other issues

Some respondents argued that issues concerning trustee fees and replacement of trustees are symptomatic of a broader range of unresolved stewardship and disclosure issues regarding the role of LTCs in the administration of charitable trusts. For instance, the issue was raised in this context as to whether greater external scrutiny or other regulatory initiatives are needed in regard to the administration of sole trustee trusts.

1.5.3 Constitutional powers

One respondent raised questions concerning the constitutional power and capacity of a national government in regard to various policy options raised in the course of this review.

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7 For instance, the article 'A game of give and take' in the *Business Review Weekly* 29 June-5 July 2006 refers to differences of view between trustees of charitable trusts and other interested parties, including descendents of donors, concerning fees charged and various other aspects of the administration of those trusts.

CAMAC seeks to make clear that matters concerning constitutional power and capacity are not within its expertise. The Committee has not sought to assess the proposals in submissions, or its own approach and recommendations, from this perspective.

1.6 Primary intent of the donor

Trust law has long recognised the importance of determining the settlor's/donor's intention in establishing a trust.[8] As summed up in one recent judicial observation:

> the polestar of trust or will interpretation is the settlor's intent.[9]

In determining a donor's intent, one approach put forward in submissions was to focus on the administrative arrangements stipulated or agreed to at the time that the charitable trust was created. The trust instrument might, for instance, expressly stipulate a particular entity to act as the trustee, either conditionally or unconditionally and either for a stipulated period or during the life of the trust. On this view, these statements of intent should continue to be respected. Accordingly, it was argued, there is no proper basis for, say, removing a trustee of a charitable trust appointed pursuant to the trust instrument where the trustee is administering the trust in accordance with the terms of the trust instrument, unless the trustee has abused its powers or breached its obligations.

CAMAC considers that while this approach may be employed in the context of private and commercial trusts generally, charitable trusts fall into a separate category, given their public benefit role, which calls for a different approach. CAMAC takes as its policy starting point the need to identify the purpose for which donors establish charitable trusts in the first place. It considers that the primary intent of each donor is to achieve the philanthropic or benevolent purposes or objectives[10] for which the donor established and funded the charitable trust, within the time frame of the trust, and in an effective and efficient manner. Administrative arrangements for operating a charitable trust should be assessed according to the extent to which they achieve the primary intent of the donor of the trust.

This policy approach would permit adjustments to the administrative arrangements of a charitable trust where they are called for in order to achieve the primary intent of the donor of that trust, even where those adjustments differed from the terms of the trust instrument. In this way, any impediments to the effective administration of charitable trusts, which in some cases may not arise or become apparent until many years after the creation of these trusts, and long after donors have had any capacity to influence the trust structure, can be overcome.

The various means by which adjustments to administrative arrangements for charitable trusts might be made in order to achieve the primary intent of the donor are discussed elsewhere in this report. In this context, for instance, proposed guidance to the court in construing and applying the primary intent of the donor is set out in Section 5.5.4 of this report.

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8 *McPhail v Doulton* [1970] 2 All ER 228, [1971] AC 424.

9 *Bryan v. Dethlefs* 959 So. 2d 314, 317 (Fla. Dist. Ct. App. 2007).

10 The court may be called upon to consider the 'spirit' of a charitable trust where its particular benevolent objectives can no longer be achieved: *The Trust Company (Australia) Limited as trustee of the Kyle Williams Home Trust v Attorney-General of New South Wales (No. 2)* [2012] NSWSC 1505.

1.7 Questions in the reference

The terms of reference asked CAMAC to advise the Government on a number of questions, as set out below.

> ***Question 1***
>
> the impact [of Chapter 5D of the Corporations Act] on the quantum of fees that are, or could be, charged to charitable trusts and/or foundations (trusts) by [LTCs] and the net funds available for trusts to distribute to not-for-profit organisations. In doing so, consideration should be given to what fee arrangements would be available if trusts were able to operate in an 'open' market

Quantum of fees

A number of respondents to the review described instances where, in their view, substantial trustee fee increases occurred following the introduction of Chapter 5D of the Corporations Act in May 2010, without any apparent independent justification for these increases. However, the FSC provided data that pointed to few fee increases since May 2010 for surveyed LTCs and explained that the increases were the residual effect of State and Territory provisions that applied prior to the introduction of Chapter 5D. What was beyond doubt, however, was the existence of widely differing views about whether the quantum of fees charged by some LTCs was reasonable or excessive.

CAMAC considers that it is not possible at this point to provide a precise answer in regard to the impact of Chapter 5D on the quantum of fees charged by LTCs. It considers that whether there is an appropriate link between the quantum of fees charged by LTCs and the services provided by them in managing charitable trusts cannot be determined without a much closer analysis of the way in which LTCs have administered, and are administering, charitable trusts. For this reason, and for other stated reasons, CAMAC recommends the conducting of Stewardship audits of charitable trusts managed by LTCs, to provide necessary foundational information, including whether trustees are providing value for the fees they receive.

This matter is further discussed in Chapter 2 of this report.

Funds available for distribution

CAMAC makes the preliminary observation that increases in the quantum of trustee fees may not necessarily result in reducing the trust funds available for distribution to not-for-profit organizations. It is not a simple equation that more fees means less distributable funds. It also depends upon the quality of the service provided by the trustee, including the extent to which the trustee has managed to increase the value of the trust assets overall, or has forestalled a decline in that value that otherwise may have taken place.

A number of respondents argued that the Chapter 5D provisions that link permissible trustee fees to a percentage of the trust assets are not consistent with a fee for service approach. In their view, this may lead to the possibility of unjustified fee increases that unduly reduce the trust assets available for distribution.

CAMAC considers that whether the fees charged have unduly reduced the trust funds available for distribution cannot be determined without a much closer analysis of what is occurring in practice by the undertaking of Stewardship audits of a cross-section of charitable trusts.

This matter is further discussed in Chapter 2 of this report.

Open market

New charitable arrangements

Persons who wish to commit their funds for benevolent or philanthropic purposes may do so in a number of ways. They may gift money outright to an existing charitable organization, either during their lifetime or under their will. Alternatively, they may establish an entity for particular charitable purposes, to commence during their lifetime or by operation of their will.

When persons decide to establish an entity for charitable purposes, they must make a number of key preliminary decisions, including:

- the legal structure to be adopted (such as a trust, a not-for-profit company, a PAF or a PuAF)
- the person(s) to administer the chosen legal structure (such as an LTC, a public trustee, an unlicensed trustee entity, an accountant, a lawyer, a financial adviser or some other individual[11])
- what, if any, provision to include for later adjustment to the administrative arrangements
- the fees, if any, for administering the chosen legal structure.

Persons wishing to commit their funds in this way would be assisted by having access to comprehensive information on the options available to them on each of these matters and the legal and financial consequences of these options. Greater awareness on the part of intending donors could encourage competition between possible service providers, thereby promoting a more open market in the charities sector. CAMAC suggests that the ACNC might consider ways to assist persons in obtaining access to this information.

The terms of reference are confined to where a person chooses the legal structure of a charitable trust, to be operated by an LTC. In the context of fees, an open market exists to the extent that an intending donor (or a representative with legal capacity) negotiates with a number of LTCs on possible fee arrangements for the provision of trustee services. Any agreement reached on fees is not affected by the fee caps in the legislation.[12] Therefore the LTC may negotiate with the donor a separate fee for any service required to be performed by the LTC in administering the trust.

Existing charitable trusts

One view in submissions was that while competition among possible service providers at the time of establishing a charitable trust is worthwhile and should be encouraged, once decisions have been made on administrative matters, the original wishes of the donor on these matters should continue to be respected, even where the trust is intended to operate for many years or in perpetuity.

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11 There is no requirement for an entity to hold an Australian financial services licence in order to act as a trustee. Traditional trustee services only constitute a financial service for the purposes of Chapter 7 of the Corporations Act when provided by a trustee company: s 766A(1A).

12 s 601TBB. This is reinforced by s 601TDB(2).

The contrary view in submissions was that this approach creates a closed and anti-competitive market, to the possible prejudice of the charitable objectives for which the trust was established. It was pointed out that administrative arrangements entered into many years ago will remain in place indefinitely, regardless of any significant change in circumstances concerning the trustee or the environment within which the trust operates.

CAMAC considers that while the express wishes of a donor on administrative arrangements for a charitable trust should be acknowledged, the circumstances that may have influenced the original decisions of the donor may have materially changed since that time. In this context, the wishes of the donor on administrative matters should be construed from the perspective of the primary intent of the donor (see further Section 1.6 of this report). The overriding consideration should be whether those administrative arrangements continue to promote that primary intent.

As well as responding to perceived difficulties or shortcomings in the current legal regime, CAMAC's proposals concerning fees, the tenure of trustees, and the role and powers of the court in regard to disputes concerning charitable trusts are designed to promote a more open market by providing opportunities, where appropriate, to alter administrative arrangements in order to achieve the primary intent of the donor.

These matters are further discussed in Chapters 3-5 of this report.

Question 2

the range of additional fees beyond those regulated under [Chapter 5D of the Corporations Act] that are, or could be, charged to trusts by LTCs

Chapter 5D regulates fees charged by LTCs for 'traditional trustee company services'[13] that consist of being the trustee or manager of a charitable trust[14] as well as various other stipulated fees and costs,[15] including through the imposition of various fee caps. It also covers disbursements in this regard.[16] The Chapter does not cover any other amounts that an LTC may seek to charge against the trust. Also, various activities, including where an LTC is acting as the responsible entity of a managed investment scheme, fall outside the concept of traditional trustee company services.[17]

The issue of the width of the concept of traditional trustee company services that consist of being the trustee or manager of a charitable trust (traditional services) has particularly arisen within the context of the extent to which various investment-related services do or do not come within that concept and, therefore, are or are not included in the legislative fee caps for charitable trusts.

As indicated elsewhere in this report (Section 3.1), the FSC has drawn a distinction between:

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13 s 601RAC(1)(a), (2)(a). Operating a common fund is also carrying on a traditional trustee service: s 601RAC(1)(d).

14 ss 601TDA, 601TDG.

15 These cover fees where trust assets are invested in a common fund (ss 601TDE, 601TDI) and some other fees, including for the provision of an account (s 601TBC) and for the preparation of taxation returns (ss 601TDF, 601TDJ).

16 s 601TBD.

17 s 601RAC(3)(a).

- *trusteeship services*, which the FSC considers to be within the concept of traditional services and which are therefore subject to the statutory fee caps, and

- *investment management services*, which the FSC considers to be outside the concept of traditional services and which are therefore not subject to the statutory fee caps.

A contrary view is that investment management of trust assets is inherent in the role of trusteeship, and therefore comes within the concept of traditional services.

CAMAC considers that the scope of the concept of traditional services, and what additional fees and costs beyond those services can reasonably be charged by an LTC, require further consideration.

As a first step, the proposed Stewardship audits (in addition to their other functions) could:

- examine what fee-charging practices are being adopted by the LTCs, including what particular services provided by LTCs they classify as either traditional services or other services, and to what extent LTCs adopt a uniform approach in this regard

- identify what services are outsourced and for what reasons, and whether the costing arrangements for these services can be justified

- determine whether there is a need for clarification of what services, in principle, should be covered by the concept of traditional services

- determine whether there are good grounds, in principle, for LTCs to charge a separate fee for various investment-related services.

Stewardship audits are further discussed in Chapter 2 of this report.

Question 3

the effectiveness of regulating 'new' fee arrangements between an LTC and a trust in the manner contained in Division 4, Subdivision A of Part 5D.3 [new client charitable trusts]

Many of the comments in response to Question 1, above, as they apply to new client charitable trusts, also apply to this Question.

For the reasons set out in Chapter 3 of this report, CAMAC recommends that a 'fair and reasonable' fee requirement apply, and that it act as a qualifier to the statutory fee caps, in the sense that the caps should be seen as fee maximums rather than statutory entitlements, and are not necessarily to be regarded as fair and reasonable in all instances.

CAMAC recommends that the 'fair and reasonable' requirement apply to all fees and costs charged against the trust, even those negotiated between the LTC and a donor or other person with authority to deal with the LTC on this matter. This extended application of the 'fair and reasonable' requirement to these agreements will also promote the primary intent of the donor that the trust achieve the philanthropic and benevolent purposes for which it was established. To this extent, the principles governing fees and other aspects of the administration of public interest charitable trusts should depart from those applicable to private and commercial arrangements.

CAMAC also considers that where disputes arise concerning fees for particular new charitable trusts, there should be an accessible and effective way to resolve them. For this

purpose, CAMAC proposes an enhanced judicial procedure for the consideration of disputes over alleged excessive fees charged by LTCs of these trusts. This matter is further discussed in Chapters 3 and 5 of this report.

Question 4

the effectiveness of grandfathering of 'existing' fee arrangements between an LTC and a trust under Division 4, Subdivision B of Part 5D.3 [existing client charitable trusts]

As an immediate measure, and consistently with the approach adopted in regard to Question 3, above, CAMAC recommends that in regard to 'grandfathered' fees for existing client charitable trusts:

- a 'fair and reasonable' requirement apply for all fees and other charges against the trust, acting as a qualifier on applicable fee caps
- there be an expansion of the jurisdiction of the court to deal with disputes alleging the charging of excessive fees.

From a longer-term perspective, however, CAMAC considers that the policy rationale behind the fee grandfathering provision (s 601TDH) may need to be reviewed. Consideration could be given, at Stage 2 or subsequently, to whether the provision is consistent with the move towards a national uniform approach to the regulation of charitable trusts administered by LTCs, and whether it should be replaced with a uniform fee regime based, say, on the fee provisions applicable to new client charitable trusts.

These matters are further discussed in Chapter 3 of this report.

Question 5

what the current position is with regard to the removal and replacement of a trustee of a charitable trust, whether this position is unsatisfactory from a consumer protection perspective and if so, what, if any, reforms are necessary to address this

By way of clarification, CAMAC considers that the reference in the question to a 'consumer protection perspective' refers, in a general sense, to the public interest philanthropic or benevolent purposes for which charitable trusts are established. CAMAC does not read this term as requiring the identification of a particular group or groups of persons and a consideration of the question purely from their perspective.

Under the current law, the regulator or the court may remove the trustee of a charitable trust, usually for some form of breach or maladministration. Otherwise, subject to any removal provision in a trust instrument, trustees of charitable trusts typically have a high level of security of tenure. For many long-term charitable trusts, this provides a level of guaranteed tenure and income for the trustees, to the point where they may construe their position as amounting to a proprietary right, with any attempt to displace them as trustee (beyond the current powers to do so) as involving a loss of their property amounting to a penalty.

CAMAC is of the view that in order to achieve the primary intent of the donor, there should be a process to permit the replacement of an LTC as the trustee of a particular charitable trust in appropriate circumstances, beyond those that currently apply. However, given the potential financial and reputational consequences for the affected LTC, that power of specific removal should be exercised only by a court. CAMAC has also proposed

guidance on how the court should construe and apply the primary intent of the donor in that context.

These matters are further discussed in Chapters 4 and 5 of this report.

Question 6

other issues that impact on the objectives of [Part 5D of the Corporations Act] or the charitable purposes of trusts

A number of respondents raised other issues that were seen to impact on the objectives of Part 5D of the Corporations Act or the charitable purposes of trusts.

CAMAC considers that some of these matters could be considered at Stage 2 of the proposed ongoing review process.

These matters are further outlined at Section 1.8, below.

1.8 CAMAC recommendations

CAMAC recommends that a two-stage approach be taken regarding the future regulation of this segment of the charities sector.

Stage 1 would involve initiatives in three areas, as outlined below, for early implementation.

Stage 2 would involve a consideration of other issues and policy alternatives, taking into account the outcome of the Stage 1 initiatives.

The overriding consideration in all matters at both Stages is to ensure that the regulatory regime for administering charitable trusts promotes the primary intent of the donor.

1.8.1 Stage 1

Information gathering

CAMAC recommends that the ACNC, or some other independent party or parties appointed by the ACNC, initiate Stewardship audits of a cross-section of charitable trusts administered by LTCs, with a particular, but not exclusive, focus on sole trustee trusts.

This initiative could be implemented without the need for legislation or the enactment of regulations.

This matter is further discussed in Chapter 2 of this report.

Fees

CAMAC recommends that the following amendments be made to Chapter 5D of the Corporations Act:

- adoption of a ‘fair and reasonable’ requirement for all fees and costs (including disbursements and other charges) charged against an existing or new client charitable trust, including for outsourced services, and including any fees that have been settled by agreement. This ‘fair and reasonable’ requirement should act as a qualifier on applicable statutory fee caps, which should remain as fee maximums. Each LTC

would be required to provide an annual statement to the designated regulator that the fees and costs charged against the trust are fair and reasonable (see further Section 3.5.3 of this report)

- expansion of the jurisdiction of the court in dealing with disputes alleging the charging of excessive fees, to cover all fees and costs charged against existing and new client charitable trusts, whether or not concerning the provision of traditional services and including any fees that have been settled by agreement (see further Section 3.5.4 of this report).

CAMAC also recommends the adoption of a standardised approach to the disclosure of services and fee schedules, to make it easier for intending donors to compare the fee regimes of different LTCs and to better understand the fees that would be charged by each if appointed as trustee. This enhanced disclosure regime might be introduced by the regulator or through an industry-based initiative (see further Section 3.4.3 of this report).

Dispute resolution

CAMAC recommends the introduction, by legislation, of an enhanced judicial procedure to resolve disputes concerning charitable trusts administered by LTCs.

The procedure proposed by CAMAC is designed to increase access to the court and to give it an enhanced power to determine matters concerning any aspect of the administration of a charitable trust, including, in addition to fee disputes, the tenure of the trustee of a particular trust, in accordance with the primary intent of the donor.

These matters are further discussed in Chapters 4 and 5 of this report (see particularly Section 4.3.3, while details of the proposed enhanced judicial dispute resolution procedure are set out in Section 5.5).

1.8.2 Stage 2

Depending upon the information obtained from the Stewardship audits, and any preliminary indications from the enhanced judicial dispute resolution process, consideration should be given to whether further regulatory or other initiatives are warranted.

CAMAC considers that, notwithstanding the concern with the current situation that has been expressed in some submissions, a clear case for a prescriptive alternative regulatory framework to that introduced in May 2010 in this segment of the charities sector has not yet been made out. As earlier stated, there is a deficit of relevant, indisputable and compelling information on the administration of a sufficient number of charitable trusts administered by LTCs.

This situation may change as information is gathered through the Stewardship audits. That information may point to the need for further remedial action. Alternatively, it may indicate that the administration of charitable trusts by LTCs is working satisfactorily, or that specific areas of concern can be appropriately resolved with little or no further regulatory intervention.

Set out below is a range of policy issues that have arisen in the current review and which could be further considered in Stage 2 in light of the outcome of the Stewardship audits.

The Stage 2 review could be conducted, or co-ordinated, by the ACNC in co-ordination with ASIC, or be undertaken by a designated external review body.

Traditional services

One key area for consideration in Stage 2 is whether, in light of the Stewardship audits, the statutory concept of traditional services needs clarification or reformulation, given that the capped fee regime in Chapter 5D of the Corporations Act applies only to these services (see further Sections 3.1 and 3.5.1 of this report).

In this context, consideration could also be given to whether there are good grounds, in principle, for permitting LTCs to charge an extra fee for various investment-related services (see further Section 3.4.2 of this report).

A related question concerns the possible unbundling of the various services in light of current practices and whether conflicts of interest have arisen or could arise (see further Section 3.4.7 of this report).

Outsourcing of services

A further related matter concerns what would be suitable fee and cost arrangements for services that are outsourced by an LTC, taking into account information from the Stewardship audits on outsourcing practices (see further Section 3.5.2 of this report).

Sole trustee trusts

Another key area for consideration in Stage 2 would be the state of administration of sole trustee trusts.

Differing views were expressed in submissions on the future of these trusts. For example, it was proposed in submissions that each trust henceforth have at least one independent non-paid trustee, whose role would be to monitor the administration of the trust by the LTC. It was also proposed that a prohibition be placed on the creation of new sole trustee trusts.[18] The contrary view in submissions was that the sole trustee structure performs an important role and should be retained. Intending donors may prefer appointing an LTC as a sole trustee, to ensure that the trust is administered only by an independent professional party (see further Section 2.3.1 of this report).

Based on the outcome of the Stewardship audits, it may be possible to say with some level of certainty whether some form of increased external oversight or other regulatory initiatives for these trusts is warranted.

Fee disclosure

The question of whether each LTC should be required to report to the ACNC on the quantum of fees and costs charged against each charitable trust it administers (or trusts above a certain threshold size) could be considered in light of information gathered in the Stewardship audits on the quantum of fees and costs that have been charged against trusts (see further Section 3.4.3 of this report).

Fee caps

Data obtained through the Stewardship audits on the services provided for the fees charged may also give some indication of whether adjustments should be made to the current statutory fee caps, such as abolishing the caps or, conversely, reducing them (see further Sections 3.4.1 and 3.4.6 of this report).

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[18] It was pointed out in submissions that a precedent in this regard is found in the structure for PAFs, which must have at least one independent director or trustee, known as the Responsible Person.

Other possible fee arrangements

The Stewardship audits may also provide useful information on which to assess the merits of other possible fee options raised in this review, such as a fee for service approach (see further Section 3.4.5) or periodic review of fees (see further Section 3.4.8).

Fee grandfathering

A further matter that could be considered at Stage 2, or subsequently, concerns the policy rationale for the fee 'grandfathering' provision for existing client charitable trusts.[19] CAMAC raises the question whether this approach to the determination of fees for these trusts should be replaced by, say, the same uniform fee regime as applies to new client charitable trusts (see further Section 3.4.4 of this report).

Tenure of trustees

The information gathered in the Stewardship audits might also be instructive in considering whether the current, in effect permanent, tenure system for various trustees (subject to a court order for the replacement of a trustee) should be changed to, say, a general spill/periodic tender system for trustee appointments (see further Section 4.3.2 of this report).

This assessment might best take place following a period to assess the effectiveness of the enhanced role of the court in regard to the replacement of particular trustees, if introduced (see further Sections 4.3.3 and 5.5 of this report).

Legal structures

A broader issue that may also arise in Stage 2, or subsequently, is whether there should be greater harmonization of the various legal structures within the charities sector generally, including charitable trusts, not-for-profit companies, PuAFs and PAFs, and, if so, how this might be achieved.

Whilst any move at this time to change the present legal structures would be clearly premature, and may prove to be unnecessary, the benevolent and philanthropic purposes for which charitable trusts are established should remain the paramount consideration. The legal form adopted should always be considered within the context of achieving those charitable objectives, for the benefit of the community.

1.9 Advisory Committee

The Advisory Committee is constituted under the *Australian Securities and Investments Commission Act 2001*. Its functions include, on its own initiative or when requested by the Minister, to provide advice to the Minister about corporations and financial services law and practice.

The members of the Advisory Committee are selected by the Minister, following consultation with the States and Territories, in their personal capacity on the basis of their knowledge of, or experience in, business, the administration of companies, financial markets, financial products and financial services, law, economics or accounting.

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[19] s 601TDH.

The members of CAMAC during the course of this review[20] were:

- Joanne Rees (Convenor)—Chief Executive Officer, Allygroup, Sydney
- David Gomez—Chief Financial Officer, Land Development Corporation, Darwin
- Jane McAloon—Group Company Secretary, BHP Billiton Limited, Melbourne
- Alice McCleary—Company Director, Adelaide
- Denise McComish—Partner, KPMG, Perth
- Marian Micalizzi—Chartered Accountant, Brisbane
- Michael Murray—Legal Director, Insolvency Practitioners Association, Sydney
- Geoffrey Nicoll—Co-Director, National Centre for Corporate Law and Policy Research, University of Canberra
- John Price—Commissioner, Australian Securities and Investments Commission (nominee of the ASIC Chairman)
- Ian Ramsay—Professor of Law, University of Melbourne
- Robert Seidler AM—Consultant, Ashurst Australia, Sydney
- Greg Vickery AM—Special Counsel, Norton Rose Australia, Brisbane.

The Executive comprises:

- John Kluver—Executive Director
- Vincent Jewell—Deputy Director
- Thaumani Parrino—Office Manager.

[20] Some changes to this CAMAC membership took effect from May 2013.

2 Stewardship audits

In this chapter, CAMAC recommends that the ACNC implement, or co-ordinate, Stewardship audits of a cross-section of charitable trusts administered by LTCs. The purpose of the audits would be to obtain information on how LTCs have performed their administrative responsibilities in the context of the philanthropic and benevolent purposes of these trusts.

2.1 Survey of LTCs

At the request of CAMAC, the FSC surveyed a number of its LTC members concerning the existing client charitable trusts and the new client charitable trusts that they administer.

2.1.1 Existing client charitable trusts

Of the approximately 1120 existing client charitable trusts referred to in replies to the survey:

- 90% were sole trustee trusts, with a total capitalisation of some $2 billion
- 10% were co-trustee trusts, with a total capitalisation of some $1.2 billion.

2.1.2 New client charitable trusts

Of the 90 new client charitable trusts referred to in replies to the survey:

- 95% were sole trustee trusts, with a total capitalisation of some $120 million
- 5% were co-trustee trusts, with a total capitalisation of some $40 million.

The FSC has also indicated that, in total, LTCs are the sole trustee or co-trustee of some 1500 charitable trusts, with a combined capitalisation of approximately $3.4 billion. The FSC estimates that the entire charitable trust sector is valued at around $7 billion. The FSC has further indicated that (excluding charitable trusts that are PAFs or PuAFs administered by LTCs) LTCs, on average, distribute annual trust income amounts equivalent to 4-6% of the total capital value of the charitable trusts that they administer.

2.2 Analysis of the survey

Based on the above information, and assuming the same general trend for charitable trusts administered by LTCs not covered in the survey, it is clear that the overwhelming majority of charitable trusts administered by LTCs are sole trustee trusts. These trusts, collectively, hold the bulk of the combined capital of charitable trusts administered by LTCs, though the average capitalisation of co-trustee trusts administered by LTCs is considerably higher than for sole trustee trusts.

It was pointed out in submissions that often the express wish of a donor is for a sole trustee arrangement, sometimes to ensure that control of the charitable trust remains in the hands of a fully independent party.

The total capitalisation of all charitable trusts administered by LTCs is small, compared with that of listed companies, the superannuation sector, or managed investment schemes. However, their proper regulation is important in the public interest, given the philanthropic or benevolent purposes for which they have been established.

2.3 Need for further information

Apart from some overall statistics,[21] it is difficult at this point in time to determine what is happening generally with the administration of charitable trusts. Greater transparency as to industry practice generally is needed.

2.3.1 Sole trustee trusts

There is a deficit of readily available information on the quality of administration of sole trustee trusts, including the relationship between the fees charged by particular LTCs and the service provided to the trust. Also, the older the sole trustee trust, the less likely it is to have descendants of the donor or other interested persons to inquire how the trust funds have been managed and whether distributions have been made in the manner envisaged by the donor.

LTCs of sole trustee trusts would be well aware of the fiduciary context in which they operate and the obligations this entails in operating the trust. For instance, LTCs are required to adhere to a 'prudent person' principle in investing trust funds as part of their fiduciary duty to a charitable trust.[22] Equally, however, with no co-trustee to act as a monitor, and with security of tenure as the trustee, there may be a concern, accurate or otherwise, that administrative complacency may develop, with little or no external pressure on a trustee of a particular trust to achieve the benevolent purposes of the trust efficiently and effectively. This issue may be exacerbated where there is no group of actual or potential donees with an interest in monitoring the affairs of a particular trust, or the level or type of distributions from that trust.

2.3.2 Co-trustee trusts

Similar issues to those discussed above may arise with the administration of charitable trusts where LTCs are co-trustees. This may particularly be the case where a co-trustee lacks the ability or inclination to monitor the performance of the LTC or unresolved disputes remain between a co-trustee and an LTC regarding the administration of a particular charitable trust.

2.4 CAMAC proposal

CAMAC is of the view that a productive way to gain a better understanding of what is occurring in practice with the administration of charitable trusts operated by LTCs is through a structured review in the form of Stewardship audits. The purpose of these audits would be to focus on how each trustee has exercised its powers and assumed its responsibilities for the purpose of fulfilling the primary intent of the donor. These audits should be implemented as part of Stage 1 (see Section 1.8.1 of this report).

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21 In addition to Section 2.1, see also Section 3.2 of this report, which contains some overall statistics concerning fees, which were obtained through a survey of FSC members.

22 See, for instance, *Australian Securities Commission v AS Nominees Limited, Ample Funds Limited, AS Securities Pty Limited and Peter Grenfell Windsor* [1995] FCA 1663.

The Stewardship audits would consider the history and current administration by LTCs of a cross-section of charitable trusts, focusing on such matters as:

- the level, and type, of active administration employed, including the history of investments and distributions and investment management practices
- the relationship between the trustees of co-trustee trusts, including how any disputes between them have been resolved
- how the concept of traditional services has been interpreted and applied in practice, in particular the range of activities that LTCs consider come within/outside the scope of that concept
- the types and quantum of fees and other costs charged against the trust, including what fees and costs LTCs treat as coming within/outside the concept of traditional services (and therefore as coming within/outside those regulated under Part 5D.3 of the Corporations Act)[23]
- the method of valuation of the assets of the trust (for fee and other purposes) and the extent of involvement of any independent external party in that valuation exercise
- the nature of any investment-related services in operating the trust (beyond investments in common funds) and the costing arrangements for those services
- what services are outsourced, for what reasons, and the costing arrangements for these services
- the extent to which the trust has received identifiable value for the various fees and costs charged against the trust
- the nature and extent of any conflicts of interest that have arisen in the administration of charitable trusts
- the extent to which the benevolent and philanthropic objectives of the trust have been achieved, including the implementation strategies that have been employed.

The views of donees on relevant matters should also be sought, where appropriate.

Such a review would go well beyond the type of information required under the disclosure and reporting requirements of the ACNC Act, such as annual information statements and annual financial reports (the contents of which are being developed).

CAMAC proposes that Stewardship audits be conducted or co-ordinated by the ACNC, with the trusts included for audit being selected by the ACNC or the party it appoints to conduct the audits. A sufficient representative sample of trusts managed by each LTC would need to be audited so that an overall assessment of this segment of the charities sector could reliably be reached.

It is anticipated that participation in Stewardship audits would be on a voluntary basis. Use by a regulator of investigative powers to conduct these audits would be inappropriate, as there is no suggestion of improper conduct. However, any failure by an LTC to fully

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[23] See also the CAMAC discussion under Question 2 in Section 1.7 and in Sections 3.4.2 and 3.4.3 of this report.

co-operate in the audit process may raise questions about the willingness of that LTC to account for the management of the charitable trusts that it administers. It may point to the need for greater external oversight in some respect.

CAMAC envisages Stewardship audits providing a controlled form of transparency. It would be a matter for the ACNC to determine what information gathered by the Stewardship audits should be published. However, CAMAC envisages that the most appropriate and useful information for public release would be overall assessments of the state of administration of this segment of the charities sector, not information concerning the administration of particular identified charitable trusts.

It could be argued that the time taken to conduct Stewardship audits may delay what some parties see as more pressing and urgent regulatory initiatives. However, these audits are required to gain a clear, balanced and accurate understanding of the way in which LTCs are presently administering charitable trusts. More broad-sweeping legislative or other reform, if needed, should not be driven by particular instances, without an appreciation of the extent to which, if at all, they point to more endemic and enduring problems.

Conversely, it could also be argued that, without some clear evidence of problematic conduct by LTCs, the conducting of Stewardship audits constitutes an unjustified intrusion into the affairs of LTCs, with their commercial reputations being unfairly placed at risk. However, the purpose of the Stewardship audits is to move beyond the present environment, with its elements of conjecture, assertion, and allegation by various interest groups, to a more fully informed understanding of what is happening in practice and the level of alignment of administrative practice with the public interest, benevolent and philanthropic objectives of charitable trusts.

3 Trustee fees

This chapter reviews a range of alternative approaches to the regulation of trustee fees suggested in submissions and outlines CAMAC's proposals, including that fees and costs charged against a charitable trust be subject to a requirement that they be fair and reasonable, with an extended power of the court to deal with disputes alleging the charging of excessive fees or costs.

3.1 Services in administering a charitable trust

As earlier indicated,[24] Chapter 5D of the Corporations Act regulates fees charged by LTCs for traditional services (as well as various other stipulated fees and costs). It also covers disbursements in this regard.[25] Chapter 5D does not cover any other amounts that an LTC may seek to charge against the trust.

What is involved in managing a charitable trust is not fully clear. For instance, one area of contention concerns the status of investment management services.

On one view, managing a charitable trust necessarily involves managing the capital and other assets of the trust. The process of asset management would include making investment decisions concerning those assets, which, in turn, may require the obtaining of investment advice. On that interpretation, matters related to investment-related services would come within the scope of traditional services, with fee arrangements for these services regulated by Part 5D.3 of the Corporations Act.

The FSC has indicated that its LTC members adopt a different approach. They divide the charitable trust services that they provide into two categories:

- *trusteeship services*, which they consider to be within the concept of traditional services
- *investment management services*, which they consider to be outside the concept of traditional services.[26]

In consequence, according to the FSC, the costs of providing investment management services, and other services provided by a related or third party, such as direct property

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24 See the discussion under Question 2 in Section 1.7 of this report.

25 s 601TBD.

26 The FSC states that investment management services include:
- advice on formulation, implementation and monitoring of investment strategies
- development of investment proposals and recommendations where applicable
- provision of investment research
- customised performance reporting
- advice on corporate actions and implementation thereof
- preparation of customised investment research based on periodically updating current capital market assumptions
- preparation of regular asset allocation and portfolio reviews and reports thereon
- preparation of investment proposals in line with approved investment strategy
- research into investment proposals put forward by co-trustees, advisory boards and donees
- management of pooled investment vehicles
- provision of specialist advice on the management of direct property and other non-listed asset management.

management services, are not subject to the statutory caps in Part 5D.3 and can be recouped by the LTC as an expense of the trust.

CAMAC considers that there is a pressing need for clarification of what trustee services are/are not covered by the concept of traditional services and therefore are/are not regulated by the fee provisions in Part 5D.3 of the Corporations Act. The CAMAC approach in this regard is discussed in Section 3.5.1 of this report.

There is also the related question of what services can properly be outsourced, and what constitute suitable costing arrangements where outsourcing occurs. The CAMAC approach in this regard is discussed in Section 3.5.2 of this report.

3.2 Fees for traditional services

3.2.1 Existing client charitable trusts

Fees for existing client charitable trusts, which may have been agreed to many years ago at the time of creation of the trust, can be subsequently amended by agreement.[27] In practice, it is unlikely that this will occur often, given the requirement that there be 'a person or persons who have authority to deal with the trustee company on matters relating to the provision of the service'.[28] In many cases, particularly with long-standing charitable trusts, there may no longer be any person with this capacity.

Pursuant to s 601TDH (the 'grandfathering' fee provision), LTCs may charge the fees that they 'could have charged', not necessarily what they actually charged, as at May 2010 for traditional services. This is clear from the wording of the provision, notwithstanding that the section is headed: 'Trustee company not to charge more than was being charged before section commenced'.

In determining the effect of s 601TDH, it is necessary to take into account that the provision relates back to fees that were permitted under differing State and Territory legislation prior to May 2010.

Originally, trustees received an income commission under State and Territory trustee legislation enacted in the early 20th Century. Subsequently WA, ACT, VIC and SA amended their legislation to allow either deregulated fees (WA and ACT) or fees based on capital. NSW, QLD and TAS did not change their income commission provisions.

Given this, when s 601TDH came into force in May 2010, the relevant legislation in NSW, QLD and TAS prescribed an income commission amount, not a capital linked cap. The FSC has stated that LTCs in those States were charging the full income commission and in line with s 601TDH continued to charge the same commission amount after May 2010. The FSC has also stated that it is only in regard to LTCs operating in VIC, SA, WA and ACT (relevant LTCs) that the fee that **was** being charged may be different to what **could** have been charged. Also, according to the FSC, this is because fees in these States and the ACT were either capped or uncapped. Hence, an LTC could have charged an amount equivalent to the cap but might have been charging less than the cap.

The survey of a number of LTC members of the FSC indicated that in regard to relevant LTCs, there were 9 instances where the total dollar quantum of fees charged by an LTC

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27 s 601TBB. Subsection (1) provides that nothing in Part 5D.3 prevents its application.
28 s 601TBB(2).

against the trust increased at any time subsequent to the coming into force of s 601TDH. The FSC pointed out that this represents 0.8% of the total number of charitable trusts in the survey.

The FSC has stated that these increases were thus due to the left-over effect of prior State legislation, grandfathered by s 601TDH (its emphasis included):

> Section 21A of the Victorian Trustee Companies Act 1984 [introduced in 2006] (and the equivalent SA provision, s 10(2)(a)) introduced an annual capped commission based on the capital value of the trust [1.065%]. Before section 21A and s 10(2)(a), commissions were prescribed in those jurisdictions as a percentage of income. Naturally, switching from a commission that is based on a percentage of income (small amount) to a commission that is based on a percentage of capital (larger amount) will result in an overall higher percentage change. This is because the change in the multiple value is significant (change from income value to capital value). In other words, many Victorian and South Australian trusts that moved from income commission to section 21A or s 10(2)(a) capital commission (regardless of when they were moved) could have experienced fee increases of up to 200%.
>
> The only incidence of any fee increase after [the coming into force of s 601TDH] is a result of an organisation wide audit that identified a handful of trusts that did not move across to section 21A, s 10(2)(a) or published rate fees when all of the company's other trusts moved across. This was due to an administrative oversight and nothing to do with [the coming into force of s 601TDH] albeit the actual increase occurred post May 2010.

The FSC has also indicated that, on average, the LTC members of the FSC charge annual trustee fees for existing client charitable trusts that equate to 0.5% of the combined capital value of the trusts they administer.

3.2.2 New client charitable trusts

Trustees of new client charitable trusts, in regard to the provision of traditional services, may choose between:

- agreement between the parties,[29] or
- a capital commission and income commission formula,[30] or
- an annual management fee, at a rate not exceeding 1.056% (GST inclusive) of the gross value of the charitable trust's assets.[31] This fee may only be drawn from the income of the trust unless approval from ASIC to pay it from capital has been granted.[32]

In regard to fee arrangements for trusts coming within the survey of LTC members of the FSC:

- 75% of those trusts had fees determined by agreement between the parties
- 0% of those trusts had fees determined by a capital commission and income commission formula

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29 s 601TBB.
30 s 601TDC.
31 s 601TDD.
32 s 601TBE(3).

- 25% of those trusts had fees determined by an annual management fee.

3.2.3 Application of the statutory caps

The fee caps in Part 5D.3 of the Corporations Act for the provision of traditional services are maximum amounts. LTCs may charge less than an applicable cap. Likewise, an LTC might choose to, say, offer a fee for service arrangement within a cap as a way of showing the value it has provided to the trust for the remuneration it receives.

The FSC has indicated that, on average, its LTC members charge annual management fees for new client charitable trusts that equate to 0.8 - 1% of the combined capital value of the trusts they administer, compared with the 1.056% cap on such fees.[33]

3.3 Judicial review of alleged excessive fees

The court has been given an express legislative power in s 601TEA to hear disputes alleging the charging of excessive fees by an LTC.[34] The relevant provision applies to 'fees charged by a licensed trustee company in respect of any estate',[35] which includes fees charged for 'acting as a trustee of any kind, or otherwise administering or managing a trust'.[36] It therefore covers fees for the provision of traditional services.

The legislation provides that the fee review power of the court does not apply to:

- fees agreed between the parties, or
- fees for new client charitable trusts that are charged as permitted under the legislation.[37]

The effect of this provision is that the judicial review power does not apply to fees charged to administer new client charitable trusts.

While the provision does apply to fees for the provision of traditional services for an existing client charitable trust, there are a number of uncertainties that arise as to its scope, including:

- in what circumstances does the exemption for fees agreed between the parties[38] apply in this context, that is, whether fees reached pursuant to an agreement between an LTC and a donor many years ago constitute fees agreed under this provision.[39] The absence of any temporal limitation in the fee agreement provision (for instance, an express statement that the provision only applies to post May 2010 fee agreements) leaves open the possibility of this very wide interpretation. The courts have yet to consider this matter

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33 s 601TDD(1).
34 The court can also review these fees on its own motion: s 601TEA(4).
35 s 601TEA(1).
36 The definition in s 601RAA of 'licensed trustee company' is based on the trustee company holding a licence that covers 'the provision of one or more traditional trustee company services'. 'Traditional trustee company services' includes 'performing estate management functions' (s 601RAC(1)(a)). 'Acting as a trustee of any kind, or otherwise administering or managing a trust' is an estate management function (definition of 'estate management functions' in s 601RAA, s 601RAC(2)(a)).
37 s 601TEA(2).
38 s 601TBB.
39 s 601TBB(2)(a).

- even if the judicial review provision does apply to particular fee arrangements for existing client charitable trusts, an application for review of fees can only be made under the provision by or on behalf of a person with a 'proper interest' in the trust.[40] A person with a proper interest is defined to include ASIC, the donor, anyone with a capacity to remove a trustee, and 'a person or a class that the trust is intended to benefit'.[41] There is no express reference to co-trustees in this definition, leaving open what rights, if any, they may have under this provision. Further, the width of the concept of 'a person or a class that the trust is intended to benefit' remains uncertain. The courts have yet to consider this matter.

Where the judicial review provision does operate, and a lawful application is made or the court acts on its own motion,[42] the court may take a number of non-exhaustive factors into account in determining whether fees charged by an LTC to administer a trust are excessive.[43]

The court also has particular powers in regard to costs.[44]

3.4 Submissions

A range of approaches was put forward in submissions, either to deregulate trustee fees or to further regulate them in various ways.

In responding to each of these proposals, CAMAC has indicated the degree to which it sees merit in the general policy direction of each proposal. CAMAC notes, however, that some of these proposals, particularly in regard to increased regulation of fees, are, in effect, alternative approaches that could not operate simultaneously.

The policy approaches that CAMAC considers should be implemented as a matter of priority in Stage 1 are discussed in Section 3.5 of this report.

3.4.1 Abolition of fee caps

Submissions

One view expressed by LTCs was that fee caps for new client charitable trusts[45] should be abolished, with fees for these trusts henceforth left to market forces as influenced by relevant industry standards. It was argued that fees in financial services generally are deregulated and that there are no capped fee arrangements comparable to those that apply to charitable trustee services.

CAMAC position

Abolition of the fee caps would permit the charging of fees in excess of the former caps. CAMAC is of the view that a compelling case has not been presented for any proposition that the existing fee caps are too low. However, the proposed Stewardship audits may provide useful information on this matter.

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40 s 601TEA(4).
41 s 601RAD(1)(a), (b).
42 s 601TEA(4).
43 s 601TEA(3).
44 s 601TEA(5), (6).
45 ss 601TDC(1), (4), 601TDD(1).

Market forces

CAMAC observes that the provision permitting parties to reach an agreement on fees[46] already provides scope for the operation of market forces. Also, an LTC that chooses, say, an annual management fee is not obliged to charge up to the cap of 1.056% of capital.[47] LTCs, and other potential trustees, could create a market at the time of creation of a charitable trust by competing on the management fees that they are prepared to charge under the cap, if appointed as trustee.

Fees in financial services

CAMAC considers that there is no direct analogy between fees charged to administer a charitable trust and fee arrangements in financial services in which an LTC may be involved.

CAMAC is of the view that the administration of charitable trusts should not be considered simply as another type of financial service. The public benefit objectives of a charitable trust are fundamentally different from the private gain objectives of financial products and services generally. The objectives of a charitable trust do not change simply because an LTC that is administering that trust is also licensed to be involved in profit-making enterprises in the financial services sector. That is, the identity of a particular trustee does not change the nature of a charitable trust.

The various matters concerning fee caps could be considered in Stage 2 (see Section 1.8.2 of this report).

3.4.2 Investment management fee

Submissions

One proposal was that the legislation specifically provide for a fee to cover investment management services in addition to those that involve a common fund, for which additional fees are already recognised in the legislation.[48] This fee (which might alternatively be described as an investment administration fee) would be in addition to trusteeship fees, and could be introduced, for example, by way of an additional amount for fair and reasonable investment management services, determined in accordance with ordinary market rates, as capped or agreed.

It was argued that this change would provide neutrality between the fee treatment of common fund investments and other kinds of investment and would ensure that LTCs could recoup the costs associated with various investment strategies and not just the costs associated with investment in a common fund.

Recognition of this additional fee, it was argued, would overcome any disincentive to invest beyond common funds. It was stated that if trustees are only able to recoup the cost of making investments into a common fund but not any other kind of investment, this carries an increased risk to the ultimate beneficiary that the trustee will prefer common fund investments over other types of investments.

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46 s 601TBB.
47 s 601TDD.
48 s 601TDE.

CAMAC position

CAMAC would be concerned if it emerged that a trustee was giving preference to the investment of trust funds in a common fund, rather than an apparently better alternative investment, because of additional fees it could receive from adopting the first option. Any such approach may be difficult to reconcile with the duty of a trustee to make investment decisions according to the 'prudent person' principle.

The issue of investment management fees is part of the broader question of what matters should come within the concept of traditional services, given that the capped fee regime in Chapter 5D of the Corporations Act applies only to these services. As discussed elsewhere in this report (Section 3.5.1), CAMAC proposes that this matter be included in the Stewardship audits, for further consideration in Stage 2 of the review, in light of information gathered in those audits.

3.4.3 Greater disclosure of fees

Each LTC must make publicly available its schedule of fees for the provision of traditional services,[49] and must disclose to the client any changes to the fees charged.[50] However, the current ACNC disclosure regime does not require LTCs to report the actual total quantum of fees they charge for administering each charitable trust.

Submissions

It was pointed out that an enhanced fee disclosure regime commenced in 2006 in the area of superannuation and managed investment schemes. It introduced standardised terminology and a fee disclosure template, which could be adopted in the present context.

CAMAC position

CAMAC supports a standardised approach to the description of the types of fees charged in the charitable trust sector, and how they are calculated. This would make it easier for intending donors to compare the fee regimes of different LTCs and to better understand the fees that would be charged by each if appointed as trustee.

In order to be meaningful, a standardised approach would need to clearly identify such matters as:

- the various services that are included
- the various categories of fees and costs for each of these services, and the fee/cost formula employed
- what effect outsourcing will have on the fees/costs chargeable by the trustee.

Consideration might also be given to a requirement that all LTC fee schedules for managing charitable trusts be disclosed on one designated website (in addition to the current disclosure obligation) using fee templates, thereby providing easily accessible, complete and comparative information at one location.

This enhanced disclosure regime might be introduced by the regulator or through an industry-based initiative.

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[49] s 601TAA.
[50] s 601TAB.

CAMAC is of the view, however, that while the disclosure of types of fees charged and fee schedules is important, it does not suffice, of itself, to ensure a satisfactory regulation of the actual quantum of fees charged by LTCs for services provided to charitable trusts.

CAMAC elsewhere proposes the introduction of a requirement that all fees and costs actually charged against the trust be fair and reasonable, and that the court have an extended jurisdiction to consider whether fees and costs are excessive (see Sections 3.5.3 and 3.5.4 of this report).

The further question of whether each LTC should be required to report to the ACNC on the quantum of fees and costs charged against each charitable trust it administers (or trusts above a certain threshold size) might best be considered in light of information on fees gathered in the proposed Stewardship audits. This matter could be further considered in Stage 2 (see Section 1.8.2 of this report).

3.4.4 The fee 'grandfathering' provision

The operation of s 601TDH, the fee 'grandfathering' provision for existing client charitable trusts, has been described in Section 3.2.1 of this report. According to the Explanatory Memorandum to the Bill that introduced the provision:

> 'Grandfathering' generally means that, when rules change, current participants remain unaffected and the new rules only apply to new participants.[51]

Submissions

Some submissions argued that s 601TDH should be amended to grandfather the quantum of fees that were actually being charged as at May 2010. The view was put that this change would bring the provision into line with the section heading, namely: 'Trustee company not to charge more than was being charged before section commenced'.

A contrary view was that s 601TDH should be retained in its current form, on the basis that LTCs are not charging fees to existing client charitable trusts that exceed the fees that they could have charged if Chapter 5D of the Corporations Act had not been introduced.

CAMAC position

CAMAC understands why some differences of view may have arisen as to the intent of s 601TDH. On the one hand, the heading of the Section refers to fees 'being charged' in May 2010. Also, the Explanatory Memorandum to the Bill that introduced the provision stated that 'grandfathering' of fees charged to existing client charitable trusts:

> means that those existing clients will continue to pay the same fees as they did before the new legislation [May 2010].[52]

On the other hand, the provision refers to fees that an LTC, as at May 2010, 'could have charged' in relation to traditional services, not necessarily the fees that they actually charged at that time, which may have been lower.

While aware that s 601TDH may have created conflicting expectations among affected parties, CAMAC is not convinced that any alternative formulation of the provision offered

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51 Explanatory Memorandum to the Corporations Legislation Amendment (Financial Services Modernisation) Bill 2009 paragraph 2.110.

52 Explanatory Memorandum to the Corporations Legislation Amendment (Financial Services Modernisation) Bill 2009 paragraph 2.66, Supplementary Explanatory Memorandum paragraph 2.69.

in submissions is clearly preferable. For instance, changing the wording from fees that an LTC 'could have charged' to, say, fees that an LTC 'actually charged' as at May 2010 (presumably with some inflation factor) could in some instances lead to anomalous results, such as fee 'windfalls' for the trust, depending upon what had been the arrangements as at May 2010.[53]

CAMAC, however, is also of the view that the policy approach behind s 601TDH may need to be reconsidered at some later stage. The section was introduced to preserve fee arrangements for existing charitable trusts with the movement from State and Territory to national regulation in May 2010. While that policy approach may have assisted in achieving the transition in May 2010, the permanent preservation of differential fee arrangements based on State/Territory legislation as it stood in May 2010 seems out of step with the notion of a uniform regulatory regime for charitable trusts under a national scheme.

CAMAC also takes into account that its recommendations in regard to fees, particularly a 'fair and reasonable' requirement (Section 3.5.3 of this report) and an enhanced jurisdiction of the court concerning alleged excessive fees (see Section 3.5.4 of this report), may result in less fee disparity over time, and therefore reduce the effect of differential fee arrangements based on State and Territory legislation.

Within that context, CAMAC considers that the principles underlying s 601TDH should be revisited, at Stage 2 or subsequently. If greater fee uniformity is considered necessary or desirable, one possible approach is to provide that henceforth the fee regime for existing client charitable trusts be more closely aligned with that for new client charitable trusts.

3.4.5 Fee for service approach

Submissions

Some respondents proposed a fee for service approach, whereby fees would be charged by an LTC having regard to the actual time and effort involved in servicing the trust, either by using a time-sheet system, or pursuant to a settled budgeted estimate of the time likely to be taken. This approach would be comparable to the fee charging arrangements typically adopted by lawyers and accountants.

A contrary position in submissions was that there are good reasons why LTCs do not offer a fee for service arrangement. For instance, it was argued that fees charged by LTCs include an intangible element of the risk and responsibility inherent in the role of a professional trustee. The element of risk and responsibility is not something that can be appropriately priced on an hourly rate. Further, fee for service providers do not assume this risk or responsibility, since they merely act in accordance with instructions from the trustee.

It was also argued that there is no solid evidence to show that a fee for service model is necessarily the cheapest means for the provision of trustee services, particularly at a time when best practice pricing in the legal profession is moving away from time-based charging.

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[53] The FSC has indicated that in May 2010 there were a number of trusts where the trustee, through administrative oversight, was, in effect, undercharging, compared with other trusts administered by that trustee: see Section 3.2.1 of this report.

CAMAC position

One of the intended purposes of a fee for service approach is to better align fees charged with work actually and properly done for the benefit of the trust.

To achieve this, it would be necessary to:

- settle an appropriate formula (for instance, $X per unit time of a particular category of work done)
- ensure that the fees charged reflect the actual time spent on behalf of the trust
- ensure that the fees charged reflect services performed for the actual benefit of the trust.

A suitable formula for determining fees would have to properly recompense the trustee, while also being in the best interests of the trust and having appropriate and workable monitoring mechanisms.

CAMAC notes that there is nothing to preclude an LTC, at any time, choosing to adopt a fee for service model, provided that the fees charged do not exceed any existing agreement on fees or relevant fee caps.

However, CAMAC has also taken into account the contention that mandating a fee for service system would require a fundamental restructuring of an LTC's business model, involving considerable cost.

On the basis of the above concerns raised in submissions, CAMAC is not convinced of the benefits to be gained from introducing a fee for service requirement. CAMAC notes, however, that voluntary adoption of this approach (within applicable statutory caps and any other agreed fee limits) may be one way for an LTC to indicate that the fees it charges are fair and reasonable in the particular circumstances of that trust (see further Section 3.5.3 of this report).

The matter of a fee for service approach could be further considered in Stage 2 (see Section 1.8.2 of this report).

3.4.6 Revise the fee caps

Submissions

Some respondents argued that the existing fee caps under Part 5D.3 are unduly generous, compared with comparable financial service sectors, including superannuation administration.

One approach was to reduce the caps. Another proposal was to introduce scaled fee caps, on the basis that present caps which permit a fee based on a flat percentage of capital[54] would not be sustainable in a competitive market, nor do they currently reflect a reasonable fee for service. On that view, the cap fee percentage should decrease as the size of the fund increases, given the economies of scale involved. These benefits of scale, it was argued, should be passed on to the charitable objectives of the trust.

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[54] A flat percentage of capital fee is permitted under ss 601TDC and 601TDD for new client charitable trusts.

A contrary contention, supported by an actuarial study commissioned by a respondent, was that fees charged by charitable trustees were only marginally higher (20 basis points) than those charged by superannuation funds.[55]

CAMAC position

Reduce the caps

CAMAC is not in a position at this point to make any determination whether the existing statutory fee caps are unduly high. It may be possible to reach a more informed view on this matter in light of the outcome of the proposed Stewardship audits.

In any event, it would also be necessary to ensure any reduction of existing fee caps did not unduly disadvantage LTCs, given the time and effort involved in discharging their trustee obligations.

Scaled fee caps

CAMAC is of the view that while the principle of a sliding fee scale has merit, its adoption would require the setting of appropriate scales. There is also the possibility that any sliding scale could be interpreted as an entitlement, on the basis that the scale itself is sufficient to guard against undue fee recovery.

CAMAC considers that the voluntary adoption of scaled fees, within applicable statutory caps and any other agreed fee limits, may be one way for an LTC itself to establish that its fees are fair and reasonable (see further Section 3.5.3 of this report).

The various matters concerning fee caps could be further considered in Stage 2 (see Section 1.8.2 of this report).

3.4.7 Unbundling of services

Submissions

One proposal was that the services now provided by an LTC should be 'unbundled', including by separating out the trustee role from the investment management role. It was argued that this would provide greater open market competition for the provision of each of these services, with greater potential for the objective comparison of fees charged against services promised and services delivered. The comment was also made that this approach would be a response to what, on one view, was the possibility of conflicted remuneration where, for instance, an LTC outsources investment-related activities to a related party provider.

A contrary perspective was that there should be no prohibition on a trustee offering a bundled product or service. The key reason for a donor choosing to appoint a particular LTC as the trustee of the charitable trust is the expertise and experience of that LTC in increasing funds under management.

It was also pointed out that a donor who wishes the investment management function to be separated from the trusteeship role may include a direction to this effect in the terms of the trust instrument itself.

It was also suggested that the disclosure regime could be enhanced by requiring all professional trustees to disclose information about the ability of a donor to elect to

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[55] Rice Warner Actuaries *Charitable Trustee Fees* (May 2013), commissioned by the FSC.

separate the trustee and investment management roles. It was further stated that where these roles are separated, the 'prudent person' duty of a trustee nevertheless dictates that the trustee remain responsible for the prudent investment of trust assets. The trustee cannot delegate its responsibilities in that regard and therefore continues to be responsible for the oversight of the investments and the making good of losses that may be incurred as a result of any breach of that duty. It was argued that it should always be at the trustee's discretion whether to accept trusteeship business that mandates appointment of a separate investment manager.

CAMAC position

CAMAC notes that the unbundling proposal seeks to ensure efficient pricing of fees for each aspect of the administration of a trust through market forces, as well as overcoming any perceived conflicts of interest.

However, CAMAC is not persuaded that LTCs are necessarily in positions of conflict where they perform the role of investment manager as well as trustee. On one view, investment management of trust assets is inherent in the role of trusteeship. Also, important issues remain concerning the potential liability of a trustee under any unbundling arrangement. More information on these matters may become available through the Stewardship audits, which in turn may assist any further consideration of the unbundling of service provision at Stage 2.

3.4.8 Periodic review of fees

Submissions

A further proposal in submissions was to the effect that there be a systematic and periodic review of fees to assess their fairness and competitiveness in the market.

For this purpose, the regulator or some other independent assessor would be required to review the fees charged by LTCs in administering charitable trusts (possibly with a threshold asset size test for relevant trusts) every five years or so, comparing the fees charged with those of other trusts of the same size and complexity. Under this approach, increases in fees would be by way of application to the regulator or assessor with supporting evidence to ensure that any increase was reasonable and justified according to the particular charitable trust.

It was also proposed that there be a requirement to disclose the reason for any increase in fees, with the information disclosed being freely available to allow for public scrutiny of the increase.

ACNC

The ACNC already has a role in this area. The ACNC has advised that under proposed Governance Standard 1, a charitable trust must (among other things) comply with its purposes and character as a not-for-profit entity. If a trustee of a charitable trust was receiving benefits that did not constitute genuine compensation for services provided to, or reasonable expenses incurred on behalf of, the trust, those excessive fees may constitute non-compliance with the governance standard and enliven the ACNC's enforcement powers. Depending upon the circumstances, the ACNC could exercise its power to issue a direction on the quantum of fees that could be charged, and any repayment of excessive fees. Alternatively, the ACNC could seek a court injunction to prevent the charging of excessive fees.

CAMAC position

CAMAC considers that the proposal in various submissions for periodic reviews of fees would go well beyond the current ACNC powers set out above. It would require a periodic review of all fees charged by LTCs for administering charitable trusts, at least those with capital assets above a stipulated threshold.

CAMAC has considerable reservations about the practicality of this proposal. It questions whether any regulator, for instance, should be asked to become this closely involved in reviewing the operation of each relevant charitable trust and in making decisions on fees on a trust-by-trust basis. It is of the view that this may go well beyond the usual functions of a regulator.

3.4.9 Power to replace the trustee

Submissions

It was suggested in some submissions that the ACNC, or some other non-judicial body, should have the power to replace a particular trustee where it considers that the fees or expenses charged by that trustee are excessive and that co-trustees should have standing to apply to that body for the exercise of this power. One particular proposal was that an independent trustee review board be established, with powers to examine fee issues and refer cases to the ACNC, which could then consider the use of its powers to suspend or remove particular trustees.

CAMAC position

CAMAC would be concerned if a regulator was given an express power to replace a particular trustee on the basis of its conclusion that the fees charged by that trustee were excessive.

Also, as the removal of a particular trustee on the basis of the fees it has charged may have significant financial, as well as reputational, implications for that entity, a right of appeal to a court from the decision of a regulator or other non-judicial body would be necessary.

CAMAC considers that a better and more direct approach is to enhance the powers of the court to review whether fees charged by a particular trustee are excessive, with additional provisions to improve access to the court. A regulator such as the ACNC would have a right of application to the court. This matter is further discussed in Section 3.5.4 and Chapter 5 of this report.

CAMAC also proposes an enhanced court role in the replacement of a trustee of a particular charitable trust, where this is called for in order to achieve the primary intent of the donor of that trust. In that context, the fees charged by an incumbent trustee could be a relevant factor. This matter is further discussed in Section 4.3.3 and Chapter 5 of this report.

3.5 CAMAC proposals

3.5.1 Scope of traditional services

As earlier indicated, Chapter 5D of the Corporations Act regulates fees charged by LTCs for traditional services (as well as various other stipulated fees and costs). It also covers disbursements in this regard.[56] The Chapter does not cover other amounts that an LTC may seek to charge against the trust.

CAMAC considers that more information is needed on how the concept of traditional services has been interpreted and applied in practice, in particular the range of activities that LTCs consider come within the concept, and whether some statutory clarification or elaboration is called for. For this purpose, CAMAC has proposed that this matter be included in the proposed Stewardship audits, and be reviewed in Stage 2 (see further Question 2 in Section 1.7, Stage 2 in Section 1.8.2 and Section 2.4 of this report).

3.5.2 Outsourcing of services

An LTC may be reimbursed for all disbursements properly made in the provision of traditional services.[57] Beyond that, no guidance is provided in the legislation in relation to what activities might properly be outsourced and the costing arrangements for outsourced services.

CAMAC considers that more information is needed on current outsourcing arrangements and charging practices concerning those arrangements. For this purpose, CAMAC has proposed that this matter be included in the proposed Stewardship audits, and be reviewed in Stage 2 (see further, Stage 2 in Section 1.8.2 and Section 2.4 of this report).

3.5.3 A 'fair and reasonable' requirement

The principle that fees and costs charged to administer a charitable trust must be fair and reasonable is in one way axiomatic. No respondent to the review disagreed with this as a general proposition, which also would be consistent with the primary intent of the donor.

The issue, however, is the means of implementation of this principle.

Possible approaches

One approach in submissions was to rely on the fiduciary duties applicable to LTCs in administering trusts, on the argument that these duties include an obligation to ensure the fees charged are fair and reasonable. It was also argued that there is no evidence that the fees actually charged by LTCs, and in accordance with relevant statutory caps, are not in fact fair and reasonable for the provision of trusteeship services.

Various other respondents argued for a more regulatory approach, either in legislation or by governance standards to be enforced by the regulator.

Preference for a legislative or regulatory approach

While recognising the fiduciary context within which LTCs operate, CAMAC nevertheless considers that a principle of such fundamental importance to the operation of

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56 s 601TBD.
57 s 601TBD.

charitable trusts should be expressly and specifically stated in legislation, or in the governance standards of a regulator, as a public benchmark. This outcome would also be consistent with ensuring that the primary intent of the donor in setting up a charitable trust is fulfilled, by ensuring that the fees and costs charged do not unduly inhibit the ability of the trust to achieve the philanthropic and benevolent purposes and objectives for which it was established.

Enshrining such a requirement in this way would provide a general and non-prescriptive approach to ensuring a properly balanced fee regime, while at the same time dealing with some of the issues identified in other proposals put forward in submissions. For instance, for the purpose of establishing that particular fees charged are fair and reasonable, a trustee may choose to adopt a fee for service approach, or charge scaled fees so that the trust benefits from any economies of scale involved.

A 'fair and reasonable' requirement for fees and costs should be implemented as part of Stage 1 (see Section 1.8.1 of this report).

Precedent

A reasonable fee requirement already applies to the preparation and lodgement of taxation returns by an LTC.[58] A fair fee concept also applies to the payment of certain fees to an LTC out of capital of the trust estate for the performance of estate management functions.[59]

A 'fair and reasonable' remuneration requirement is also found in the tax guidelines for public ancillary funds (PuAFs) and private ancillary funds (PAFs). It acts as a qualifier to the stipulated statutory caps. Under Guideline 43 (emphasis added):

> - The trustee is only permitted to pay **fair and reasonable remuneration** for the services of the trustee in administering the trust, at a rate **not exceeding** 1.056% annually (GST inclusive) of the gross value of the trust fund; and
>
> - the trustee is only entitled to be reimbursed for reasonable expenses incurred as trustee of the trust.

CAMAC considers that adoption in statutory form of the same principle for charitable trusts regulated under Chapter 5D of the Corporations Act would facilitate a degree of uniformity and harmonization in regard to fees within the various segments of the charities sector.

Elements of a fair and reasonable requirement

CAMAC considers that an LTC, as the party with overall responsibility for managing a charitable trust, should be under an obligation to ensure that all claims for payment against the trust, from whatever source, are fair and reasonable.

To achieve this, the terms of a legislative or regulatory requirement that all fees and costs involved in the administration of a charitable trust by an LTC be fair and reasonable (the standard) should make clear that:

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58 ss 601TDF, 601TDJ.
59 s 601TBE(4).

- the standard applies to all fees and costs charged against the charitable trust, including, but not confined to, fees charged by LTCs for traditional services. All charges arising from outsourced services would also be included

- the standard applies to fees agreed under s 601TBB

- the standard applies within relevant statutory fee caps, which would remain. Charging fees that are no more than the statutory fee caps does not necessarily satisfy the standard. In that respect, fee caps are maximums rather than a statutory entitlement, with the standard acting as a qualifier on those caps

- the factors set out in s 601TEA(3) (which the court takes into account when considering whether fees are excessive) are relevant in determining and applying the standard

- LTCs must turn their mind to all fees and costs charged against each of the charitable trusts that they administer through a periodic statement to the designated regulator that, in regard to each of those trusts, the fees and costs comply with the standard, with supporting reasons.

Some of these matters are further discussed below.

Caps are maximums, not automatic entitlements

CAMAC considers that mere compliance with the statutory caps under Part 5D.3 regarding fees for the provision of traditional services would not necessarily meet the standard, or necessarily encourage the best administrative practices to achieve the charitable objectives of the trust. CAMAC would be concerned with any approach that automatically deems fees that do not exceed an applicable statutory cap to be, ipso facto, fair and reasonable.

CAMAC considers that the standard should be treated as a qualifier on the existing statutory fee provisions in Part 5D.3. The standard should apply to all charitable trusts, whether existing or new client charitable trusts. It would reinforce the fact that the existing statutory caps are fee maximums, not necessarily fee entitlements for the provision of traditional services.

Agreements on fees

CAMAC has given consideration to whether the standard should apply where the parties themselves have agreed on the fee regime.[60] In this context, 75% of the fee arrangements for new client charitable trusts covered in the FSC survey were determined by agreement between the parties.[61]

The view was expressed in submissions that LTCs may compete over fees in seeking to build their client base and that this market mechanism, as reflected in fee agreements reached with donors, helps to ensure that fees are fair and reasonable.

CAMAC takes a different approach. It considers that entry into a charitable trust arrangement, which is intended for public benefit philanthropic purposes, should not be treated in the same manner as a private benefit or commercial transaction, where fees and

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60 s 601TBB.
61 See Section 3.2.2 of this report.

other matters are usually determined through a once-off negotiation process, with the obligation resting on each of the parties to obtain their own advice on these matters.

With charitable trusts, there should be a recognition that a financially/legally literate donor (or any other person with a legal capacity to deal with an LTC on fee matters[62]), even when independently advised, might still make decisions about fee arrangements, which, considered objectively (either at the outset or in light of changed circumstances), are not fair and reasonable in the shorter or longer term. The achievement of the benevolent or philanthropic purposes for which a charitable trust was established should not be forever compromised by a once-off poor fee decision of this nature.

For these reasons, CAMAC considers that even where fees are negotiated with the donor or a representative with legal capacity, the fee regime should remain subject to an overriding 'fair and reasonable' test.

Compliance

There should be a requirement that each LTC, in respect of each of the charitable trusts that it administers, provide an annual statement to the designated regulator that all the fees and costs charged against the trust are fair and reasonable, with an explanation by the LTC of the basis for that conclusion for each relevant trust, including supporting information. Merely stating, for instance, that fees charged are not in excess of statutory caps should not be considered a satisfactory explanation.

The annual statement by the LTC would include any amounts charged against the trust arising from outsourcing services or for any services that are not traditional services.

The factors set out in s 601TEA(3) would be relevant in determining a 'fair and reasonable' standard, and could be applied in the explanation accompanying the annual statement.

CAMAC considers that these annual compliance statements should be publicly available.

Implementation

A 'fair and reasonable' requirement and a compliance statement could be introduced by legislative amendment or by regulation under Chapter 5D of the Corporations Act, if possible. Either approach has the benefit of all the provisions concerning LTC fees for administering a charitable trust being in one location. Alternatively, they could be introduced through amendment to ACNC governance standards and financial reporting regulations.

CAMAC considers that regulatory or industry guidance should be provided on the elements to be taken into account in assessing whether fees are fair and reasonable. That guidance could point out that the standard does not necessarily constitute the imposition of a uniform or minimal fee requirement. In determining what is fair and reasonable, full consideration may be given to the tasks and responsibilities involved in administering the particular charitable trust, including the type and level of expertise required.

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62 s 601TBB(2)(a).

3.5.4 Expanding the jurisdiction of the court to deal with disputes alleging the charging of excessive fees

CAMAC notes that just as it is axiomatic that fees charged to administer a charitable trust must be fair and reasonable, it is axiomatic that fees and costs that are excessive cannot be fair and reasonable. Also, charging excessive fees and costs would be inconsistent with the primary intent of the donor.

As previously indicated, the court has a power under s 601TEA in some circumstances to review the fees charged by an LTC to determine whether they are excessive. However, there are significant limitations, and uncertainties, on the operation of this power, as outlined in Section 3.3 of this report.

CAMAC considers that to ensure the full effectiveness of s 601TEA, the provision should be amended to extend the jurisdiction of the court to all fees and costs charged against a charitable trust, from whatever source:

- whether in relation to an existing or new client charitable trust
- whether for the provision of traditional services or otherwise
- whether related to services provided by the LTC or outsourced services
- whether or not any of those fees and costs were agreed to by the donor or any other person with proper authority.[63]

CAMAC acknowledges that extending the jurisdiction of the court to negotiated fee agreements could lead to their re-opening. However, CAMAC restates its view that the achievement of the benevolent or philanthropic purposes for which a charitable trust was established should not be forever compromised by a fee agreement that turns out to be flawed from the perspective of achieving the primary intent of the donor.

The factors that the court may consider in determining whether fees are excessive are already set out in s 601TEA(3) and should be retained, with adjustments for the extended application of the provision to all fees and costs against the trust, from whatever source.

The proposed judicial dispute resolution procedure should apply to disputes alleging the charging of excessive fees. The procedures proposed in Section 5.5 of this report should be adopted in lieu of the current procedural aspects of s 601TEA.[64]

These amendments to s 601TEA should be implemented as part of Stage 1 (see Section 1.8.1 of this report).

63 s 601TEA(1)-(2) would need to be amended.
64 s 601TEA(4)-(6) would need to be amended.

4 Replacement of a trustee

In this chapter, CAMAC considers issues concerning the tenure of LTCs as trustees of charitable trusts and the possible procedures for replacing a trustee. CAMAC proposes an enhanced role for the court in replacing a trustee, where called for in order to achieve the primary intent of the donor.

4.1 Current position

A trustee of a charitable trust may be replaced by:

- the donor, if alive and with legal capacity to do so
- the terms of the trust instrument itself, for instance, where a person is given a power in the instrument to replace the trustee, or (very rarely) where the instrument itself makes provision for change, such as a periodic 'spill' of the trustee
- legislative process, such as where a trustee is no longer capable of acting in that role[65]
- a regulator in certain circumstances
- the court.

A trustee may also choose to retire, thereby necessitating the appointment of a new trustee.

4.1.1 Role of the regulator

Both the ACNC and ASIC have powers, within the context of their respective enabling legislation, to replace a trustee.

The ACNC may suspend or remove a trustee of a charitable trust for breach of the ACNC Act or its regulations, including governance standards and external conduct standards. The ACNC Act requires the ACNC to give consideration to a range of factors, including the nature, significance and persistence of any non-compliance, before exercising its suspension or removal powers. The exercise by the ACNC of its powers to suspend or remove a trustee is also subject to internal review and subsequent review by the Administrative Appeals Tribunal or a court.

LTCs must hold an Australian financial services licence, issued by ASIC. In various circumstances, ASIC may cancel the licence of an LTC, in which case it may transfer the estate assets and liabilities of the LTC to another LTC or in certain circumstances to a Public Trustee.[66] There are procedural requirements for cancellation of a licence, including that ASIC be satisfied that certain misconduct has taken place.[67]

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65 See, for instance, s 41 of the *Trustee Act 1958* (Vic).
66 See generally Part 5D.6, Div 2 of the Corporations Act.
67 s 915C of the Corporations Act.

4.1.2 Role of the court

A court of equity under its inherent powers, or pursuant to specific powers under State or Territory trustee legislation, may remove a trustee in various circumstances, including where the trustee has acted in breach of trust. The relevant principles are set out in Section 5.2.2 of this report.

4.2 Tenure of a trustee

In circumstances other than those set out in Section 4.1 above, a trustee, once lawfully appointed, remains in office for the period of the trust. It appears that most charitable trusts administered by LTCs have trustees with this form of extended tenure (sometimes described as permanent tenure, if the trust was established as a trust in perpetuity[68]).

4.2.1 Submissions

Support for continuing tenure

One perspective was that the current position provides certainty of administration, and is consistent with the intention of the donor. The donor of each trust that employs an LTC has specifically selected that entity as the trustee. Except in circumstances of misconduct, that LTC should have the right to continue as trustee pursuant to the stated terms of the trust instrument.

It was also argued that giving other parties, such as co-trustees or donees, some unilateral power to replace the trustee (except if so provided for in the trust instrument) would be contrary to the intention of the donor and would be at odds with trust law. It could also give those other parties undue influence, such as seeking to have the trust operate, or make distributions, in a manner contrary to the donor's original intention.

It was further argued that there is ample opportunity for open competition at the time a charitable trust is created concerning whom to appoint as the trustee of that trust. LTCs may compete for that role with each other, with individuals, and with unlicensed professional trustees. The FSC estimated, for instance, that LTCs are the trustees of less than 50% of all charitable trusts.

In this context, it was argued that for new charitable trusts, there could be an enhanced disclosure regime which would explain to donors, prior to creating the trust, that they could include specific powers within the trust instrument concerning the tenure of the trustee. Such a regime could, for example, mandate that professional trustees and solicitors specifically point to the permanency of appointing a professional trustee and advise the donor of the right to choose other options, such as including a provision granting another person or entity the power to replace the trustee in stated circumstances and/or periodically. It was noted that a similar disclosure regime has been implemented for enduring powers of attorney.

Proposals for change

Other respondents were critical of the current position which, in their view, inhibited any attempt at effective ongoing competition for the delivery of trustee services for charitable trusts. It was pointed out, for instance, that charitable trusts are often in the unique position that the individual who established the trust and appointed the LTC is no longer capable of

[68] Charitable trusts are not subject to the common law rule against perpetuities.

reviewing and, if thought appropriate, replacing the LTC. In effect, following the demise of the donor, the trusteeship defaults to a perpetual appointment.

It was also argued that some LTCs have changed fundamentally in their professional profile since they were designated the trustee in the trust instrument. This may particularly be the case with some older trustee companies which, through internal changes or external takeovers, may have become far removed in philosophy and business practice from what they were when chosen years ago by the donor. All that may remain, in effect, is the name of the LTC. Those LTCs, it was argued, may no longer be suitable for such a key role in the philanthropic sector, where non-commercial considerations should be given greater prominence.

Some respondents also pointed to other situations where provision is made for altering existing administrative arrangements, such as with managed investment schemes. Reference was also made to 'portability' rights given to various parties in superannuation and banking and other aspects of financial services provision.

4.2.2 CAMAC response

CAMAC makes the initial observation that the notion of trustee tenure, to the extent, say, that it is reliant on the terms of a trust document, is not a fully mutual arrangement. An LTC can retire as trustee of a particular trust, notwithstanding any statement of the donor in the trust instrument that the LTC remain in that role.

Analogy with managed investment schemes

CAMAC is of the view that it is not useful to try to draw any analogy between removing the trustee of a charitable trust and removing the responsible entity of a managed investment scheme. Unlike a charitable trust, a managed investment scheme has investors who, in that capacity, are entitled to determine who should continue to manage their funds on their behalf. There are no investors in a charitable trust, apart from the donor. It is thus unproductive to try to equate actual or potential donees of a charitable trust with scheme investors.

Analogy with concept of portability

CAMAC also considers that it is unproductive to bring into the discussion of replacing an LTC as trustee of a charitable trust the concept of 'portability' rights. This concept has been applied, for instance, to the right of superannuation contributors to change their superannuation fund, to the right of mortgagees to transfer their home loans and to certain other rights of retail consumers of financial services. There is no direct analogy between the position of these persons and co-trustees or donees of a charitable trust.

Current provisions contemplating the replacement of a trustee

It was argued in submissions that Part 5D.6 of the Corporations Act already permits the replacement of a trustee company without reference to the donor of the charitable trust, thereby constituting legislative recognition of limitations on the principle of trustee tenure.

For instance, Part 5D.6 regulates the particular situation where an incumbent LTC needs to be replaced in consequence of the cancellation of its Australian financial services licence. This Part also permits the transfer of the trust to a new trustee in certain circumstances.[69]

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[69] See ASIC Regulatory Guide 237 *Trustee companies: Transfer determinations by ASIC* (June 2012).

In addition, various State and Territory provisions contemplate circumstances where a trustee may need to be replaced.[70]

CAMAC considers that Part 5D.6 is clearly designed for particular circumstances which would not necessarily be in the contemplation of a donor and which are driven in part by the impetus towards uniform national regulation of LTCs, not in consequence of some underlying general principle concerning the tenure of a trustee.

Change of control within an LTC

CAMAC has considered the argument in submissions that since the shareholders of an LTC can agree to an internal change of shareholding control, such change, in effect, constitutes a change of trustee. Since May 2010, Ministerial approval is required for an acquisition of more than 15% of the voting power in an LTC.[71]

While CAMAC does not agree with this proposition on its face, it nevertheless considers that a change of internal control of a trustee is a relevant consideration for a court to take into account in reviewing whether it is appropriate for that LTC to be replaced (see further the Note to Principle (4) in Section 5.5.4 of this report).

Competitive market approach

CAMAC acknowledges that there may be a competitive open market to determine who will be appointed as the trustee of a particular charitable trust (and the terms of that appointment) at the time the trust is created.

However, CAMAC is concerned to ensure that any competitive process to select a trustee at the outset not also entrench that trustee, thereby foreclosing any competitive market influence for the remaining life of the trust. There needs to be some continuing capacity to adjust administrative arrangements, including by replacing a trustee of a particular charitable trust, where called for to achieve the primary intent of the donor of that trust.

Disclosure approach

CAMAC notes that the proposed disclosure approach, in referring to 'the permanency of appointing a professional trustee' except where the donor chooses a non-entrenchment option,[72] might be viewed by some as an indirect attempt to entrench a trustee in that role.

CAMAC does not support any form of trustee entrenchment for charitable trusts administered by LTCs, whether or not intended. As indicated above, there needs to be some continuing capacity to adjust administrative arrangements, including by replacing a trustee, where this is called for to achieve the primary intent of the donor.

4.2.3 CAMAC proposal

As with other aspects of the regulation of charitable trusts, CAMAC considers that the primary intent of the donor should be the policy cornerstone which underpins consideration of the tenure of trustees of these trusts.

In accordance with this principle, provision would need to be made for the possibility of replacing the trustee of a charitable trust in the interests of achieving its philanthropic and

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70 See, for instance, s 41 of the *Trustee Act 1958* (Vic).
71 See Part 5D.5 of the Corporations Act.
72 See the fourth paragraph under *Support for continuing tenure* in Section 4.2.1 of this report.

benevolent purposes and objectives, even where this replacement overrides the express wishes of the donor in the trust instrument and in circumstances where the incumbent trustee has not breached any applicable law or regulatory requirement.

Furthermore, these circumstances may arise even where the particular arrangements concerning the nomination and tenure of a trustee were originally entered into by a fully informed and properly advised donor.

CAMAC proposes in Section 4.3.3 of this report that the court have the power to replace a trustee, to be exercised in the context of achieving the primary intent of the donor.

4.3 Procedure for replacing a trustee

4.3.1 Submissions

Some proposals centred on giving a regulator, or some other independent person, a range of review and replacement powers over trustee appointments. It was argued that these procedures were necessary to stimulate greater competitive market forces in the administration of charitable trusts.

A further suggested procedure was the adoption of some form of mandatory periodic review of trustees, combined with a tendering process for the role of trustee of a charitable trust (above a threshold capital size).

Proponents of these initiatives argued that introduction of a more competitive open market for trustee services would be consistent with principles of transparency and accountability of trustee conduct, while at the same time improving consumer protection by requiring LTCs to continue to provide high quality and cost effective services to charitable trusts or otherwise risk losing their tenure.

4.3.2 CAMAC response

Role of the regulator

As earlier indicated, both the ACNC and ASIC may remove a trustee for various forms of regulatory breach.

Neither regulator has the power to remove an LTC in other ‘non-fault’ circumstances where there is no evidence of a regulatory breach or other misconduct by the LTC, but rather, say, where there is irreconcilable disputation between an LTC and a co-trustee, or between an LTC and donees.

CAMAC has earlier expressed its reservations about calling upon a regulator to make decisions about the trusteeship of a particular charitable trust in such ‘non-fault’ circumstances. Such a power and responsibility would go well beyond the usual administrative role of such a body (see Section 3.4.9 of this report).

If such a procedure were to be contemplated, CAMAC considers that, given the potential financial and reputational consequences for the affected LTC, a right of appeal to a court from any decision of the regulator to remove that entity as a trustee of a particular charitable trust would be required as a matter of fairness.

Independent person

CAMAC has the same reservations regarding any procedure whereby some other designated independent person or persons, such as a specialist independent trustee review board, would have the power to decide from time to time matters concerning who should manage a particular charitable trust.

Spill and tender

Various submissions proposed a procedure involving a general spill of existing trustees of all charitable trusts (or those trusts with capital in excess of a minimum threshold), followed by an ongoing periodic tendering process for trustee services of those trusts.

While the intended purpose of a general spill/tender procedure may be to bring more competitive market forces into play in the administration of charitable trusts, CAMAC has concerns about its workability and possible detrimental consequences to trusts, including the diversion of trust funds in meeting the substantial costs that may be involved in any properly conducted spill and tender process. Also, such an approach could generate ongoing uncertainty and unnecessarily destabilise those trustees who are seeking to fully advance the interests of the trusts they administer. Further, a spill and tender process may result in important knowledge and expertise concerning the administration of particular trusts being lost.

The question also arises of how determinations under the spill/tender process should be made and whether there should be some form of regulatory guidance or oversight in this regard.

Taking all these matters into account, CAMAC considers that the case for an immediate move to a general spill/tender procedure for trustee services has not been sufficiently made out at this time, nor have all the necessary elements of any such procedure been identified.

In the event that the Stewardship audits indicate that, overall, the primary intent of donors is being materially compromised by the current trustee tenure arrangements, then the general spill/tender proposal for trustee appointments could be revisited. In those circumstances, however, close consideration would need to be given to the tendering regime, including how tenders are to be assessed, as well as the appropriate duration of contract periods for the administration of charitable trusts.

4.3.3 CAMAC proposal

Having considered the competing proposals, CAMAC is of the view that the power to replace a particular LTC as trustee of a particular trust (over and above the powers already given to the regulators) should reside in the court, not in a non-judicial body, given the potential reputational as well as financial damage to that entity from being removed as trustee.

This situation differs from any general spill and tender process that might be introduced, which would apply to the trustees of all charitable trusts (or those above a particular capital threshold) and which, therefore, would not be directed at the trustee of a particular trust. All trustees would be equally affected by the change in tenure arrangements under a spill and tender approach.

CAMAC is further of the view that the court should be given a general power to replace a trustee of a particular trust in circumstances other than breach, where this is called for in order to achieve the primary intent of the donor of that trust (see further Section 5.5 of this

report, which sets out proposed guidance to the court on this matter). This should be implemented as part of Stage 1 (see Section 1.8.1 of this report).

CAMAC observes that giving the court a power to replace a trustee of a particular trust does not mean that this power should be employed without due consideration of the possible consequences for the trust. The court may need to take into account, for instance, that the trusteeship of a particular charitable trust may be much more than merely a series of administrative tasks. It may require skilled judgement and particular expertise in managing substantial assets over a long period. The skills and experience of both the current trustee and any proposed replacement trustee would need to be closely assessed in this regard.

5 Dispute resolution

This chapter sets out proposals by CAMAC for an enhanced judicial process for the resolution of disputes over the administration of charitable trusts.

5.1 Context

During the course of this review, it became clear that, in addition to general policy issues concerning the administration of charitable trusts managed by LTCs, conflicting views were held on the suitability and effectiveness of the current means to resolve disputes concerning these trusts. This concern was driven, in part at least, by what appeared to be some long-standing and unresolved disputes between particular LTCs on the one hand and co-trustees or other interested parties on the other.

CAMAC considers that having an effective dispute resolution procedure is an important element in a properly functioning regulatory environment for charitable trusts. The objective should be to ensure that the dispute resolution mechanism is properly accessible to bona fide involved parties while at the same time producing binding outcomes on administrative matters which are consistent with the purposes for which charitable trusts were established.

5.2 Current position

5.2.1 Non-judicial dispute resolution

LTCs, as a condition of their licence, must have a dispute resolution system, including being a member of an external dispute resolution (EDR) scheme.[73] The Financial Ombudsman Service (FOS) is the EDR for trustee services. However, the question remains as to who has access to this EDR scheme in this segment of the charities sector generally. As well, there are constraints on the FOS considering fee-related disputes.

5.2.2 Judicial dispute resolution

Prior to the coming into force of Chapter 5D of the Corporations Act in May 2010, judicial review of matters concerning charitable trusts was the exclusive preserve of State and Territory courts, under their inherent equity jurisdiction over trusts, as well as pursuant to judicial powers under the various Trustee Acts.[74]

The introduction of Chapter 5D did not disturb this inherent jurisdiction:

> Any inherent power or jurisdiction of courts in respect of the supervision of the performance of traditional trustee company services is not affected by anything in [Chapter 5D].[75]

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73 s 912A(2).
74 See, for instance, s 70 of the *Trustee Act 1925* (NSW).
75 s 601SAA(1).

Relevant case law provides judicial guidance on the exercise of this inherent jurisdiction, including the removal of a trustee. For instance:

> The jurisdiction to remove a trustee is exercised with a view to the interests of the beneficiaries, to the security of the trust property and to an efficient and satisfactory execution of the trusts and a faithful and sound exercise of the powers conferred upon the trustee. In [any decision] to remove a trustee the Court forms a judgment based upon considerations, possibly large in number and varied in character, which combine to show that the welfare of the beneficiaries is opposed to his continued occupation of the office. Such a judgment must be largely discretionary.[76]

In the case of a charitable trust, it has been further held that:

> the focus, of course, must be on whether the objectives of the trust are opposed to the continuation of the trustee, since a charitable trust has no beneficiaries.[77]

Applying these principles, the Court in a recent decision refused an application to replace the trustees of a charitable trust on the basis that:

> there is no suggestion that those trustees have failed to execute the trust in accordance with the testator's wishes and in a way that best achieves the objects of the trust … In addition, it is not obvious that the trust would be more effectively administered if the current trustees were replaced.[78]

The court will also replace a trustee where the trustee has breached its fiduciary duties, has acted, or failed to act, in circumstances that endanger the trust property or has displayed a lack of honesty, or where the trustee no longer has a proper capacity to undertake the administration of the trust.[79]

As previously indicated, the court in some circumstances may review the fees charged by an LTC to see if they are excessive.[80] There are significant limitations and uncertainties on when this power can be exercised (see Section 3.3 of this report). CAMAC has elsewhere put forward proposals regarding the future application of that provision (see Section 3.5.4 of this report).

5.3 Non-judicial dispute resolution

5.3.1 Submissions

One approach proposed was to expand the non-judicial dispute resolution mechanism for disputes between an LTC and other affected parties. This could involve, for instance, empowering the ACNC to set up a body to hear and resolve disputes in this segment of the charities sector. A suggested model was the Takeovers Panel, which, in the corporate area, can make various binding determinations.

5.3.2 CAMAC position

CAMAC places importance on an accessible non-judicial dispute resolution procedure in this segment of the charities sector. An independent arbitrator, such as the FOS, may have

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76 *Miller v Cameron* (1936) 54 CLR 572 at 580-581 per Dixon J.
77 *Crowle Foundation v NSW Trustee & Guardian* [2010] NSWSC 647 at [33].
78 *Sir Moses Montefiore Jewish Home & Ors v Perpetual Company Limited & Anor* [2012] NSWSC 210 at [31]-[32].
79 See, for instance, *Garrett v Yiasemides* [2004] NSWSC 828 at [27].
80 s 601TEA.

a valuable role to play in mediating between parties, and assisting them to reach a mutually-agreed position on a contentious matter.

It may be beneficial if thought is given to clarifying and, if necessary, expanding the role of the FOS in mediating disputes involving the administration of charitable trusts, including those involving co-trustees or donees of a trust. CAMAC suggests that the ACNC could liaise with the FOS on these matters.

The parties to a successful mediation could be required to execute a deed of settlement, to be lodged with the ACNC. This would be an end to the dispute, unless it can later be shown that the settlement did not involve full candour on both sides.

CAMAC, however, would be concerned about going beyond the role of mediation and giving the FOS, or any other non-judicial intermediary, the power to make non-agreed and binding determinations on matters concerning the administration of charitable trusts, such as the fees to be charged by a trustee or who shall administer a particular trust.

In CAMAC's view, any non-judicial determination on matters not agreed to by the parties would have to be open to appeal to a court, given the financial interests and commercial reputations that may be at stake. CAMAC considers that the preferable option to ensure greater finality of proceedings, and to avoid the time and costs of a two-tier review process, is to vest the original jurisdiction to make non-agreed binding determinations in the court.

5.4 Judicial dispute resolution

5.4.1 Submissions

One view was that the current role, powers and processes of the court are satisfactory and should not be changed. Parties with a sufficient interest who are dissatisfied with any aspect of the administration of a charitable trust can seek remedies through a judicial determination.

A contrary view was that, while a judicial dispute resolution procedure exists, it does not function in a suitable manner. Respondents pointed particularly to the difficulties that can arise in establishing sufficient standing to bring a matter concerning a particular charitable trust to court. They also pointed to the potential costs that may arise from a judicial hearing, including a possible adverse costs order. The view in various submissions was that these matters can act as a strong, sometimes decisive, deterrent to the use of this dispute resolution procedure, even for the most deserving of cases.

5.4.2 CAMAC position

CAMAC places considerable importance on the effective role of the court in resolving disputes in this segment of the charities sector which cannot be successfully mediated, as proposed in Section 5.3.2, above. However, it appears that currently there are a number of actual or perceived barriers to the effective utilisation of the court in this area. These matters are considered in the judicial dispute resolution procedure proposed by CAMAC, below.

5.5 CAMAC proposal for enhanced judicial dispute resolution

5.5.1 Overview

As outlined in this Section, CAMAC proposes the enactment of enabling legislation[81] to give the court an enhanced role in the resolution of disputes involving charitable trusts administered by LTCs. This legislation would be in addition to the current inherent powers of the court in regard to these trusts. It should be implemented as part of Stage 1 (see Section 1.8.1 of this report).

The enabling legislation should deal with:

- standing to apply for a judicial hearing
- grounds for granting a hearing
- guidance on applying the primary intent of the donor
- powers of the court to make orders
- grounds of appeal
- costs of the parties.

The legislation should provide that the court means the Federal Court and any court of a State or Territory given jurisdiction to hear and decide applications pursuant to the enabling legislation.

While the CAMAC proposals in this Section focus on charitable trusts managed by LTCs, it is arguable that, in principle, and to achieve greater harmonization, a uniform and consistent approach to the role and powers of the court in dispute resolution should apply to all segments of the charities sector.

5.5.2 Standing to apply for a judicial hearing

Current position

Historically, the affairs of charitable trusts have been regulated through State and Territory laws and courts. While rules of standing to apply for a judicial hearing have differed, some jurisdictions have permitted an 'interested person' in the administration of a trust to apply for a judicial hearing. Generally, the courts have held that an 'interested person' is someone with an interest that is 'materially greater than or different from that possessed by ordinary members of the public'. That category could include a potential donee of a charitable trust.[82]

Under Chapter 5D of the Corporations Act, a 'person with a proper interest', as defined under s 601RAD, has standing to apply to the court in relation to various matters under that Chapter, the most relevant one being in relation to the power of the court in disputes alleging the charging of excessive fees.[83] In the context of a charitable trust, those persons

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81 The enabling legislation could be an additional Part of Chapter 5D of the Corporations Act.

82 *In re Hampton Fuel Allotment Charity* [1988] 3 WLR 513 per Nicholls LJ. See further GE Dal Pont *Law of Charity* (LexisNexis Butterworths, 1st ed, 2010) at 375.

83 s 601TEA. Other provisions involving a 'person with a proper interest' are ss 601SBA and 601SBB, dealing with accounts in relation to estates.

are set out in s 601RAD(1)(b), which includes 'a person of a class that the trust is intended to benefit'. There remains doubt, or differences of view, as to the width of that class. To date, there has been no judicial determination on the matter. Also, notably, co-trustees are not expressly included in the statutory definition.

Submissions

One proposal was that a regulator, such as the ACNC, be granted the power to make a preliminary assessment of whether a person should be classified as someone with a sufficient interest to apply for a judicial hearing and the merit of that person's claim. The regulator could consent to, or refuse, the interested person bringing such an action. Such an approach, it was argued, would dispense with the costs associated with seeking the leave of the court, while ensuring that only properly interested parties with a serious claim gain access to the court.

CAMAC approach

Application by the regulator

CAMAC proposes that the ACNC be given automatic standing to itself request a judicial hearing or to intervene at any stage in a hearing regarding the administration of a charitable trust commenced by any other party. The regulator might decide to act in response to complaints regarding a particular trustee or the administration of one or more trusts.

Application by other parties

CAMAC is of the view that the determination of the question of standing for persons other than the regulator should remain with the court, not an external body.

A broad test of standing should be adopted to include co-trustees and other persons with an interest in the administration of the trust, including actual and potential donees. This could be achieved by adopting in the enabling legislation the 'interested person' test as it has been interpreted by the courts, namely someone with an interest that is:

> materially greater than or different from that possessed by ordinary members of the public.[84]

It might be made clear in the Explanatory Memorandum to the enabling legislation that one of the intended effects of this proposed test is to permit applications to be made concerning trusts where an LTC is the sole trustee, where there are no involved parties that can be linked to the donor of that trust, and where there may be no recipients of benefits from the trust. Persons within any general class of potential donees of these sole trustee trusts may have such a material interest.

5.5.3 Grounds for granting a hearing

To curtail unmeritorious applications, CAMAC considers that the legislation should state that the court should hear a matter only if satisfied at the prima facie level that:

- the applicant with standing is acting in good faith
- there is a genuine dispute concerning the administration of a trust, and

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[84] *In re Hampton Fuel Allotment Charity* [1988] 3 WLR 513 at 520.

- it is in the best interests of the trust that the matter proceed to a hearing.

The legislation should also provide that where it is the regulator that makes an application, the court need only be satisfied as to the third element, namely that it is in the best interests of the trust to proceed to a hearing.

The legislation should further provide the court with a discretionary power to make directions for mediation between the parties before further considering a matter concerning a charitable trust. The Financial Ombudsman Service might be a suitable body to mediate in such cases.

5.5.4 Guidance on applying the primary intent of the donor

CAMAC proposes that guidance be provided to assist the court in determining a matter concerning a charitable trust in accordance with the primary intent of the donor.

This guidance, which could be set out in the Explanatory Memorandum to the enabling legislation, should include the following:

(1) the primary intent of the donor in establishing a charitable trust is to achieve the benevolent or philanthropic purposes or objectives for which the trust was created, (or to achieve the 'spirit' of the trust where its particular benevolent objectives can no longer be achieved), within the time-frame of the trust, and in an effective and efficient manner

(2) the administrative arrangements for a charitable trust should at all times be consistent with achieving the primary intent of the donor

(3) further to (2), the administrative arrangements of a charitable trust, including the fees and costs charged against the trust, the tenure of a trustee, and the relationship between co-trustees, should be assessed according to how well they achieve the primary intent of the donor

(4) the primary intent of the donor should prevail over any statement by the donor in a charitable trust instrument or otherwise as to the administrative arrangements for the trust, including the nomination of a particular trustee

Note: the commercial profile of a particular trustee (including in consequence of any internal changes of control of the trustee or external changes of control of any corporate group of which the trustee is a member), the particular tasks required of the trustee, and the markets within which the trust operates, may change over time, and in a manner unforeseen by the donor.

(5) in considering whether particular administrative arrangements should be changed in order to achieve the primary intent of the donor, the court may determine the matter:

- whether or not the donor was fully informed and independently advised on those administrative arrangements at the time of establishment of the trust

- notwithstanding that a trustee has not breached any legal or fiduciary obligation or requirement.

This guidance would provide the court with the flexibility to adjust administrative arrangements for a particular trust in a manner that departs from, or even in some respects is contrary to, the terms of the trust instrument, where the court considers that the adjustment is called for in order to achieve the primary intent of the donor of that trust.

5.5.5 Powers of the court to make orders

CAMAC considers that the court should be given a general power to consider any matter in dispute concerning a particular charitable trust being administered by an LTC, including any aspect of its administration, whether or not any allegation of breach or misconduct is being asserted.

Fees

CAMAC has earlier proposed that the court have an enhanced jurisdiction to deal with disputes alleging the charging of excessive fees or costs against a trust, whether in relation to the provision of traditional services or otherwise (see Section 3.5.4 of this report). The factors to be taken into account in reaching a determination would be those set out in the current legislation.[85]

The CAMAC proposals in this Section regarding the procedural aspects of any such application would substitute for the existing procedural provisions in s 601TEA.[86]

Replacing the trustee

CAMAC has earlier proposed that the court have an enhanced jurisdiction concerning whether the trustee of a particular charitable trust should be replaced (see Section 4.3.3 of this report).

The court could replace a trustee where it considers that this is called for to achieve the primary intent of the donor of the trust. The exercise of that power would not depend on the court being satisfied that any form of maladministration by the incumbent trustee has taken place.

Other matters affecting the trust

The court should also have the power to make other adjustments to the administration of a trust, where considered necessary to achieve the primary intent of the donor. The Explanatory Memorandum might set out examples of orders, including that:

- one or more unpaid (or minimum paid) independent trustee(s) be appointed to a trust, with powers to monitor the conduct of the LTC in administering the trust. This power would be particularly relevant in the context of sole trustee trusts

- a trustee provide certain disclosures to, or adopt some other course of conduct in relation to, a co-trustee or some other person.

Legal structure

The court should have the power, in exceptional cases, to convert the charitable trust into some other legal structure, such as a not-for-profit company or a PAF, where it considers

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85 s 601TEA(3).

86 If s 601TEA is to remain as a discrete provision, then the procedures in subsections (4)-(6) would need to be amended to bring them into line with the approach in Section 5.5 of this report.

that such a change is necessary in all the circumstances to fulfil the primary intent of the donor, which can no longer be attained by the continuance of the trust in its current form.

Evidence

CAMAC has also considered whether the strict application of the rules of evidence may unduly inhibit a bona fide party seeking to challenge any aspect of the administrative arrangements of a charitable trust.

While pre-trial discovery may be used to obtain admissible information, CAMAC can also see a benefit in giving the court a discretion not to be bound by the strict rules of evidence. The legislation could make clear that the court can determine the weight to be accorded to any information that it admits other than pursuant to the rules of evidence.

5.5.6 Grounds of appeal

The legislation should provide that any right of appeal against the determination of the court under the enabling legislation is limited to an error of law.

The Explanatory Memorandum could point out that, for the purpose of achieving finality within a reasonable time, the intention of this limited right of appeal is to exclude any form of re-hearing of the facts of the matter, or any challenge to the lawful exercise by the court at first instance of a discretion based on those facts.

5.5.7 Costs of proceedings

From time to time the courts have made determinations on disputed matters concerning charitable trusts. However, a number of respondents have argued that the potential costs of litigation act as a strong disincentive to the commencement of an action. For this reason, it is asserted, the existing judicial remedy may in large measure be beyond the reach of many bona fide involved parties.

Private parties

It has been argued in some submissions that trustees may have the comfort of indemnity rights against trust assets to cover their legal costs in judicial proceedings. By contrast, persons seeking to challenge the conduct of a trustee may remain personally exposed, including to any adverse costs order in the event that their application is unsuccessful.

For these reasons, CAMAC has considered two options:

- exclude all parties, including trustees, from recouping their costs from the assets of the trust in judicial dispute resolution matters, or
- expand the range of parties who may recoup their costs from the trust assets.

In regard to the first option, it may be argued that, given the benevolent and philanthropic purposes for which charitable trusts are established, their assets should only be used directly for those purposes. To permit a number of parties to, in effect, access these assets to fund court actions to settle their disputes, albeit ones directly related to the trust, may be difficult to reconcile with the charitable objectives of those trusts.

Notwithstanding this, CAMAC considers that excluding altogether a right of recoupment from trust assets could result in the judicial dispute resolution procedure becoming even more inaccessible, especially where there is a genuine dispute that needs to be resolved in the best interests of the trust.

On balance, CAMAC considers that the better approach is to increase the level of access to judicial dispute resolution by adoption of the second option. Without some financial comfort, recourse to the judicial process to resolve genuine disputes involving charitable trusts may largely be beyond the reach of deserving parties.

Under this approach, the legislation could set out the cost principles for parties in court actions involving charitable trusts, along the following lines:

> each party to have their reasonable costs met by the trust, except where the court is satisfied that a party has acted improperly, vexatiously or otherwise unreasonably, in which case the court can make such orders as to costs concerning that party as it thinks fit in the circumstances, including an order that the party shall bear all or some of its own costs and/or the costs, including on an indemnity basis, of another party to the hearing.[87]

CAMAC is aware that, in some cases, this prima facie right of access to trust assets could materially reduce those assets, thereby compromising to some extent the philanthropic or benevolent objectives of the trust. CAMAC considers, however, that the above costs constraints will act as a deterrent to unmeritorious claims.

The regulator

A further question arises as to whether the ACNC should be able to recoup its costs from the trust assets when it commences or intervenes in an action concerning a particular charitable trust.

An argument for recoupment is that costs incurred by the ACNC in what might, in effect, be an internal dispute within a particular charitable trust should not be borne from public revenue. A further argument in favour of recoupment is that parties might otherwise seek to have the ACNC, rather than themselves, initiate judicial proceedings, to avoid any drain on trust assets.

An argument against recoupment is that the ACNC regulates in the public interest, and recovery of its costs from private trusts is out of step with the performance of that role.

CAMAC considers that, on balance, the ACNC should not have a right of access to trust assets to recoup its costs when it commences or intervenes in an action concerning a particular charitable trust. CAMAC anticipates that the ACNC would initiate or intervene in proceedings to resolve a matter of material public interest, which should be funded from public revenue.

5.5.8 Implications of an enhanced judicial procedure

It is not possible at this point in time to accurately predict the extent of recourse to the proposed enhanced judicial dispute resolution procedure, if introduced.

On current indications, it may initially attract a number of applications, in particular in relation to some long-standing disputes. Equally, however, it may also provide an incentive for co-trustees or other interested parties to reach agreement on matters of contention, given the greater access of parties to the judicial review mechanism and the knowledge that the court can order them to mediation in any event.

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87 cf s 664F(4).

CAMAC considers that some time needs to be given for this judicial dispute resolution machinery to operate before any meaningful assessment of its effect can be made. It may then be possible to determine whether the enhanced court powers provide an effective mechanism to resolve disputes in this segment of the charities sector, or rather highlight embedded structural problems within the administration of charitable trusts which may need to be addressed by further legislative or other regulatory initiatives.

Appendix Terms of reference

20 September 2012

Ms Joanne Rees
Convenor
Corporations and Markets Advisory Committee
GPO Box 3967
SYDNEY NSW 2001

Dear Ms Rees

I am writing to refer to Corporations and Markets Advisory Committee a matter for its consideration and to report back to Government by May 2013. The matter relates to the regulation of certain aspects of the activities of trustee companies under the *Corporations Act 2001* and the portability of their services.

By way of background, in 2009 the Parliament passed the *Corporations Legislation Amendment (Financial Services Modernisation) Act 2009* (CLAFSMA). Among other things, this Act established a national regulatory framework for the traditional activities of trustee companies in the Corporations Act replacing diverse legislation that previously existed at the state/territory level.

One of the key objectives of the reforms was to promote efficient pricing of services provided by trustee companies.[88] As part of achieving this objective, the Act placed a cap on the amount a trustee corporation can charge a charitable trust to act as manager or trustee of either:

- a one-off capital commission of 5.5 per cent of the trust's assets plus an annual income commission of 6.6 per cent of the trust's income; or
- an annual management fee of 1.056 per cent of the trust's assets.

These provisions do not affect the ability of a charitable trust and the trustee company to negotiate different fee arrangements. The trustee company may also charge common fund administration fees and fees for returns for any duties or taxes. Fee arrangements already in place prior to this date were grandfathered and are not subject to these caps.

When introducing these reforms, the Government indicated that it would review the fee arrangements in the CLAFSMA after they had been in operation for two years.

In light of the objectives of the reforms and the experience of industry since the commencement of the reforms, I request that CAMAC inform the Government on:

88 Refer to Objective Six outlined in the Regulation Impact Statement.

- the impact the CLAFSMA has had on the quantum of fees that are, or could be, charged to Charitable Trusts and/or Foundations (Trusts) by Professional Trustee Companies (PTC) and the net funds available for Trusts to distribute to not-for-profit organisations. In doing so, consideration should be given to what fee arrangements would be available if Trusts were able to operate in an 'open' market;

- the range of additional fees beyond those regulated under CLAFSMA, that are, or could be, charged to Trusts by PTCs;

- the effectiveness of regulating 'new' fee arrangements between a PTC and a Trust in the manner contained in Division 4, Subdivision A of Part 5D.3;

- the effectiveness of grandfathering of 'existing' fee arrangements between a PTC and a Trust under Division 4, Subdivision B of Part 5D.3;

- what the current position is with regard to the removal and replacement of a trustee of a charitable trust, whether this position is unsatisfactory from a consumer protection perspective and if so, what, if any, reforms are necessary to address this; and

- other issues that impact on the objectives of CLAFSMA or the charitable purposes of trusts.

CAMAC may, depending on the issues raised under the sixth Term of Reference, choose to consider these issues further. Furthermore, for those issues which CAMAC considers are pertinent but is not in a position to review, CAMAC could bring these to the attention of the Government for its further consideration.

I note that CAMAC, as part of this review, will be consulting with interested parties including through the hosting of roundtables with relevant stakeholders.

Yours sincerely

BERNIE RIPOLL