

Using a Power of Advancement to Resettle on a New Trust

Generally, the income and capital of a trust can only be resettled (i.e. assets transferred from one trust to another trust) if there is a power in the trust deed to resettle or transfer the trust's income and capital to another trust ("power of resettlement"). An example of a circumstance when resettling an old trust into a new trust is advantageous is to reduce the administration costs of a number of old trusts by resettling them into one new trust.

What if there is no power of resettlement in a trust deed?

Unfortunately some trust deeds, particularly older ones, do not contain a power of resettlement. However, there are two ways that trustees can effect a resettlement without a power of resettlement, which are:

1. Power of advancement contained in the trust instrument

- Many trust deeds contain an express power of advancement ("power of advancement") which allows trustees to advance all or part of the income and capital of the trust for the purpose of maintenance, education, advancement or benefit of one or more beneficiaries.
- In *Pilkington v Inland Revenue Commissioner* [1962] 3 All ER 622 (House of Lords) the Court decided that trustees can use a power of advancement in a trust deed to effect a resettlement so long as certain criteria are met. These criteria are set out below.

2. Power of advancement contained in section 41 of the Trustee Act 1956

- Some trust deeds will not contain a power of advancement either. However, section 41 of the Trustee Act 1956 gives trustees a statutory power of advancement to apply up to one-half of the presumptive or vested share or interest of a beneficiary.
- Under the proviso to section 41, the High Court has discretion to apply a greater share.
- Section 41 gives trustees the power to resettle half of the income and capital of a trust into another trust so long as certain criteria are met, which are set out below.


What are the Criteria for using a power of advancement?

Trustees can use a power of advancement to effect a resettlement so long as the following criteria are met:

- The new trust is for the benefit of a beneficiary of the old trust;
- That beneficiary does not have a vested interest in the old trust; and
- The rule against perpetuities is not infringed.

1. The new trust is for the benefit of a beneficiary of the old trust

A beneficiary of the old trust must be benefited by resettling the old trust's income and capital on the new trust.



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It is important to note that a power of advancement must be genuinely exercised for the benefit of one or more beneficiaries. In the Pilkington case, the word “benefit” was interpreted to mean:

“any use of the money which will improve the material situation of the beneficiary....if the disposition itself, by which I mean the whole provision made, is for the beneficiary’s benefit, it is no objection to the exercise of the power that other persons benefit incidentally as a result of the exercise”.

An example of a benefit to beneficiaries when a power of advancement is used to effect a resettlement is to simplify the administration of a number of trusts which will reduce compliance costs in the future.

2. That beneficiary does not have a vested interest in the old trust

A power of advancement cannot be exercised to effect a resettlement to benefit a beneficiary who has a vested interest in the old trust. A vested interest does not include beneficial realisation of trust assets at the end of the perpetuity period of the old trust.

3. The rule against perpetuities is not infringed

The new trust’s perpetuity period (life of the trust) must expire on or before the termination date of the old trust. For example, if the old trust is due to be wound up on 1 January 2030, then the new trust’s perpetuity period must expire on or before 1 January 2030 to avoid infringing the rule against perpetuities.

Are there any gift duty implications of a resettlement?

Inland Revenue’s view on resettlements and gift duty is detailed in its Gift Duty Guide issued on 22 June 1999. Inland Revenue accepts that a resettlement made in accordance with an express power of advancement or resettlement in a trust deed or in accordance with a valid advancement under section 41 of the Trustee Act 1956, is not a gift. This means that capital resettlements made under power of advancements are not taxed if done correctly.

If you would like to discuss the above in more detail, please feel free to contact the writer or Dennis King.

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