Obligations and Powers of Superannuation Trustees concerning Situations of Actual or Possible Conflict

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Abstract

Part 1 summarises the present status as a matter of precedent in Australia of the general law rule that a fiduciary not be in a situation of conflict, the meaning of being "in a situation of conflict", and the recognised circumstances in which there is an exception to the rule. It also criticises the application of the rule to a superannuation trustee in *Jones v AMP Perpetual Trustee Co NZ Ltd*[1]. Part 2 considers the relationship of the pre-existing general law and statute law governing trusts to the provisions of the *Superannuation Industry (Supervision) Act 1993* ("*SIS Act*"). Part 3 considers the effect of the initial introduction of the *SIS Act* on the application of the no-conflicts rule to superannuation trusts. Part 4 considers how the replacement of the original statutory covenants in the *SIS Act* with a set that included express obligations concerning conflicts affects the possible application of the general law no-conflicts rule. It argues that it is still possible, in some circumstances, for the general law no-conflicts rule to apply, and considers the limitations on now amending a trust deed that did not already exclude the no-conflicts duty to amend or limit that duty. Part 4 also considers various aspects of the construction and practical application of the new covenants concerning conflicts, including the role of the prudential standards, and some other statutory amendments that came into operation in 2013 and 2019 that bear upon a trustee's actions in a situation of conflict. Part 5 provides several miscellaneous examples, discussed with particular reference to outsourcing, of principles that do not mention the word "conflict" but that could need to be taken into account when a superannuation trustee is in a situation of conflict.

Introduction

Superannuation trustees need to know what they are free to do, what they must do, and what they must not do when they are in a situation where there is a conflict or the possibility of conflict. This paper examines that question by considering the matter historically. It considers what the general law obligations and powers of a superannuation trustee concerning conflicts were before the *Superannuation Industry (Supervision) Act 1993 (Cth)* ("*SIS Act*") was enacted, then what the obligations and powers of the trustee were after the

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[1] [1994] 1 NZLR 690

SIS Act was enacted but before the amendments that took effect in 2013, and finally what those obligations and powers are after the 2013 amendments took effect.

The title of this paper has been chosen quite deliberately. It focuses on obligations and powers *concerning situations* of conflict. That is because, in deciding how to act concerning situations of actual or possible conflict the trustee cannot confine its attention to statutory provisions and statements of general law principles that include the word "conflict". There are quite a few principles of the general law, and provisions of legislation and legislative instruments, that have some apparently different subject matter but can be applicable in a situation of actual or possible conflict. It is not possible for this paper to identify them all, but it can indicate something of their potential range and variety.

PART 1 – GENERAL LAW PRINCIPLES CONCERNING CONFLICTS

First, there is nothing special about superannuation trustees so far as the application to them of the general law governing trustees is concerned. It is elementary that "the trusts of pension funds are in general governed by the ordinary law of trusts, subject to any contrary provision in the rules or other provisions which governed the trust."[2].

Second, all trustees are fiduciaries[3]. Indeed, the trust is the archetype of the fiduciary[4]. Thus, the law concerning the duties of a fiduciary applies to trustees of superannuation funds. This brings with it the obligation of the trustee to act at a standard higher than the usual standards of the marketplace[5]. A superannuation trustee must behave better than the ordinary businessperson or business corporation.

Third, current Australian authority, established by several High Court cases, is that there are only two distinctively fiduciary duties. They are both proscriptive duties – ones that say what the fiduciary *must not* do, rather than prescriptive duties that say what the fiduciary *must* do.

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[2] *Cowan v Scargill* [1985] 1 Ch 270 at 290 per Megarry V-C; *Bathgate v National Hockey League Pension Society* (1994) 16 O R (3d) 761 per Morden ACJO, Houlden & Goodman JJA. The possibility that the trust instrument alters the application of "the ordinary law of trusts" to a particular trust is itself part of the ordinary law of trusts – see section 1.2.1 below.

[3] *Visnic v Sywak* [2009] NSWCA 173; (2009) 57 ALR 517 at [34], [48]; *Breen v Williams* (1996) 186 CLR 71 at 137; J D Heydon & M J Leeming, *Jacobs' Law of Trusts in Australia* (8th ed LexisNexis Butterworths Australia 2016) (hereinafter *Jacobs on Trusts*) at [2-02]

[4] *Maguire v Makaronis* (1997) 188 CLR 449 at 473 per Brennan CJ, Gordon, McHugh and Gummow JJ

[5] Over 90 years ago Cardozo J said:

> "A trustee is held to something stricter than the morals of the market place. Not honesty alone, but the punctilio of an honor the most sensitive, is then the standard of behaviour. As to this there has developed a tradition that is unbending and inveterate. Uncompromising rigidity has been the attitude of Courts of equity when petitioned to undermine the rule of undivided loyalty by the 'disintegrating erosion' of particular exceptions. Only thus has the level of conduct for fiduciaries been kept at a level higher than that trodden by the crowd. It will not consciously be lowered by any judgment of this Court.": *Meinhard v Salmon* 249 NY 458 (1928) at 464.

His remarks have been endorsed repeatedly by the Australian appellate courts, most recently in *Northern Territory v Griffiths* [2019] HCA 7, 364 ALR 206 at [338]; *Lifeplan Australia Friendly Society Limited v Ancient Order of Foresters in Victoria Friendly Society Limited* [2017] FCAFC 74, 250 FCR 1 at [63]; *Paciocco v Australia and New Zealand Banking Group Ltd* [2015] FCAFC 50, 236 FCR 199 at [270]; *Vines v Australian Securities and Investment Commission* [2007] NSWCA 75, 73 NSWLR 451 at [779]; *Betella v O'Leary* [2001] WASCA 266 at [4]; *Warman International Ltd v Dwyer* (1995) 182 CLR 544 at 557.

The formulation that the High Court has adopted is this statement by Gaudron and McHugh JJ in *Breen v Williams*:

> "… Australian courts only recognize proscriptive fiduciary duties … In this country, fiduciary obligations arise because a person has come under an obligation to act in another's interests. As a result, equity imposes on the fiduciary proscriptive obligations -- not to obtain any unauthorised benefit from the relationship and not to be in a position of conflict. If these obligations are breached, the fiduciary must account for any profits and make good any losses arising from the breach. But the law of this country does not otherwise impose positive legal duties on the fiduciary to act in the interests of the person to whom the duty is owed."[6].

I will call this passage "the Two Duties Quotation".

There is some argument afoot about whether as a matter of principle, despite the current view of the High Court, all fiduciary duties are proscriptive, and whether there are only two fiduciary duties. Some judges and commentators argue that there can be more fiduciary duties than these two. They argue that a fiduciary, and in particular a trustee, can be under certain duties that require positive action that and are properly classified as fiduciary duties[7]. This paper will not get involved in that argument – what matters for the purpose of this paper is that under the general law, because a superannuation trustee is a fiduciary, it is subject to the fiduciary obligation not to be in a position of conflict.

1.1 "Obligation Not to Be in a Position of Conflict"

Some elaboration is needed concerning what the general law regards as the "position of conflict" that a fiduciary is obliged to avoid.

1.1.1 The types of conflict

First, for a conflict to be a relevant one, it must arise concerning activities of the fiduciary that are within the scope of the fiduciary duty in question[8]. For example, the trustee of a trust whose only asset is a parcel of land is free to purchase shares for his own benefit even if that purchase is unfavourable to the interests of the trust beneficiary, provided only that the

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[6] *Breen v Williams* (1996) 186 CLR 71 at 113 per Gaudron and McHugh JJ; adopted verbatim by McHugh, Gummow, Hayne and Callinan JJ in *Pilmer v Duke Group Ltd (In Liquidation)* (2001) 207 CLR 165 at [74]; *Youyang v Minter Ellison* [2003] HCA 15, 212 CLR 484 at [41]

[7] *Westpac Banking Corporation v The Bell Group (in liq) (No 3)* (2012) 44 WAR 1 esp at [900] – [902] per Lee AJA, [1957] – [1978] per Drummond AJA, [3036] (where Carr AJA is led by authority to the strained view that a director's duties to act bona fide in the interests of the company and to exercise powers for the proper purpose are proscriptive duties); *Pilmer v Duke Group Ltd (In Liquidation)* (2001) 207 CLR 165 at [128] per Kirby J (dissenting); J D Heydon, M J Leeming & P G Turner, *Meagher Gummow & Lehane 's Equity Doctrines and Remedies* (5th ed LexisNexis Butterworths Australia 2015) (hereinafter *MGL*) at [5-385]-[5-440]. *Jacobs on Trusts* at [16-01] argues that the High Court decisions holding that the only fiduciary duties are the proscriptive ones have been weakened by the decision in *Pitt v Holt* [2013] 2 AC 108, and claims at [17-04] that a trustee's duty to adhere to the terms of the trust "is a positive, prescriptive duty, not a negative, proscriptive duty. It has been described, rightly, as a 'fiduciary' duty.". See also Lionel Smith "Prescriptive Fiduciary Duties" (2018) 37 (2) University of Queensland Law Journal 261

[8] *Aas v Benham* [1891] 2 Ch 244; *Warman International Ltd v Dwyer* (1995) 182 CLR 544 at 559; *Howard v Commissioner of Taxation* [2014] HCA 21, 253 CLR 83 at [34], [91], [111]; *North and South Trust Co v Berkeley* [1971] 1 WLR 470 at 486

purchase of the shares is not connected in any way to his trusteeship of the land. That is because the trustee owes fiduciary duties only concerning the land, so in purchasing the shares he does not owe any relevant fiduciary duty, and thus there is no conflict between his duty to the beneficiary and his personal interest.

Second, the general law requires four different types of conflict to be avoided. The first is a conflict between the interests of the trustee and those of the beneficiary. The currently authoritative statement of this aspect of the "no conflicts" principle in Australian law is that it is:

> "an obligation not to promote his personal interest by making or pursuing a gain in circumstances in which there is a conflict or a real or substantial possibility of a conflict between his personal interests and those of the persons who he is bound to protect."[9]

Though this statement comes from the dissenting judgment of Mason J in *Hospital Products*, it has since been adopted by a majority in the High Court[10].

The "personal interest" of the fiduciary that is involved might be his interest in acquiring a benefit for himself, or it might be his interest in having a benefit arise for a third party whom he favours[11]. The interest of the fiduciary or the third party might be pecuniary or nonpecuniary, direct or indirect. A nonpecuniary interest includes an interest by way of association, whether through kinship or business connection[12]. However, the interests of the beneficiary that are relevant to the no-conflict rule are only economic ones, not, for examples, any interest in not being sexually abused or physically maltreated. That is because the law recognises as fiduciary relationships only ones which protect economic interests of the beneficiary[13].

The second type of conflict that the "no conflicts" rule requires to be avoided is between the duty that the fiduciary owes to the beneficiary and the duty that he owes to someone else[14].

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[9] *Hospital Products Ltd v United States Surgical Corporation* (1984) 156 CLR 41 at 103.
[10] *Pilmer v Duke Group Ltd (In Liquidation)* (2001) 207 CLR 165 at [78]
[11] Eg a company in which the fiduciary has a commercially significant shareholding (*Transvaal Lands Company v New Belgium (Transvaal) Land and Development Co* [1924] 2 Ch 488 at 503-4), a partnership of which the fiduciary is a salaried partner but not an equity partner (*In Re Hill; Claremont v Hill* [1934] Ch 623), the fiduciary's employer (*In Re F T Hawkins & Co Ltd* [1952] Ch 881),,or a local real estate agent who a solicitor wants to help (*Haywood v Roadknight* [1927] VLR 512 per Dixon AJ).
[12] *Settlement Agents Supervisory Board v Property Settlement Services Pty Ltd* [2009] WASCA 143 at [71] per McLure JA (Owen and Newnes JJA agreeing)
[13] *Paramasivam v Flynn* (1998) 90 FCR 489 at 504, 507-8; *Michael Brown v State of New South Wales* [2008] NSWCA 287 at [34]-[40]; *Pope v Madsen* [2015] QCA 036, [2016] 1 Qd R 201 at [33]
[14] *Transvaal Lands Company v New Belgium (Transvaal) Land and Development Co* [1924] 2 Ch 488 at 497, 501, 503 (trustee who is also company director cannot purchase from the company); *Fulwood v Hurley* [1928] 1KB 498 at 502; *Moody v Cox and Hatt* [1917] 2 Ch 71 at 81 per Lord Cozens-Hardy MR ("A solicitor may have a duty on one side and a duty on the other, namely a duty to his client as solicitor on the one side and a duty to his beneficiaries on the other; but if he chooses to put himself in that position it does not lie in his mouth to say to the client "I have not discharged that which the law says is my duty towards you, my client, because I owe a duty to the beneficiaries on the other side." The answer is that if a solicitor involves himself in that dilemma it is his own fault. He ought before putting himself in that position to inform the client of his conflicting duties, and either obtain from that client an agreement that he should not perform his full duties of disclosure or say – which would be much better – "I cannot accept this business."); *North and South Trust Co v Berkeley* [1971] 1 WLR 470 at 484-5 ("fully informed consent apart, an agent cannot lawfully place himself in a position in

The third is between the interest of the beneficiary and the duty that the fiduciary owes to someone else. The fourth is between the duty of the fiduciary to the beneficiary and the interests of the fiduciary. In many cases the duty of the fiduciary to the beneficiary will be to promote the interests of the beneficiary, so this fourth type of conflict could also be analysed as being the first type of conflict. However not all of the duties of the fiduciary to the beneficiary will be of that type. For example, it would be odd to characterise the duty of a trustee to act fairly between different classes of beneficiaries as a duty to promote the interests of the beneficiaries.

1.1.2 Obligation to avoid possible conflicts as well as actual conflicts?

1.1.2.1 the Original English Orthodoxy

There is long-standing English authority that the obligation of a fiduciary is not only to avoid situations where there is an actual conflict, but also situations where there is a possible conflict[15]. One of its sources is the speech of Lord Cranworth LC in *Aberdeen Railway Co v Blaikie, Brothers*[16]

> "… It is a rule of universal application, that no one, having [fiduciary] duties to discharge, shall be allowed to enter into engagements in which he has, or can have, a personal interest conflicting, *or which possibly may conflict*, with the interests of those whom he is bound to protect"

Lord Upjohn[17] has explained that passage as follows:

> "the phrase "possibly may conflict" requires consideration. In my view it means that the reasonable man looking at the relevant facts and circumstances of the particular case would think that there was a real sensible possibility of conflict; not that you could imagine some situation arising which might, in some conceivable possibility in events not contemplated as real sensible possibilities by any reasonable person, result in a conflict."

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which he owes a duty to another which is inconsistent with his duty to his principal …"); *in re McIntosh (No 4); Perpetual Trustee Co Ltd v McIntosh* (1905) 5 SR (NSW) 389; *in re Service* (1914) 31 WN (NSW) 95 (trustee of one estate not to advance money to another estate of which it is also trustee); *Beach Petroleum NL v Kennedy* [1999] NSWCA 408, (1999) 48 NSWLR 1 at [196], [202]. See generally Matthew Conaglen, *Fiduciary Loyalty* (Hart Publishing Oxford 2011) p 142 – 158.

[15] In *Regal (Hastings) Ltd v Gulliver* (decided in 1942, but reported at [1967] 2 AC 134) Viscount Sankey said, at 137 "The general rule of equity is that no one who has duties of a fiduciary nature to perform is allowed to enter into engagements in which he has *or can have* a personal interest conflicting with the interests of those whom he is bound to protect." (Emphasis added). In *Boardman v Phipps* [1967] 2 AC 46 at 88 Viscount Dilhorne dissented in the application of principle to the facts, but accepted that the relevant principle was that there was no liability because there was no "conflict *or possibility of a conflict* between the personal interests of the appellant's and those of the trust.", while Lord Cohen held at 104 there was liability because there was "a *possibility of a conflict* between his interest and his duty". See also per Lord Hodson at 111, 123-124 per Lord Upjohn

[16] (1854) Macq 461 at 471, emphasis added. Lord Scarman, delivering the advice of the Privy Council in appeal from New South Wales, said that this was an authoritative declaration of the law: *Queensland Mines Ltd v Hudson* (1978) 18 ALR 1 at 3.

[17] *Boardman v Phipps* [1967] 2 AC 46 at 124. Even though Lord Upjohn dissented in *Boardman v Phipps*, this explanation has force in Australian law because Mason J specifically referred to it in *Hospital Products* at 103, and Lord Scarman accepted it in *Queensland Mines v Hudson* at 3.

Earlier, as Upjohn LJ[18], he had similarly said:

> " … a broad rule like this must be applied with common sense and with an appreciation of the sort of circumstances in which over the last 200 years and more it has been applied and thrived. It must be applied realistically to a state of affairs which discloses a real conflict of duty and interest and not to some theoretical or rhetorical conflict."

One part of the justification for the obligation to avoid being in a situation where there was merely a possible conflict was explained by Lord Herschell in *Bray v Ford*[19]:

> "… human nature being what it is, there is a danger, in such circumstances, of the person holding the fiduciary position being swayed by interest rather than by duty, and thus prejudicing those whom he was bound to protect. It has, therefore, been deemed expedient to lay down this positive rule."

1.2.2.2 Sir Frederick Jordan's Challenge to the Orthodox View

For a few decades there was a question about whether the Australian law continues to recognise a legally enforceable obligation to avoid being in a situation of conflict. It arose from some remarks of Sir Frederick Jordan, and their adoption by two very highly regarded judges, though not by a majority, in two High Court cases. In *Chapters on Equity in New South Wales* Sir Frederick said:

> "It has often been said that a person who occupies a fiduciary position ought to avoid placing himself in a position in which his duty and his interest, or two different fiduciary duties, conflict.
>
> That is rather a counsel of prudence than a rule of equity; the rule being that a fiduciary must not take advantage of such a conflict if it arises."[20]

Deane J adopted that remark in *Chan v Zachariah*[21], and continued:

> 'indeed, even as an unqualified counsel of prudence it may, in some circumstances, be inappropriate: se eg *Hordern v Hordern* [1910] AC 465 at p 475; *Smith v Cock (*1911) 12 CLR 30 at pp 36-37; [1911] AC 317 at pp 325-326. The equitable principle *governing the liability to account* is concerned not so much with the mere existence of a conflict between personal interest and fiduciary duty as with the pursuit of personal interest by, for example, actually entering into a transaction or engagement "in which he has, or can have, a personal interest conflicting … with the interests of those whom he is bound to protect" (per Lord Cranworth LC, *Aberdeen Railway Co v*

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[18] *Boulting v Association of Cinematograph, Television and Allied Technicians* [1963] 2 QB 606 at 637-8

[19] at 51-52, approved by Gaudron and McHugh JJ in *Breen v Williams* at 108. Other judges have expressed much the same thought in different words: "the rule is so to speak good for discipline: [it is] calculated to deter agents from behaving in that way" (*Phipps v Boardman* (1965] Ch 992 at 1031 (CA)); "equity imposes stringent liability on a fiduciary as a deterrent – *pour encourager les autres*" (*Murad v Al-Saraj* [2005] EWCA Civ 959, [2005] WTLR 1573 at [74]).

[20] Sir Frederick Jordan, *Chapters on Equity in New South Wales* (sixth edition by FC Stephen, Sydney, 1947) p 115

[21] (1984) 154 CLR 178 at 198 (emphasis added)

> *Blaikie Bros*) or the actual receipt of personal benefit or gain in circumstances where such conflict exists or has existed.'

Deane J recognised[22] that, in the varying formulations of the principle governing liability of fiduciaries to account there are two themes:

> "The first is that which appropriates for the benefit of the person to whom the fiduciary duty is owed any benefit or gain obtained or received by the fiduciary in circumstances where there existed a conflict of personal interest and fiduciary duty *or a significant possibility* of such conflict: the objective is to preclude the fiduciary from being swayed by considerations of personal interest. The second is that which requires the fiduciary to account for any benefit or gain obtained or received by reason of or by use of his fiduciary position or opportunity or knowledge resulting from it: the objective is to preclude the fiduciary from actually misusing his position for his personal advantage."

He concluded[23] that:

> "Stated comprehensively in terms of the liability to account, the principle of equity is that a person who is under a fiduciary obligation must account to the person to whom the obligation is owed for any benefit or gain (i) which has been obtained or received in circumstances where a conflict *or significant possibility* of conflict existed between his fiduciary duty and his personal interest in the pursuit or possible receipt of such a benefit or gain or (ii) which was obtained or received by use or by reason of his fiduciary position or of opportunity or knowledge resulting from it."

It will be seen that what Deane J has done here is to move away from what Sir Frederick Jordan was talking about, namely what the obligation of a fiduciary is concerning action that he takes, and to talk instead about the circumstances in which a fiduciary must submit to a particular equitable remedy, that of account. It is necessarily true that it is only if a benefit or gain has actually been received that there can be an obligation to account. Deane J accepts that the obligation to account exists both when the benefit or gain was received when there was an actual conflict of duty and interest, or when there was a significant possibility of conflict[24].

In *Hospital Products* at page 103 Mason J said early on the page that he agreed with a finding by the trial judge that the defendant was under a duty "that within the ambit of its fiduciary responsibility it should not act in a way in which there was a possibility of conflict between its own interests and those of [its beneficiary]". While he says that the fiduciary must not *act* in a way in which there was a possibility of conflict, entering a situation of potential conflict can be acting. At that stage his Honour appears to be accepting the orthodox position concerning possible conflicts.

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[22] at 198-9, emphasis added
[23] At 199, emphasis added
[24] Deane J's remark that *Hordern v Hordern* and *Smith v Cock* show that it is not always an appropriate counsel of prudence to say that a fiduciary should not place himself in a situation of conflict is readily explained. Both *Hordern* and *Smith* were cases that held that if A is appointed to a position that confers a discretionary power that is capable of benefiting himself, he is not precluded from taking the position. See Section 1.2.3, "Conflict created by the settlor as an exception to the "no conflicts' obligation", below

However, further down the page, after referring to Sir Frederick Jordan's remark, he said:

> "Accordingly, the fiduciary's duty may be *more accurately* expressed by saying that he is under an obligation not to promote his personal interest by making or pursuing a gain in circumstances in which there is a conflict or a real or substantial possibility of a conflict between his personal interests and those of the persons whom he is bound to protect."

That formulation is one that states the duty in terms of what the fiduciary must not do *when in* a situation of conflict or possible conflict. It goes further than Deane J's formulation because it seems to accept that there woud be a breach if a gain was pursued while the fiduciary was in a situation of conflict, even if the gain had not actually been made. But it does not say that the fiduciary has an obligation not to be in the situation of conflict or possible conflict at all. This raises a question of whether Australian law currently recognises an obligation for a fiduciary not to be in a position of conflict.

1.1.2.3 Orthodoxy Re-Established

Later authority makes clear that there is still a general law obligation for a fiduciary to avoid being in a situation of conflict. *Chan v Zachariah* was decided in June 1984, *Hospital Products* in October 1984. Notwithstanding what Deane J and Mason J had said in those cases, in 1991 a strong bench of the Full Federal Court[25] was able to say, with no qualifications:

> "Not only must the fiduciary avoid, without informed consent, placing himself in a position of conflict between duty and personal interest, but he must eschew conflicting engagements.[26]"

Further, in 1996 McHugh and Gaudron JJ in *Breen v Williams* were able to say that the distinctive fiduciary obligations included the proscriptive obligation "not to be in a position of conflict". The importance of this statement is all the greater because the Two Duties Quotation clearly aims to be an exhaustive statement of the full extent of the fiduciary duties.

Decisively, so far as precedent is concerned, the majority judgment in *Pilmer*[27] in 2001 quoted verbatim[28] the Two Duties Quotation from the judgment of Gaudron and McHugh JJ in *Breen v Williams*, that stated one fiduciary obligation as being one not to be in the situation of conflict. Their Honours in *Pilmer* also said[29]:

> "In particular, the fiduciary is under an obligation, without informed consent, not to promote the personal interests of the fiduciary by making or pursuing a gain in circumstances in which there is "a conflict or a real or substantial possibility of a conflict" between personal interests of the fiduciary and those to whom the duty is

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[25] Davies, Sheppard and Gummow JJ
[26] *Commonwealth Bank of Australia v Smith* (1991) 42 FCR 390 at 392. For completeness I mention that in 1995 the joint judgment in *Warman International Ltd v Dwyer* (1995) 182 CLR 544 at 557 said that a fiduciary must account for a profit or benefit obtained "when there was a conflict or possible conflict between his fiduciary duty and his personal interest". However, this statement was made in a case where account was the only remedy in question, and there was no occasion to make a statement of the full extent of the duties of the fiduciary.
[27] *Pilmer v Duke Group Ltd (in liq)* (2001) 207 CLR 165
[28] at [74]
[29] At [78]

> owed. This is how the matter was put by Mason J in *Hospital Products*. Similar reasoning applies where the alleged conflict is between competing duties, for example, where a solicitor acts on both sides of a transaction."

The only way I can reconcile these two different aspects of the judgment in *Pilmer* is that their Honours continue to recognise an obligation for a fiduciary not to be in a situation of conflict, and that the obligation as stated by Mason J in *Hospital Products* is a particular aspect or consequence of it.

Later judgments of the High Court have referred to the Two Duties Quotation in *Breen* as authoritative[30]. I am also comforted that Gageler J has very recently confirmed that the Two Duties Quotation continues to be the law in Australia[31], and has stated the fiduciary law in terms involving there being an obligation not to place oneself in a position of conflict[32]. I conclude that there remains an obligation in Australian law for a fiduciary to avoid being in a situation of conflict. Further, the situation of conflict that is to be avoided includes one where there is a real possibility of conflict[33].

1.1.2.4 Correctness of Orthodox View Demonstrated by Availability of injunction to restrain a possible conflict

A litmus test for there being a fiduciary obligation not to be in a position of possible conflict is whether an injunction is available as a remedy to stop either an ongoing breach of the obligation, or an expected breach of the obligation[34]. If the duty were to be formulated in the narrower way that Deane J formulated it, and that were the only aspect of a fiduciary duty that relates to possible conflicts, only a remedy of account would be available. If the duty were tobe formulated in the way Mason J did an injunction would be available to stop an

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[30] *Friend v Brooker* [2009] HCA 21, 239 CLR 129 at [84]; *Ancient Order of Foresters in Victoria Friendly Society Ltd v Lifeplan Australia Friendly Society Limited* [2018] HCA 43, 360 ALR 1 at [67] ; *Howard v Commissioner of Taxation* [2014] HCA 21, 253 CLR 83 at [33] per French CJ and Keane J, at [56] per Hayne and Crennan JJ

[31] Stephen Gageler, "Expansion of the Fiduciary Paradigms into Commercial Relationships: the Australian Experience" in Peter Devonshire and Rohan Havelock (eds) *The Impact of Equity and Restitution in Commerce* (Bloomsbury Publishing plc 2018) 165 at 169

[32] Ibid at 170 (twice), 173

[33] In *Clay v Clay* [2001] HCA 9, 202 CLR 410 at [55] the reason given by the joint judgment of Gleeson CJ, McHugh, Gummow, Hayne and Callinan JJ for holding there was no breach of fiduciary duty was that "there is no sensible real or substantial possibility of conflict in the necessary sense". That a fiduciary has an obligation not to be in a situation of conflict or possible conflict was accepted as the relevant law in cases including *Settlement Agents Supervisory Board v Property Settlement Services Pty Ltd* [2009] WASCA 143 at [4]-[7] per Owen JA, [72]-[73], [75]-[76] per McLure JA (Owen and Newnes JJA agreeing), *In the matter of Gladstone Pacific Nickel Ltd* [2011] NSWSC 1235, 86 ACSR 432 at [67], [69]-[70], *Brady Street Developments Pty Ltd v M E Asset Investments Pty Ltd* [2013] NSWSC 1755 at [13], [46], [55] and *Bell Group Ltd v Westpac Banking Corporation (No 9)* [2008] WASC 239, 39 WAR 1 at [4506], [4508].

[34] In general, an injunction is available to restrain trustees from engaging in a breach of trust: *Balls v Strutt* (1841) 1 Hare 146, 66 ER 984; *Dance v Goldingham* (1873) LR 8 Ch App 902; *Park v Dawson* [1965] NSWR 298 at 300 – 301; *Kerr on Injunctions* (6th ed Sweet & Maxwell London 1927) p 506 – 512; *Jacobs on Trusts* [16-03]. Such an injunction might be one to restrain an ongoing breach of a trustee's obligation not to be in a situation of conflict, or it might be a *quia timet* injunction to restrain an anticipated breach of that obligation: *In Re Thomson; Thomson v Allen* [1930] 1 Ch 203, a decision accepted by Mason J in *Hospital Products* at 103, Gibbs J in *Consul Development Pty Ltd v DPC Estates Pty Ltd* (1975) 132 CLR 373 at 394 , and in *Settlement Agents Supervisory Board v Property Settlement Services Pty Ltd* [2009] WASCA 143 at [73] .

ongoing or expected pursuit of a gain while in a situation of conflict, but not to prevent the fiduciary being in a situation of conflict at all.

Case law of the last few decades has confirmed the availability of an injunction to restrain a fiduciary being in a situation of actual or potential conflict. Many of the cases concern solicitors, and the cases must be approached bearing in mind that only comparatively recently has it become clear that the solicitor's fiduciary duty to a client comes to an end when the retainer has been fully performed[35]. There are many cases where a solicitor's *former* client obtains an injunction to prevent a solicitor from acting contrary to that client's interests by taking on a new client[36], but the better view is that these can now be justified only on the basis of preservation of confidential information, or the court's inherent power to protect the integrity of the administration of justice[37], not by any no-conflicts duty of the solicitor that continues after the end of the retainer.

However, there are also cases that recognise that an *existing* client of a solicitor can obtain an injunction, based on an apprehended breach of the no-conflicts rule, to prevent the solicitor from taking on or continuing to act for a new client when to do so could be contrary to the interests of the existing client[38]. An injunction to stop a possible conflict is not only available concerning conflicts of interest. An injunction can prevent a solicitor from continuing in a situation of owing conflicting duties by acting for one client to defeat a claim

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[35] It was first made clear only in *Prince Jefri Bolkiah v KPMG* [1999] 2 AC 222 at 235 per Lord Millett (with whom Lord Browne Wilkinson, Lord Hope of Craighead, Lord Clyde and Lord Hutton agreed.) There is an exception to this principle when the fiduciary deliberately resigns his position to enable himself to carry out an act that would be a breach of the no-conflicts rule if he did not resign: *Gould v O'Carroll* [1964 NSWR 803 at 805, and see Conaglen, *Fiduciary Loyalty*, p 188 – 190. In *Ismail-Zai v Western Australia* [2007] WASCA 150, (2007) 34 WAR 379 at [20] – [24] Steytler JA collected authorities that support the fiduciary duty ending when the retainer ends, and those that held that it can continue, and preferred the former. Since then *Cooper v Winter* [2013] NSWCA 261 at [92]-[102], [136], *Dealer Support Services Pty Limited v Motor Trades Association of Australia Ltd* (2014) 228 FCR 252 at [36], [40] – [89]; *Maxwell-Smith v S & E Hall Pty Ltd* [2014] NSWCA 146; (2014) 86 NSWLR 481 at [24] and *Técnicas Reunidas v Andrew* [2018] NSWCA 192 at [36] have all held that no fiduciary duty survives termination of a solicitor's retainer.

[36] *National Mutual Holdings Pty Ltd v The Sentry Corporation* (1989) 22 FCR 209 at 228 – 230; *Mallesons Stephen Jaques v KPMG Peat Marwick* (1990) 4 WAR 357 at 362-3 (both of which appear to assume that the fiduciary obligations survive termination of the retainer, and adopts the no-conflicts rule as one basis for grant of the injunction); *Farrow Mortgage Services Pty Ltd (in liq) v Mendall Properties Co Ltd* [1995] 1 VR 1 at 5 per Hayne J; *Newman v Phillips Fox* [1999] WASCA 171, (1999) 21 WAR 309 at [63]; *Dealer Support Services Pty Limited v Motor Trades Association of Australia Ltd* (2014) 228 FCR 252 at [34]; *World Medical Manufacturing Corporation v Phillips Ormonde & Fitzpatrick Lawyers* [2000] VSC 196 at [120]; *Sent v John Fairfax Publication Pty Ltd* [2002] VSC 429 at [33] per Nettle J; *Belan v Casey* [2002] NSWSC 58 at [21]; *Asia Pacific Telecommunications Ltd v Optus Networks Pty Ltd* [2005] NSWSC 550 at [51] – [55]; *Babcock & Brown Diff III Global Co-Investment Fund LP v BBLP LLC* [2015] VSC 453 at [70]

[37] See the cases collected in *Ismail-Zai* at [30] – [40]

[38] *Prince Jefri Bolkiah* at 124-5, approved by Brereton J in *Kallinicos v Hunt* [2005] NSWSC 1181, 64 NSWLR 561 at [35], [76]; *Newman v Phillips Fox* [1999] WASCA 171, (1999) 21 WAR 309 at [20] ; *Marks & Spencer plc v Freshfields Bruckhaus Derringer* [2004] EWHC 1337, [2004] 1 WLR 2331, [26]-[27] of which makes clear that actual or potential conflict of interest was the principal and sufficient ground for granting the injunction, with protection of confidential information as an alternative ground. The decision was affirmed at [2004]EWCA Civ 741. In *Kallinicos v Hunt* at [70] – [72] and [87] – [89] Brereton J granted an injunction against a solicitor acting partly on the basis of the court's disciplinary power over solicitors, but also on the basis that a solicitor whose conduct could be called into question in litigation should not act in that litigation because there would be a conflict between his interest in preserving his personal integrity and his duty to his client and the court. See also *Snell's Equity* 34th ed (Sweet & Maxwell 2020) at 7-064.

made against a fund while also acting for the administrator of that fund whose duty is to impartially decide whether to allow claims against that fund[39]. That such a *quia timet* injunction is available shows that there continues to be a legally enforceable duty for a fiduciary not to enter a situation of possible conflict[40].

It would be undesirable from a policy point of view if there were no such duty. Judges and commentators often refer to the "prophylactic function" of the rule that a fiduciary avoid being in a situation of conflict – it is a rule that is clear and simple, and aims to prevent a fiduciary being at risk of failing to be loyal to his beneficiary. As well, if a fiduciary is in a situation where there is a real possibility of a conflict, and the fiduciary actually prefers his own interest, or prefers to perform the duty owed to someone else, the person owed the duty will sometimes not find out until after the breach. Even if the breach is discovered any remedy that is given after the breach will sometimes be inadequate. One way of lessening the risk of these consequences arising is to have a rule saying that there cannot be any such conflict. It lessens the risk because many people will try to perform their legal obligations if they are told what they are, and a simple rule requiring the avoidance of situations where there is a real possibility of a conflict is one that solicitors who are giving advice can easily communicate.

1.2 Juristic Nature of the "No Conflicts" Obligation

Some elaboration is also needed concerning the type of legal rule that the obligation of a fiduciary to avoid conflicts is. Like most, maybe all, equitable rules, it is not a rigid rule that must always be obeyed come what may[41]. Rather, it is a default rule, that will apply unless there is some reason of equitable principle why it should not apply in particular circumstances[42].

When there is a principle that stops the no-conflicts rule from applying in particular circumstances the explanation for why the rule stops applying will depend upon the type of conflict that is involved. If the conflict is one between the interest of the trustee and the interest of the beneficiary, or between the interest of the beneficiaries and the duty the trustee owes to someone else, the interests that are involved are ones that exist as a matter of fact. If a principle stops the no-conflicts rule from applying to that type of conflict it is not as though the conflict stops existing – rather, the conflict becomes one that is permissible. However, if the conflict is one between the trustee's duty to the beneficiary and the duty the trustee owes to someone else, or between the duty that the trustee owes to the beneficiary

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[39] *Horne (Trustee), in the matter of Pruzanski* [2000] FCA 151, approved in *Re Temple* [2000] FCA 1406

[40] That there is an obligation for a trustee not to enter a situation of possible conflict is relevant to what is the feared legal wrong that could justify the grant of a *quia timet* injunction. In deciding whether to grant a *quia timet* injunction the task of the court is "balancing the magnitude of the evil against the chance of its occurrence": *Earl of Ripon v Hobart* (1834) 3 My & K 169 at 176, 40 ER 65 at 68, and see generally ICF Spry, *Equitable Remedies* (9th ed Lawbook Co Australia 2014) p 391 - 5. When the evil is the trustee being in a situation of possible conflict, a *quia timet* injunction is easier to obtain than if the relevant evil were being in a situation of actual conflict.

[41] In *Hospital Products* (1984) 156 CLR 41 at 102-103 Mason J said that "the so-called rule that the fiduciary cannot allow a conflict to arise between duty and interest … cannot be usefully applied in the absolute terms in which it has been stated". Gleeson CJ, McHugh, Gummow, Hayne and Callinan JJ repeated that remark in *Clay v Clay* [2001] HCA 9, 202 CLR 410 at [46].

[42] The way in which the duties of a trustee are default duties is explained in a little more detail in J C Campbell, "Some Aspects of the Civil Liability Arising From Breach of Duty By a Superannuation Trustee" (2017) 44 Australian Bar Review 24 at 26-28

and the interest of the trustee, the principle is one that alters the duty of the trustee, so that a conflict no longer exists.

1.2.1 The Trust Instrument As An Exception to the "No Conflicts" Obligation

There are several recognised types of circumstance that could stop the duty to avoid a situation of conflict from applying in a particular case. One is that the terms of a particular trust deed can completely exclude the obligation of a trustee to avoid conflicts, or permit trustees to act despite a conflict of duty and interest[43]. The duty of a trustee is to carry out faithfully the office of being trustee of the *particular* trust of which it is trustee[44], and it is the trust deed that defines many of the parameters of what is involved in being trustee of that particular trust. As *Jacobs on Trusts* at [16-17] says:

> "It must never be forgotten that a third source of law [additional to the general law and statute] is the trust instrument. To a large extent a settlor or testator can amend, alter or modify any of the powers, duties and discretions which would otherwise apply; and can also determine what consequences flow from the breach of a duty. Just as the law of contract permits the parties to a contract to determine its terms, subject to any relevant legislation, the law of trusts permits the settlor or testator to determine the incidents of a trust, at least to a large extent"

Similarly, in *Cowan v Scargill*[45] Sir Robert Megarry V-C said:

> "I can see no reason for holding that different principles apply to pension fund trusts from those which apply to other trusts. Of course, there are many provisions in pension schemes which are not to be found in private trusts, and *to these the general law of trusts will be subordinated*. But subject to that, I think that the trusts of pension funds are subject to the same rules as other trusts."

It is also possible for a contract between trustee and beneficiary to remove the trustee's obligation to avoid conflicts, so far as a beneficiary who is party to the contract is concerned[46].

Even if the trust deed does not remove completely the obligation of the trustee not to be in a situation of conflict, the deed might remove it in part by allowing the trustee to carry out

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[43] *Hordern v Hordern* [1910] AC 465 (PC on appeal from NSW) at 475 (not strictly about a trustee, but about a person appointed executor of one partner acting under a clause in the partnership agreement entitling him, as surviving partner, to acquire the partnership business); *Chan v Zacharia* (1984) 154 CLR 178; *National Nominees Ltd v Agora Asset Management Proprietary Limited (No 2]* [2011] VSC 425 at [29]; *Bowering v Knox* [2014] NSWSC 1749 at [32],

[44] This is explained in more detail in JC Campbell, "Exercise by Superannuation Trustees of Discretionary Powers" (2009) 83 ALJ 159 at 159 – 160, (also printed in M Scott Donald and Lisa Butler Beatty (eds) *The Evolving role of Trust in Superannuation* (Federation Press Sydney 2017) p 212) , and in JC Campbell, "Should the 'Rule in Hastings-Bass' Be Followed in Australia? – Trustees' Duties to Enquire and Trustees' Mistakes" (2011) 34 Australian Bar Review 259 at pp 270-277. See also *SAS Trustee Corporation v Cox* [2011] NSWCA 408; 285 ALR 623 at [148], approved in *Segelov v Ernst & Young Services Pty Ltd* [2015] NSWCA 156; 89 NSWLR 431 at [53], [109], [139].

[45] [1985] Ch 270 at 290 (emphasis added), a passage approved by Waddell CJ in Eq in *Lock v Westpac Banking Corporation* (1991) 25 NSWLR 593 at 610

[46] *ASIC v Citigroup Global Markets Australia Pty Ltd (No 4)* (2007) 160 FCR 35; *Chan v Zacharia* at 196; *Woolworths v Kelly* (1991) 22 NSWLR 189 at 225

some particular type or types of act that would ordinarily involve a conflict[47]. There is no breach of trust involved when a trustee acts *bona fide* and for a proper purpose in a way that is permitted by the trust instrument.

Another possibility is that the trust deed leaves the obligation to avoid conflicts in place, but removes or limits the *liability* of the trustee for any breach of it, or for certain types of breach of it[48].

Whether a clause is framed as removing what would otherwise be the obligation of the trustee, or as excluding or limiting the trustee's liability for breach of it, is relevant to who bears the onus of proof. A plaintiff suing the trustee would bear the onus of proving that the plaintiff had breached its obligation, while the trustee would bear the onus of proving that it had the benefit of an exclusion clause[49].

Under the general law a clause that excludes what would otherwise be the liability of a trustee is construed strictly[50], but it is possible for *"clear and unambiguous words*"[51] in a trust deed to exclude the liability of a trustee for a negligent breach of trust[52]. It is doubtful that a clause that purported to remove liability for deliberate breaches of trust would be effective, because it would impinge on the irreducible core of a trustee's obligations.

There is a limit that the general law imposes on both to what extent the trust deed can free the trustee from obligations that the general law imposes, and on the extent to which the deed can whittle down the liability of a trustee for breach of an obligation. The limit arises from the concept that there is an irreducible core of obligations that a trustee must have, and

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[47] A very common example of such a clause is one allowing the trustee to charge fees: *Hull v Christian* LR (1874) LR 17 Eq 546; *In Re J Thorley* [1891] 2 Ch 613; *In Re Sykes* [1909] 2 Ch 241; *In Re Wells* [1962] 1 WLR 874; *Space Investments Ltd v Canadian Imperial Bank of Commerce Trust Co (Bahamas) Ltd* [1986] 1 WLR 102 at 1073-1075

[48] The distinction between a condition that limits or reduces the defendant's duty, those which exclude the defendant's liability for breach of a duty, and those that limit the extent to which the defendant is liable to indemnify the plaintiff in respect of the consequences of a breach of duty is recognised in *Kenyon, Sons & Craven Ltd v Baxter Hoare & Co Ltd* [1971] 2 All ER at 711, [1971] 1 WLR 519 at 522–3, approved in *Trade and Transport Inc v Iino Kaiun Kaisha Ltd* [1973] 2 All ER 144 at 162; [1973] 1 WLR 210 at 230 (Kerr J) and *Gardiner v Agricultural and Rural Finance Pty Ltd* [2007] NSWCA 235at [214] (Basten JA)

[49] *Gardiner v Agricultural and Rural Finance Pty Ltd* at [214] per Basten JA, approved by Edelman J in *Australian Securities and Investments Commission v Drake (No 2)* [2016] FCA 1552, 340 ALR 75 at [296]. The usual principle is that a person who seeks to avail himself or herself of some ground for exception or excuse in a statute bears the onus of proving the facts that bring his or her case within it: *Dowling v Bowie* (1952) 86 CLR 137 at 139-140; *Director of Public Prosecutions v United Telecasters Sydney Ltd* (1990) 168 CLR 594 at 611. The principle is not confined to matters of exception or qualification to obligations imposed by statute: *The King v Lee* (1950) 82 CLR 133 at 152-3.

[50] *McLean v Burns Philp Trustee Co Pty Ltd* (1985) 2 NSWLR 623 at 641C (Young J); *Midland Bank Trustee (Jersey) Ltd v Federated Pension Services Ltd* [1997] 2 LRC 81 at 102, 105, 109 (Jersey CA - a decision containing a thorough and useful collection of previous case law relating to clauses excluding liability of trustees); *Leerac Pty Limited v Fay* [2008] NSWSC 1082 at [13].

[51] *Armitage v Nurse* [1998] Ch 241 at 255

[52] *Jacobs on Trusts* [16-17], [16-19], [22-02]; *Leerac Pty Limited v Fay* [2008] NSWSC 1082 at [26]; *Spread Trustee Co Ltd v Hutcheson* [2011] UKPC 13, [2012] 2 AC 194 at [46], [52], [56], [57], [106]; *Segelov v Ernst & Young Services Pty Ltd* [2015] NSWCA 156, 89 NSWLR 431 at [144]-[146]; *Australian Securities and Investments Commission v Drake (No 2)* [2016] FCA 1552, 340 ALR 75 at [281] – [285]. There can be circumstances where equity could prevent a trustee from relying on an exclusion clause on the basis that it would be unconscientious to do so: *Wilkinson v Feldworth Financial Services Pty Ltd* (1998) 29 ACSR 642 at 745 – 6, *Jacobs on Trusts* [22-02].

of liability that a trustee must be under, without which the basis on which a person held property could not properly be called a trust[53]. However, the duties that make up the irreducible core are very few, basically that the trustee performs the trusts honestly and in good faith for the benefit of the beneficiaries, and that the identity of the trust property is known[54]. Thus, so far as the general law is concerned, there is a very wide scope indeed within which the trust deed can modify or exclude duties or liabilities of a trustee, including duties and liabilities relating to conflicts.

1.2.2 Consent of the Beneficiaries as an Exception to the "No Conflicts" obligation

Another way in which the avoidance of conflicts rule might not apply is that a fiduciary can act in what would otherwise be a situation of conflict between duty and interest or interest and interest if the beneficiary gives a fully informed consent[55]. There is a slightly different consent exception concerning a conflict between duty and duty. A person who owes a fiduciary duty to A is prohibited from entering into an engagement that would involve a fiduciary duty to B without the informed consent of both A and B[56]. However if the fiduciary is sued by one of A or B, and that plaintiff has consented to the fiduciary entering the double employment, that plaintiff will not be able to succeed in an allegation of breach of the no-conflicts duty whether or not the other beneficiary has consented to the fiduciary entering the double employment[57].

1.2.3 Conflict Created by the Settlor as an Exception to the "No Conflicts" Obligation

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[53] *Armitage v Nurse* [1998] Ch 241 at 253-4; *SAS Trustee Corporation v Cox* [2011] NSWCA 408, 285 ALR 623 at [148]; *Wilden Pty Ltd v Green* [2009] WASCA 38, 38 WAR 429 at [163]; *Segelov v Ernst & Young Services Pty Ltd* [2015] NSWCA 156; 89 NSWLR 431 at [145]; *Australian Securities and Investments Commission v Drake (No 2)* [2016] FCA 1552, 340 ALR 75 at [284]-[285] per Edelman J; *Jacobs on Trusts* at [16-20]; *Rinehart v Welker* [2012] NSWCA 95, 95 NSWLR 221 at [139-[140]; *Baker v J E Clark & Co (Transport) UK Ltd* [2006] EWCA Civ 464 esp at [21]; *Spread Trustee Co Ltd v Hutcheson* [2011] UKPC 13, [2012] 2 AC 194 at [46], [52], [56], [57] [106]. The legislation of the States and Territories can also impose duties on a trustee that are incapable of being excluded.

[54] Present authority is that the irreducible core does not include the trustee's duty of skill and care, prudence and diligence (*Armitage v Nurse* [1998] Ch 241 at 253 - 4; *Scaffidi v Montevento Holdings Pty Limited* [2011] WASCA 146 at [149] (the reversal of that decision in the High Court – *Montevento Holdings Pty Ltd v Scaffidi* [2012] HCA 48; 246 CLR 325 – turned solely on construction of a provision of the trust deed); *Rinehart v Welker* [2012] NSWCA 95, 95 NSWLR 221 at [139]; *Segelov v Ernst & Young Services Pty Ltd* [2015] NSWCA 156; 89 NSWLR 431 at [145]); Justice David Hayton, "Trusting the Trust", Preface to M Scott Donald and Lisa Butler Beatty (eds) *The Evolving role of Trust in Superannuation* (Federation Press Sydney 2017) p viii. Present authority also establishes that the irreducible core does not include a duty not to engage in any type of equitable fraud: *Wilden Pty Ltd v Green* [2009] WASCA 38, 38 WAR 429 at [163]. It is not universally accepted that the possibility of excluding duties goes as wide as this - *Jacobs on Trusts* at [17-18] contends that the trustee's duty of care *is* fiduciary, and doubts that liability for gross negligence can be excluded. It is likely that the duty to perform the trusts honestly and in good faith will give rise by implication to some more specifically formulated duties, eg to account to the beneficiaries (at least to some extent) for the trustee's stewardship of the trust property (*Re Simersall* (1992) 35 FCR 584 at 589) and to become acquainted with the terms of the trust.

[55] *Maguire v Makaronis* (1997) 188 CLR 449 at 466 ; *Farah Constructions Pty Ltd v Say-Dee Pty Ltd* [2007] HCA 22; (2007) 230 CLR 89 at [107] – [108]; *Commonwealth Bank of Australia v Smith* (1991) 42 FCR 390 at 393.

[56] *Fulwood v Hurley* [1928] 1KB 498 at 502; *Moiler v Forge* (1927) 27 SR (NSW) 69 at 71-2, 73; *Bristol and West Building Society v Mothew* [1998] Ch 1 at 18 - 19

[57] *Bristol and West Building Society v Mothew* [1998] Ch 1 at 18 - 19

If a trust deed appoints as trustee a person who will predictably have a conflict, that is an implied consent to the trustee acting notwithstanding that conflict[58]. This principle has particular relevance to superannuation funds in which the rules require there to be both member representatives or employer representatives - those representatives can exercise discretionary powers in ways that affect the group they represent, including themselves, without being in breach of the no-conflicts rule[59].

1.2.4 Court Permitting a Conflict as an Exception to the "No Conflicts" Obligation

There is an imprecisely defined inherent jurisdiction for a court with equity jurisdiction to permit a trustee to engage in what would otherwise be an impermissible conflict between a trustee's duty and interest. It has been exercised when a court permits a trustee to receive remuneration from the trust assets as recompense for work done in administering or preserving the assets[60], or permits a trustee to purchase trust property when the sale is advantageous to the beneficiaries, such as when no other purchaser can be found[61]. A similar jurisdiction is exercised when the court permits the liquidator of a corporate trustee to receive remuneration from the trust assets for work done in administering or preserving the trust assets[62]. It is not clear whether the court's inherent jurisdiction to authorise conflicts extends any wider than these examples.

Some transactions that a trustee proposes to enter, but would lack power to enter because of the no conflicts rule, might possibly be authorised by the court under its statutory jurisdiction to grant to trustees the power to enter advantageous dealings whenever the court is satisfied it is expedient to do so[63]. As Jacobs says, this statutory jurisdiction "is so much more extensive than the court's inherent jurisdiction as to render the latter virtually

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[58] eg if the person appointed as trustee of a discretionary trust is also one of the potential beneficiaries (*El Sayed v El Hawach* [2015] NSWCA 26, (2015) 88 NSWLR 214 at [16]), or if a person appointed as executor has a discretionary power the exercise of which might affect his personal interests (*Sargeant v National Westminster Bank Plc* (1990) 61 P & C R 518 at 523) . See also *Mordecai v Mordecai* (1988) 12 NSWLR 58 at 66; *Bowering v Knox* at [34] – [37] and cases there cited

[59] *Edge v Pensions Ombudsman* [1998] Ch 512 at 538 – 541 per Sir Richard Scott V-C, approved obiter by the Court of Appeal in *Edge v Pensions Ombudsman* [2000] Ch 603 at 622 despite the appellant having abandoned any argument that the decision of Scott V-C on this point was wrong.

[60] *Marshall v Holloway* (1820) 2 Swans 432 at 453, 32 ER 1128; *Morison v Morison* (1838) 4 My & Cr 215 at 224, 41 ER 85; *Forster v Ridley* (1864) 4 De G J & S 452 at 453, 46 ER 993; *Re Freeman's Settlement Trusts* (1887) 37 Ch D 141 at 152; *Re Masters* [1953] 1 WLR 81 at 83; *Re Jarvis* [1958] 1 WLR 815 at 820; *Re Cadd's Will Trusts* [1975] 1 WLR 1139 at 1140; *Re Duke of Norfolk's Settlement Trusts* [1982] Ch 61 at 75; *Foster v Spencer* [1996] 2 All ER 672. The inherent jurisdiction of the court to grant remuneration is recognised in Australia: *Richardson v Allen* (1870) 10 SCR (Eq) (NSW) 1 at 3; *Re Cox's Will* (1890) 11 NSWLR (Eq) 124; *Plomley v Shepherd* (1896) 17 NSWLR (Eq) 215; *Johnston v Johnston* (1903) 4 SR (NSW) 8; *Nissen v Grunden* (1912) 14 CLR 297. See generally *Jacobs on Trusts* at [17-39], M Conaglen, "The Extent of Fiduciary Accounting" (2011) 70 Cambridge Law Journal 548 at 565 - 573

[61] *Campbell v Walker* (1800) 5 Ves 678 at 681-2, 31 ER 801; *Brocksopp v Barnes* (1820) 7 Madd 90 at 90-91, 56 ER 829; *Farmer v Dean* (1863) 32 Beav 327, 55 ER 128; *Jacobs on Trusts* at [17-44]

[62] *Re Berkeley Applegate (Investment Consultants) Ltd* [1989] Ch 32 at 50 – 52; *Re Sutherland; French Caledonia Travel Service Pty Ltd (in liq)* [2003] NSWSC 1008, 59 NSWLR 361 at [194]-[217]

[63] Section 81 *Trustee Act 1925 (NSW)*. Analogous provisions are found in section 94 *Trusts Act 1973 (Qld)*, , section 59B *Trustee Act 1936 (SA)*, section 47 and 55 *Trustee Act 1898 (Tas*), section 63 . *Trustee Act 1958 (Vict)*, section 89 *Trustees Act 1962 (WA*), section 81 *Trustee Act 1925 (ACT)*, and section 50A *Trustee Act (NT)*. See generally *Jacobs on Trusts* [17-06] and, as to the limitations on the power, *Re Dion Investments Pty Ltd* [2014] NSWCA 367, 87 NSWLR 753; *Cisera v Cisera Holdings Pty Ltd* [2018] NSWCA 286, 98 NSWLR 747*)*.

obsolete."[64] Exercise of this jurisdiction can confer powers on a trustee transaction by transaction or type of power by type of power, but could not grant a trustee carte blanche freedom from the no conflicts rule.

1.2.5 Effect of Removal or Limiting of "No Conflicts" Obligation

In one or other of these various ways the general law might result in the trustee being freed from the obligation not to be in a position of conflict, either generally, or concerning some particular type or types of conflict. Thus, whether the trustee of a particular superannuation trust actually is subject, either in whole or part, to the general law default rule that a trustee must avoid being in a situation of conflict is very much a product of the terms of the particular trust deed, and of the circumstances in which the trustee came to be the trustee of that deed. As well, even if the trustee of a particular deed remains subject to all or part of the default rule against being in a situation of conflict, the remedies that are available against the trustee will depend on whether and if so to what extent the trust deed has freed the trustee from liability for breach of that obligation, or limited the trustee's liability.

1.2.6 *Jones v AMP Perpetual Trustee Co NZ Ltd*

One of the few cases to have considered the general law no-conflicts duty as it applied to a superannuation trustee entering significant transactions with a related company is *Jones v AMP Perpetual Trustee Company NZ Ltd*[65].

The defendant was the employer of the plaintiffs, and a wholly owned subsidiary of AMP. It was also the sole trustee of a superannuation scheme of which the plaintiffs were members. The scheme adopted what now appears to be an old-fashioned structure, whereby the trustee took out an insurance policy with AMP and paid premiums under that policy, in return for which AMP promised to fund the benefits payable under the trust deed. Most of the assets of the superannuation fund were used to pay the premiums. The premiums were used in part to pay for term life policies for each fund member, but the greater part was invested in a unitised fund, the A Unit, managed by AMP, in which various other superannuation funds also invested. The trustee had stipulated that that part of the premiums was to be invested in the A Unit. Most of the assets that comprised the A Unit were invested in equities. Their value declined sharply after a stock market crash in October 1987. The plaintiffs argued that the defendant was in breach of its fiduciary duty by investing in its parent company, and thus was liable to make good the loss that had been sustained in the stock market crash[66]. Their argument failed.

Even leaving aside any question of whether the facts of that case, if repeated today, would involve any breach of prudential standards or statutory covenants, I doubt that an Australian

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[64] *Jacobs on Trusts* [17-06]
[65] [1994] 1 NZLR 690
[66] The plaintiffs also made other allegations, namely that the insurance policy was not a permitted investment, that the taking out of the policy involved an improper delegation of discretion to AMP, that the investment of part of the premiums in the A Fund involved an improper intermingling of trust money with other money, and that in investing the fund moneys as it had done the defendant had breached its general law obligations of skill and care. All those allegations failed.

court today would come to the same conclusion concerning the application of the equitable no-conflict principle.[67]

In *Jones* there appears to have been no provision in the trust deed removing or lessening the no-conflicts duty, and there was no analogue of s 58B *SIS Act*[68], so the question at issue was a pure one of the requirements of the general law no-conflicts duty. The argument for breach of the fiduciary duty that the plaintiffs put was a very narrow one - the breach arose "in that [the defendant], or its parent company, AMP, profited personally from the investment"[69] because various fees were payable to AMP under the policy. In my view this focus on pecuniary benefits was too narrow. Officers of the defendant had given evidence that AMP had not pressured the defendant into dealing with AMP. Thomas J rejected that evidence, and accepted with equanimity that the role of the defendant within the AMP group put pressure on it to deal with its parent company:

> "I do not doubt that Perpetual's decisions were influenced by its corporate relationship with AMP. It would, I believe, have been unthinkable for it to have invested the superannuation fund with AMP's main competitor. Had that been the case, the inter-company upheaval, I suggest, would have been swift and decisive. It would be commercially naive not to recognise that, whether Perpetual accept the point or not, it was working within certain confines which were only slightly less real than if they had been spelt out in a head office directive."

His reasons for this influence not amounting to a breach of fiduciary duty was that AMP was a leading life insurance company with a comparatively attractive investment record, and Perpetual was not influenced in its decision by the thought that AMP would gain fees. Even if another insurer were chosen "equivalent fees" would be payable to it. Thus, Perpetual's

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[67] Justice Black is also of the view that "an Australian court would not necessarily reach the same result at general law" as was reached in *Jones*: Justice Ashley Black, "Trusts, Financial Services and Conflicts" 2015 Libby Slater Plenary Session paper 2015 *Superannuation Forever*, also accessible at http://www.supremecourt.justice.nsw.gov.au/Documents/Publications/Speeches/Pre-2015%20Speeches/Black/black_20150219.pdf page 25-26. *Jones* has never been referred to in an Australian decision. In New Zealand it has been mentioned in the Supreme Court of New Zealand in *Fenwick v Naera* [2016] 1 NZLR 354 at [75], but only in connection with rejecting an argument that the self-dealing rule applied only to purchases. *Fenwick* distinguished *Jones*, on the basis that "the case was not decided on the basis of an exception to the self-dealing rule but was instead decided on the basis that there was no sensible possibility of a conflict." *Jones* was mentioned in a first-instance decision in *Staite v Kusabs* [2017] NZHC 416 at [143] but solely in the course of giving an account of *Fenwick*. It has also been referred to in the Court of Appeal of England and Wales in *Fuji Finance Inc v Aetna Life Insurance Co Ltd* [1997] Ch 173 and in the New Zealand Maori Land Court in *Ratima v Sullivan* (2017) 64 Takitimu MB 121 at [9], but on each occasion on a point other than the present one. Thus the correctness of *Jones* on the application of the no-conflicts rule has not been judicially considered.

[68] Section 58B is considered at Section 4.2, "Is the general law no-conflicts rule ousted by section 52(2)(d)", below. There had been special legislation of the New Zealand Parliament, which provided that notwithstanding the fiduciary rights obligations and liabilities of the defendant, it was authorised to transact with AMP or any subsidiary of AMP any business whenever it was satisfied on reasonable grounds that it was in the best interests of the trust to do so, and even if AMP or a subsidiary of AMP were to receive fees from that business. That legislation came into effect on 1 April 1988, which would have been too late to save the defendant from any breach that was involved in sustaining losses in the stock market crash of October 1987. However, Thomas J, at 712 did not regard that legislation as changing his conclusion that there had been no breach of fiduciary duty.

[69] P 710

ability to serve the best interests of the beneficiaries was not impaired, and hence, his Honour concluded, no relevant conflict arose.

The type of loyalty to the corporate group that Thomas J recognised is an interest of a nonpecuniary kind that can fall within the no conflicts rule[70]. It would be a fairly clear breach of duty for a trustee to award a particular supply contract to a supplier who has promised a job to the trustee's daughter. That trustee would be in breach of his fiduciary duty even if the contract was otherwise on the best available market terms, so that the beneficiaries were not disadvantaged, and even if the daughter had not asked her father to try to find her a job. In a similar way, for the defendant to award the contract to its parent involved it acting in a situation where there was a realistic possibility of conflict between its interest in being a loyal member of the group and its duty to the beneficiaries. The contract was inherently of a type that would involve many complex terms, and evaluating that contract against the terms of alternative contracts available in the market, or that might be negotiated if negotiations with a supplier other than AMP were to be opened, was the type of task concerning which there was a realistic possibility that the defendant might come to be in a conflict between the interest of the beneficiaries and its role as a member of the AMP group. To paraphrase Lord Herschell[71], the point of the no-conflicts rule extending to situations of possible conflict is to enable it to operate as a way of preventing any temptation or unconscious tendency for the trustee to do anything other than act in the interests of the beneficiaries. Testing transactions after the event, to see whether the beneficiaries have in fact been disadvantaged, does not allow the rule its full scope of prophylactic operation. It is directly contrary to long-standing statements of high authority, starting at least from the time of Lord Eldon[72]. For example, in *Aberdeen Railway v Blaikie*[73] Lord Cranworth LC said, concerning a situation where a contract had been entered in breach of a company director's fiduciary duty:

> "so strictly is this [no-conflict] principle adhered to, that *no question is allowed to be raised* as to the fairness or unfairness of the contract so entered into … It may sometimes happen that the terms on which a trustee has dealt or attempted to deal with the estate or interest of those for which he is a trustee, have been as good as could have been obtained from any other person – they may even at the time have been better. But still so inflexible is the rule that *no enquiry on that subject is permitted*."

In Australia Isaacs J[74] Dixon J[75] and Gibbs J[76] have all approved the statement[77] that:

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[70] The *Final Report of the Royal Commission into Misconduct in the Banking Superannuation and Financial Services Industry* (Commonealth of Australia 2019), in section 2,2,2, page 229 - 232 gives details of practical situations in which outsourcing to a related company can give rise to conflict of interest.
[71] *Bray v Ford,* at footnote 19 above
[72] *ex parte James* (1803) 8 Ves 337 at 345 – 9, 32 ER 385 at 388 - 9
[73] (1854) Macq 461 at 471-2. Conaglen, *Fiduciary Loyalty* at page 65 footnote 32 cites sixteen other cases as further authority for the proposition.
[74] *Gray v Dalgety & Co Ltd* (1914) 19 CLR 81 at 374, where Isaacs J paraphrased the statement as that once the no-conflicts rule is broken "the Court will not listen to any suggestion that the principal has sustained no injury".
[75] *Birtchnell v Equity Trustees, Executors and Agency Co Ltd* (1929) 42 CLR 384 at 408–9
[76] *Consul Development Pty Ltd v DPC Estates Pty Ltd* (1975) 132 CLR 373 at 394
[77] Of James LJ in *Parker v McKenna* (1874) LR 10 Ch App 95 at 124-5

> 'the general principle that … no agent in the course of his agency, in the matter of his agency, can be allowed to make any profit without the knowledge and consent of his principal … is an inflexible rule, and must be applied inexorably by the Court, which is *not entitled … to receive evidence, or suggestion, or argument as to whether the principal did or did not suffer any injury in fact by reason of the dealing of the agent*; for the safety of mankind requires that no agent shall be able to put his principal to the danger of such an inquiry as that'

That passage has been held to apply not just to agents but generally to persons in a fiduciary position[78].

Thomas J concludes his discussion of fiduciary duty by saying:

> "… I do not consider Perpetual is in breach of its fiduciary duty to serve the best interests of the trust or the beneficiaries"

This is not what current Australian law understands a fiduciary duty to be[79].

PART 2 – RELATION OF THE SIS ACT TO THE GENERAL LAW

The accepted rationale for the no-conflicts duty in the general law is that it is a way of giving effect to the fundamental concept of who a fiduciary is. A fiduciary is a person who performs some particular task that aims to provide a benefit to someone else, when the fiduciary must have undivided loyalty to that someone else concerning the performance of that task[80]. The general law did not allow the fiduciary to be in a situation of either actual or realistically possible conflict because of the risk that in the conflict situation the fiduciary might not give undivided loyalty to the interests of the beneficiary. Undivided loyalty was a means of

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[78] *Consul Development Pty Ltd v DPC Estates Pty Ltd* (1975) 132 CLR 373 at 394 per Gibbs J

[79] Compare that statement with the Two Duties Quotation at footnote 6 above. For completeness I should mention that David Hayton, Paul Matthews and Charles Mitchell (eds) *Underhill and Hayton Law of Trusts and Trustees* (19th ed 2016 LexisNexis) at [27.69] give an account of *Jones* which appears to accept the judge's conclusion that there was no real sensible possibility of conflict, but the discussion is very brief.

[80] *Bristol and West Building Society v Mothew* [1998] Ch 1 at 19, cited with approval in *Maguire v Makaronis* (1987) 188 CLR 449 at 473 and in *Bofinger v Kingsway Group* [2009] HCA 44; (2009) 239 CLR 269 at [49]._Other places where the High Court has given passing recognition to "*undivided loyalty*" as a requirement of fiduciary duties, without disapproval but not as part of the ratio of the case, are in *Breen v Williams* (1996) 186 CLR 71 at 108 (Gaudron & McHugh JJ) and in *Pilmer v The Duke Group Ltd (in liq)* [2001] HCA 31; (2001) 207 CLR 165 at [76] (plurality, but as part of recounting the reasoning of the court below), [142] & [149] (Kirby J dissenting). Approval has been given to "*loyalty*" as an indicium of a fiduciary relationship in *Breen v Williams* at 93, 95 (Dawson & Toohey JJ). Gummow J at 125 expressed it conversely, saying "*in fiduciary law "informed consent" is an answer to circumstances which otherwise indicate disloyalty*", while at 134 he quoted with apparent approval a statement by La Forest J in *Hodgkinson v Simms* [1994] 3 SCR 377 at 406; (1994) 117 DLR (4th) 161 that " *whereas undue influence focuses on the sufficiency of consent and unconscionability looks at the reasonableness of a given transaction, the fiduciary principle monitors the abuse of a loyalty reposed…*" *MGL* at [5-005] say "the distinguishing characteristic of a fiduciary relationship, then, is that its essence, or purpose, is to serve exclusively the interests of a person or group of persons to put the matter negatively, it is a relationship in which the parties are not free to pursue their separate interests. Thus, the essence of a trust is that a trustee holds and deals with the property in the interest of beneficiaries."

protecting and promoting the interests of the beneficiaries. As Gaudon and McHugh JJ said in *Breen v Williams*, "fiduciary obligations arise *because* a person has come under an obligation to act in another's interests."

What has happened in the modern law governing superannuation is that the same objective that the general law sought to achieve by the no conflicts rule, of protecting and promoting the interests of the beneficiaries, is now sought by the *SIS Act* and delegated legislation made under it prescribing standards of conduct for a trustee. Some of these standards now say expressly that they apply in a situation of conflict. Others are expressed in more general terms, but are capable of applying in a situation of either actual or potential conflict. Several of these standards incorporate expressly an obligation for the trustee to act in the best interests of the beneficiaries.

But the *SIS Act*'s standards of conduct continue to operate, except where there is an inconsistency, alongside requirements of the general law concerning trusts, and the State and Territory statutory law governing trusts. This arises from the interaction of two widely separated sections of the *SIS Act*, section 7 and section 350, both of which have stood unchanged since the Act was first enacted. Section 7 provides:

> This Act applies to a superannuation entity despite any provision in the governing rules of the entity, including any provision that purports to substitute, or has the effect of substituting, the provisions of the law of a State or Territory or of a foreign country for all or any of the provisions of this Act

That section has the effect of doing away with the possibility that the trust deed creating a superannuation fund might exclude or limit those obligations of the trustee that were required by any of the express provisions of the *SIS Act*.

When the *SIS Act* was first enacted the definition of "governing rules" was an exhaustive one – it was:

> **"governing rules",** in relation to a fund, scheme or trust, means any trust instrument, other document or legislation, or combination of them, governing the establishment and operation of the fund, scheme or trust;

The inclusion of the words "other document" in the definition of "governing rules" had the effect that a written contract was ineffective to exclude or limit the obligations of the trustee required by the statutory covenants[81]. The words "or legislation" in the definition of governing rules had the effect that state or territory legislation could also not exclude or limit the obligations of the trustee required by the express provisions of the *SIS Act*.

Section 350 has always provided:

> It is the intention of the Parliament that this Act is not to apply to the exclusion of a law of a State or Territory to the extent that that law is capable of operating concurrently with this Act.

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[81] There was a theoretical possibility that an oral contract or an estoppel might exclude a trustee's liability concerning covenants in section 52, but the practical likelihood of there being such a contract or estoppel seems minimal. In any event there might be an argument that such a contract or estoppel contravened the policy of the statute

The express statement of legislative intention in section 350 is in keeping with what the general law principles of statutory interpretation would otherwise require. There is repeated High Court authority that when a statute operates in a field where the *common law* had previously operated it is presumed that the statute alters the common law only to the extent that its wording does so expressly, or alteration of the pre-existing law is a necessary implication of its wording[82]. Thus "where two alternative constructions of legislation are open, that which is consonant with the common law is to be preferred"[83].

Importantly for present purposes, this presumption has been held to be applicable to *principles of equity* as well as to principles of the common law[84]. Indeed, it is hard to think of any plausible argument why the presumption might apply to one part of the judge-made law, but not to another part of the judge-made law.

I recognise that of recent years there has been a tendency for principles of statutory construction to be stated without reference to presumptions[85]. Notwithstanding that, the High Court continues to recognise that there is a difference

> "between Commonwealth laws that operate within the framework of the general law and Commonwealth laws which operate to lay down a rule or rules in terms which convey that the rule or rules so stated, *and no other rules*, are to govern in a given case"[86].

Concerning a Commonwealth statute that operates within the framework of the general law, the general law continues to operate in so far as it is not inconsistent with the statute[87].

Both the SIS Act when first enacted, and some amendments to the *SIS Act* considered below that came into operation on 1 July 2013 came into existence in a field in which the general law, supplemented but not completely replaced by statute, had previously operated. Thus, unless there is either an express provision or a necessary implication in the *SIS Act* that a provision of the general law concerning trustees will not apply to superannuation funds, that provision of the general law will continue to apply.

A "law of a State or Territory" relating to trusts, continued in operation by s 350 except where that law cannot operate alongside the *SIS Act*, includes its statutory law governing trusts. The State and Territory statutory law governing trusts has some significant variations from

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[82] *Potter v Minahan* (1908) 7 CLR 277 at 304; *Bropho v Western Australia* [1990] HCA 24; (1990) 171 CLR 1 at 18; *Coco v R* [1994] HCA 15; (1994) 179 CLR 427 at 437. See generally D Pearce, *Statutory Interpretation in Australia* (9th ed LexisNexis Australia 2019) at [5.34]-[5.36].
[83] *Balog v Independent Commission against Corruption* [1990] HCA 28; (1990) 169 CLR 625 at 635-6
[84] *Minister for Lands and Forests v MacPherson* (1991) 22 NSWLR 687; *Registrar of Titles v Mrsa* [2015] WASCA 204 at [32] per Martin CJ (Newnes and Murphy JJA agreeing); *Binetter v BCI Finances Pty Ltd (in liq)* [2015] FCAFC 122, 235 FCR 410 at [32]-[34] per Besanko, McKerracher and Pagone JJ. In *Commonwealth Bank of Australia v Butterell* (1994) 35 NSWLR 64 at 70-71 Young J implicitly applied that principle when he held that general provisions in the *Corporations Act* about order of priority of payments in a winding up did not exclude entitlements to an equitable lien. See generally. Mark Leeming "Equity: Ageless in the Age of Statutes" (2015) 9 Journal of Equity 108 at 125 - 6.
[85] Eg *R v A2* [2019] HCA 35, 373 ALR 214 at [32]-[37] per Kiefel CJ and Keane J (Nettle and Gordon JJ at [148] agreeing generally), [124]-[125] per Bell and Gageler JJ, [163]-[165] per Edelman J; *State of Victoria v Thompson* [2019] VSCA 237 at [40]
[86] *Williams v Wreck Bay Aboriginal Community Council* [2019] HCA 4, 363 ALR 631 at [69] per Kiefel CJ, Keane, Nettle and Gordon JJ (emphasis in original)
[87] *Ibid* at [71]-[72]

one jurisdiction to another. Thus, for any particular superannuation trust, it will be necessary to identify what is the proper law of the trust[88], to ascertain which is the State or Territory whose statutory law continues to apply to that particular trust.

PART 3 – EFFECT OF INITIAL INTRODUCTION OF THE SIS ACT ON CONFLICTS

3.1 Scope of Application of the *SIS Act*

When the *SIS Act* first came into effect it applied only to things that were within its definition of "superannuation entity". That term was defined in a way designed to cover entities the regulation of which fell under the Commonwealth's corporations power, or pensions power, or taxation power. However, in practice practically all superannuation funds fell within the scope of the Act[89].

3.2 Initial Version of the Statutory Covenants in section 52 SIS Act

Section 52 required the governing rules of a superannuation entity to be taken to contain certain covenants by the trustee[90]. The covenants that were required by the original version of s 52 were ones that, to a very large extent but not entirely, reproduced default rules of equity concerning the obligations of a trustee[91]. The NSW Court of Appeal decided in 2011, after examining the wording of the then section 52 and the history of its introduction, that its

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[88] Principles for ascertaining the proper law of a trust are summarised in M Davies, AS Bell, PLG Brereton and M Douglas, *Nygh's Conflict of Laws in Australia* (10th ed, LexisNexis Australia 2020) at [34.16]-[34.27]

[89] See the definitions of "superannuation fund" in section 10, "regulated superannuation fund" in section 19 *SIS Act* 1993 as originally enacted.

[90] In addition, the original section 52 (8) contained some highly compressed drafting which deemed there to be certain covenants by the director of a corporate trustee. The directors' covenants were expanded and made more explicit when the original section 52 (8) was repealed and a new section 52A became effective in the *SIS Act* from 1 July 2013. The operation of the director's covenants is outside the scope of this paper.

[91] The covenants that section 52 required included:

> (f) to formulate and give effect to an investment strategy that has regard the whole of the circumstances of the entity including, but not limited to, the following:
>
> (i) the risk involved in making, holding and realising, and the likely return from, the entity's investments having regard to its objectives and its expected cash flow requirements;
>
> (ii) the composition of the entity's investments as a whole including the extent to which the investments are diverse or involve the entity in being exposed to risks from inadequate diversification;
>
> (iii) the liquidity of the entity's investments having regard to its expected cash flow requirements;
>
> (iv) the ability of the entity to discharge its existing and prospective liabilities;
>
> (g) if there are any reserves of the entity-to formulate and to give effect to a strategy for their prudential management, consistent with the entity's investment strategy and its capacity to discharge its liabilities (whether actual or contingent) as and when they fall due;
>
> (h) to allow a beneficiary access to any prescribed information or any prescribed documents.

The covenants required by clauses (f) and (g) were more specific than the default rules of equity, but in their application to a superannuation fund might well be nothing more than stating what was required by one aspect of the duty of care and skill. The covenant in clause (h) had the capacity to require more information or documents than the general law would require, depending on what the regulations prescribed.

purpose was to require a minimum set of duties that could not be derogated from by the deed or other constituting document of the trust, but not to impose obligations that were different to or more onerous than the general law obligations on a trustee[92]. In other words, the statutory covenants were imposed to remove some of the freedom that the general law allowed to the drafter of a trust deed to modify or exclude almost completely the general law default duties of a trustee.

The covenants contained in the original section 52 said nothing about a trustee's obligations concerning conflicts. Thus, consistently with section 350 of the *SIS Act*, and not detracted from by section 7 of the *SIS Act*, the general law position concerning conflicts remained. Hence it was possible for the trust deed to exclude or limit almost completely the trustee's default obligation not to be in a position of conflict. However, to the extent that the trust deed did not exclude or limit that obligation, the trustee remained subject to it. Further, if the trustee acted in breach of its obligation not to be in a situation of conflict then, to the extent that the trust instrument did not limit the remedies available for breach of a trustee's obligation, the trustee could be subject to whichever was appropriate of the equitable remedies – principally account of profits or other benefits[93], equitable compensation and injunction.

Section 55 of the *SIS Act* introduced a statutory remedy of damages, available to anyone who suffered loss or damage as a result of conduct in contravention of a covenant in, or taken to be in, the governing rules of a superannuation entity[94]. Because of section 7[95], this right to damages could not be excluded or limited by the trust instrument in the way that the deed could exclude or limit a right to equitable compensation. However, if a trustee had acted honestly, and in all the circumstances ought fairly be excused, there was a power for the court to relieve the trustee from liability, in whole or part, on such terms as the court thinks fit[96].

Consistently with the covenants in section 52 reproducing obligations of the general law, the remedy in section 55 was an extra remedy for breach of those obligations. However it did not supplant the general law remedies, in particular account of profits or, if ever its quantification might be different to that of damages under section 55, equitable compensation.

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[92] *Manglicmot v Commonwealth Bank Officers Superannuation Corporation Pty Ltd* [2011] NSWCA 204; 262 ALR 167 at [110]-[114], [118]. By contrast, in *VBN and Australian Prudential Regulation Authority* [2006] AATA 710; (2006) 92 ALD 259 at [306]-[330], a decision to which the court that decided *Manglicmot* was not referred, the AAT had concluded that the statutory covenants imposed obligations that were different in some respects to the general law obligations. The rewriting of the covenants effective from 1 July 2013 makes it unnecessary to resolve this difference of opinion, except concerning any breaches of trust alleged to have occurred before 1 July 2013.

[93] *Ancient Order of Foresters in Victoria Friendly Society Ltd v Lifeplan Australia Friendly Society Limited* [2018] HCA 43; 360 ALR 1 holds that a defaulting fiduciary can be required to account for the value of all benefits received, even if they do not take the form of profits that have been actually realised at the date of judgment.

[94] The operation of section 55 is considered in more detail in JC Campbell, "Some aspects of the civil liability arising from breach of duty by a superannuation trustee" (2017) 44 Australian Bar Review 24 at 65-75

[95] Set out in Part 2, "Relation of the *SIS Act* to the general law", above

[96] Section 310. The identity of the "court" that could exercise this power was clarified by the definition of "court" (with a lower case "c") in s 10. It was any court exercising jurisdiction under the *SIS Act*. Thus if, for example an action for damages under section 55 was brought against a trustee in the District Court, the District Court judge could exercise the excusing power under section 310.

3.3 1999 Change in Definition of "Governing Rules"

The *Superannuation Legislation (Amendment) Act 1999*[97] amended the definition of "governing rules", so that it became:

> ***governing rules***, in relation to a fund, scheme or trust, means:
>
> (a) any rules contained in a trust instrument, other document or legislation, or combination of them; or
>
> (b) any unwritten rules;
>
> governing the establishment or operation of the fund, scheme or trust.

Reading section 7[98] together with this definition of "governing rules" it appears that the Act is to apply despite any provision in, inter alia, the general law governing the trust. That result is unchanged from the previous position, that in the event of inconsistency the Act is to apply, but otherwise the general law can continue to apply.

Including any unwritten rules in the definition of "governing rules" had the effect of making those provisions of the general law that governed a superannuation fund part of its "governing rules"[99]. Thus, to the extent that the requirement not to be in a position of conflict had not been excluded by the trust instrument, it continued to apply to the fund by virtue of the general law, and so it became part of the "governing rules" within the statutory definition. This reinforced the situation that had previously applied by virtue of section 350, that if any

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[97] No 38 of 1999, Schedule 2 cl 46. The first compilation of the *SIS Act* in which the amendment appeared as current law was that of 15 December 1999.

[98] Set out in Part 2, "Relation of the *SIS Act* to the general law", above

[99] I am indebted to Nuncio D'Angelo for pointing out that it is not the general understanding of either the industry or APRA that those provisions of the general law that govern a superannuation fund are part of its governing rules. Rather, he informs me that the general view is that "unwritten rules" are ones that emerge or are established through a course of conduct or practice, or result from the trustee exercising discretionary powers to make rules, in each case that are not otherwise stated in the trust instrument. And that the mention of "legislation" in para (a) of the definition is understood to mean State, Territory and Commonwealth legislation for public sector superannuation funds, and the *SIS Act* itself, rather than the State or Territory trusts legislation. Accepting that these views are held, the *SIS Act* definition of "governing rules" still means what it says, judge-made rules are archetypal "unwritten rules", the ordinary meaning of "legislation" includes any State or Territory legislation, and the view of the industry and APRA is, in my opinion, at odds with the meaning of the words in the definition. When Australia has no *Chevron* doctrine, whereby a court will defer to the reasonably held view of a federal agency concerning the proper construction of a statute administered by it (*Corporation of the City of Enfield v Development Assessment Corporation* (2000) 199 CLR 135; *Minister for Immigration and Citizenship v Yucesan* [2008] FCAFC 110, 169 FCR 202 at [13]-[15]) any sharing by APRA of the industry view will not give it any extra acceptability to a court. I accept that there is a difficulty in incorporating the literal meaning of the new definition of "governing rules" into s 58B (2), but that difficulty is not sufficient reason to alter the ordinary English meaning of the definition because (a) the application of the definition to s 58B(2) would be subject to the requirement stated at the beginning of section 10 *SIS Act*, that its definitions apply "unless the contrary intention appears". Such a formula authorises a defined meaning of a term in a statute not to be applied in some particular provision of the statute if, inter alia, it does not make sense when applied in that provision: *Cvetkovic v R* [2010] NSWCCA 329 at [272] and cases there cited, and (b) the definition was altered to include unwritten rules in 1999, and section 58B was added only in 2013. The addition of a new substantive provision in 2013 cannot change the meaning of a 1999 definition.

provision of the *SIS Act* was inconsistent with the no-conflicts rule, it was the *SIS Act* that would prevail.

However, at that time there was nothing in the *SIS Act* that even arguably was inconsistent with the no-conflicts rule. Indeed, before 1 July 2013 one of the covenants that were required to be treated as being in the governing rules of a superannuation entity was the one required by s 52 (2) (e). It was a covenant "not to enter into any contract, or do anything else, that would prevent the trustee from, or hinder the trustee in, properly performing or exercising the trustee's functions and powers". If the trust deed had not excluded or limited the trustee's obligations concerning conflicts, that covenant would have impliedly prohibited any contract by the trustee that weakened the general law obligation not to be in a situation of conflict.

Including the general law rules in the "governing rules" did not, however, confer any additional remedy. The remedy in s 55 was for contravention of a covenant. A "covenant" is a particular type of legal obligation of a type that usually arises by agreement[100]. The no-conflicts rule would not be classified as a covenant, so no action under section 55 could lie for breach of it.

PART 4 – THE AMENDMENTS EFFECTIVE FROM 1 JULY 2013

The most significant change, so far as the application of the general law concerning conflicts to regulated superannuation funds was concerned, came from two pieces of legislation. One was passed in 2012[101], the other was passed in 2013[102]. Notwithstanding the different dates of enactment, both of them became operative so far as presently relevant from 1 July 2013.

4.1 The New Covenants in Section 52

The 2012 Act completely replaced the pre-existing section 52 with a new set of covenants that were to be taken to be included in the governing rules. It narrowed the scope of application of the covenants arising under the replacement section 52 of the Act, so that they applied only to a "registrable superannuation entity" ("RSE"). That term was defined[103] so

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[100] David M Walker, *The Oxford Companion to Law* (Clarendon Press Oxford 1980) p 311 refers to the mediaeval personal action of covenant, and continues "The word is also applied to a promise or agreement under seal, and to a particular undertaking contained in the deed, or implied by law in a deed of a particular kind, as in, e.g. 'covenants running with the lands' or 'covenants in restraint of trade'. P G Osborne, *A Concise Law Dictionary* (5th ed Sweet & Maxwell 1964) p 96 defines it as "An agreement creating an obligation contained in a deed."

[101] *Superannuation Legislation Amendment (Trustee Obligations and Prudential Standards) Act 2012*, No 117 of 2012

[102] *Superannuation Legislation Amendment (Service Providers and Other Governance Measures) Act 2013*, No 61 of 2013. Section 58B was introduced by item 72 of Schedule 1 of that Act, which section 2 provided was to commence on 1 July 2013. Section 58B was not retrospective in effect. Item 130 of the Act said: "The amendment made by item 72 of this Schedule, to the extent that it relates to proposed section 58B, applies in relation to things done on or after 1 July 2013."

[103] Sectiion 10

that it did not include a self-managed superannuation fund[104], but was likely to include most others.

For the first time, the covenants set out in the new section 52 (2) included some that gave a trustee obligations expressly related to conflicts[105]. They were:

> (d) where there is a conflict between the duties of the trustee to the beneficiaries, or the interests of the beneficiaries, and the duties of the trustee to any other person or the interests of the trustee or an associate of the trustee:
>
> (i) to give priority to the duties to and interests of the beneficiaries over the duties to and interests of other persons; and
>
> (ii) to ensure that the duties to the beneficiaries are met despite the conflict; and
>
> (iii) to ensure that the interests of the beneficiaries are not adversely affected by the conflict; and
>
> (iv) to comply with the prudential standards in relation to conflicts;

4.2 Is the General Law No-conflicts Rule Ousted by Section 52 (2) (d)?

These new covenants specifically contemplate that the trustee is in a situation of conflict, and state what the trustee must do when it is in a situation of conflict. That raises a question of whether the new statutory covenants are inconsistent with there still being any general law duty for the trustee of a regulated superannuation fund to avoid conflicts. If there were an inconsistency between the new covenants and the equitable duty to avoid conflicts, the equitable duty would by implication be ousted in so far as it had applied to the trustees of regulated superannuation funds.

Another change that came into effect on 1 July 2013 is relevant to whether there is an implied repeal of the general law no-conflicts duty. The 2013 Act added a new section 58B, which states:

> (1) This section applies if a trustee, or the trustees, of a regulated superannuation fund does one or more of the following:
>
> (a) acquires a service from an entity;
>
> (b) invests assets of the fund in or through an entity;
>
> (c) invests assets of the fund in or through a financial product;
>
> (d) purchases a financial product using assets of the fund;

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[104] A new section 52B required a different, somewhat less onerous set of covenants from the trustees of a self- managed superannuation fund. As well section 29 VN was added, containing some extra obligations that apply to the trustee of a regulated superannuation fund that offered a MySuper product. The covenants required from a director of a corporate trustee were also altered, by the inclusion of a new section 52A. Analysis of all of these changes is outside the scope of this paper.

[105] From its first enactment the *SIS Act* had included a covenant in section 52(2) (c) requiring the trustee "to ensure that the trustee's duties and powers are performed in the best interests of the beneficiaries" Though such a covenant advances a part of the purpose why the general law has a no-conflicts rule (see the Two Duties Quotation, text at footnote 6 above), it allows outcomes to be assessed ex post facto, and is not breached if some particular action cannot be shown to have caused the beneficiaries any harm. It does not perform the same prophylactic function as the general law no-conflicts rule.

(e) uses assets of the fund to make payments in relation to a financial product.

(2) If the trustee, or the trustees, would not breach:

(a) a provision of any of the following:

(i) this or any other Act;

(ii) a legislative instrument made under this or any other Act;

(iii) the prudential standards;

(iv) the operating standards;

(v) the governing rules of the fund; or

(b) any covenant referred to in this Part or prescribed under this Part;

in doing one or more of the things mentioned in subsection (1), the general law relating to conflict of interest does not apply to the extent that it would prohibit the trustee, or the trustees, from doing the thing.

In my view it is still possible for the equitable obligation to avoid conflicts to apply to the trustee of a regulated superannuation fund in some but not all situations.

4.2.1 Implications of Section 58B for Application of the No-conflicts Rule

The new section 58B is an express provision that sometimes prevents the equitable no-conflicts duty from applying to a regulated superannuation fund. But it does not completely prevent the no-conflicts rule from applying to such a fund.

First, s 58B prevents the operation of the no-conflicts rule only concerning certain types of transactions, namely those listed in s 58B (1). The most that section 58B could do is to make the no-conflicts rule inapplicable to a fund transaction by transaction, not in any blanket or overall fashion.

Second, it well may be that many of the transactions that a trustee engages in fall under one or other of the paragraphs of s 58B(1), but not all of them will[106]. Concerning those transactions that do not fall within s 58B(1) the no conflicts rule would continue to apply, unless concerning the particular fund, and the particular decision, there was one of the circumstances that equity recognises as causing the no conflicts rule not to apply.

Third, even if a decision is one concerning which s 58B (1) applies, 58B (2) makes the no conflicts rule inapplicable only if every one of the conditions listed in s 58B (2) (a) and (b) applies[107]. Thus, for example, if the decision is one concerning which s 58B(1) applies, but the trustee has failed to comply with the prudential standards concerning it, s 58B does not prevent the application of the no- conflicts rule. If the decision is one concerning which s

[106] The definition of "entity" in section 10 *SIS Act* is very broad – it is any of an individual, a body corporate, a partnership or a trust. However, the definition of "financial product" in section 10 *SIS Act* adopts a definition from chapter 7 of the *Corporations Act*, which would not cover the full range of subject matters of a transaction that a trustee might enter. For example, a purchase of land or goods would not fall within s 58B(1).

[107] There is a question about who bears the onus of proving the applicability of the conditions in section 58B(2). See the principle and cases at footnote 49 above.

58B(1) applies, but the trustee has breached one of the statutory covenants concerning it, s 58B does not prevent the no conflicts rule from applying.

The very fact that section 58B prevents the no-conflicts rule from applying only in some particular situations is in itself a recognition of the possibility of the no-conflicts rule applying in other situations.

4.2.2 Application of Primary Obligation/Secondary Obligation Analysis

The new covenants in s 52 concerning conflicts say what the trustee must do *if it is in* a situation of conflict. Thus, they presuppose that the trustee is already in the situation of conflict. However, that does not lead to any necessary implication that the equitable duty to avoid conflicts cannot apply. The law recognises numerous situations in which one legal provision creates an obligation to act in a certain way, but there is another legal provision that says that if the first, or primary obligation, is breached, there is then an obligation to act in some different way. This sort of secondary obligation arises only if the primary obligation is breached.

One example of this type of structure of obligations is that there can be a primary contractual obligation to act in a particular way, but if the primary obligation is breached the general law imposes a secondary obligation to pay the amount of damages caused by the breach[108]. A particular application of that is that if there is a primary contractual obligation to act in a particular way, but the primary obligation is breached, a valid liquidated damages clause imposes a secondary obligation to act in some different way – namely to pay the amount of the liquidated damages[109]. If a debt has been guaranteed the liability of the guarantor is a secondary liability, enforceable only when and if the principal debtor fails to pay on time[110]. If a debt has been guaranteed at the request of the debtor, the debtor breaches his obligation to pay the debt on time, and the guarantor is required to pay, that gives rise to a secondary obligation on the debtor to indemnify the guarantor[111].

This familiar pattern of primary and secondary legal obligations is readily capable of being applied to the equitable no-conflicts duty, and the specific obligations concerning conflicts in the new s 52. Concerning those funds whose rules have not negatived the no-conflicts rule,

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[108] *Photo Production v Securicor* [1980] AC 827 at 848-50; *Lep Air Services v. Rolloswin Ltd*. (1973) AC 331 at 350, quoted with approval by Brennan J in *Progressive Mailing House Pty Ltd v Tabali Pty Ltd* (1985) 157 CLR 17 at 48 and by Foster AJA (Sheller and Santow JJA agreeing) in *Narui Gold Coast Pty Ltd v Charles Harrison Pty Limited* [2003] NSWCA 238 at [31]:*Mann v Paterson Construction Pty Ltd* [2019] HCA 32 at [12], [38] per Kiefel CJ, Bell and Keane JJ, [83] per Gageler J, [197] per Nettle, Gordon and Edelman JJ. See also *Pacific Brands Sport & Leisure Pty Ltd v Underworks Pty Ltd* [2005] FCA 288 at [9] (Finkelstein J); *Tszyu v Fightvision Pty Ltd* [2001] NSWCA 103, (2001) 104 IR 225 at [59] (Powell JA); and *Kennedy Taylor (Vic) Pty Ltd v Baulderstone Hornibrook Pty Ltd* [2000] VSC 43 at [24] (Beach J). The secondary obligation continues to exist even if the primary obligations of the contract are ended because the contract is terminated for breach of the primary obligation: *Hyundai Heavy Industries Co Ltd v Papadopoulos* [1980] 1 WLR 1129 per Lord Edmund-Davies

[109] *Cavendish Square Holding BV v El Makdessi; ParkingEye Ltd v Beavis;* [2015] UKSC 67, [2016] AC 1172 at [7], [9], [13], [14], [32], [84],[241], [242],[251], [280], [291]; *Holyoake v Candy* [2017] EWHC 3397 (Ch) at [467]

[110] *Turner Manufacturing Co Pty Ltd v Senes* [1964] NSWR 692 at 694; *Sunbird Plaza Pty Ltd v Maloney* [1988] HCA 11, 166 CLR 245 at [4], *Bofinger v Kingsway Group Limited* [2009] HCA 44 at [7]; *Grave v Blazevic Holdings* [2010] NSWCA 324 at [26]; *Karacominakis v Big Country Developments Pty Ltd* [2000] NSWCA 313 at [242]

[111] *Israel v Foreshore Properties Pty ltd (in liq*) (1980) 30 ALR 631

or there is not some other recognised basis in equitable principle for the rule to not apply, the no-conflicts rule will apply as a primary obligation, with the statutory covenants concerning conflicts operating as secondary obligations if the trustee comes to breach the no-conflicts rule.

4.2.3 Assistance from the Explanatory Memorandum

When a provision in Commonwealth legislation is being interpreted it is permissible to give consideration to an explanatory memorandum[112] relating to a Bill containing the provision either:

> (a) to confirm that the meaning of the provision is the ordinary meaning conveyed by the text of the provision taking into account its context in the Act and the purpose or object underlying the Act; or
> (b) to determine the meaning of the provision when:
> (i) the provision is ambiguous or obscure …

The Explanatory Memorandum for the legislation that introduced the new section 52(2)(d)[113] supports the general law no-conflicts rule still sometimes applying to a regulated superannuation entity. Paragraph 1.51 of that Memorandum specifically contemplated continued operation of the no conflicts rule. It said

> "The general law requires trustees to avoid conflicts of duties and interest, subject to certain exceptions that allow the trustee to act despite the conflict, for example by authorisation under the fund's governing rules. Where a conflict exists, and the general law allows the trustee to proceed despite the conflict, there will be a number of additional requirements that must be met."

The Memorandum then went on to paraphrase the new s 52(2) (d). It also contemplated possible continuing operation of the general law concerning conflicts when paragraph 1.57 of the Memorandum said:

> "The new provisions are not intended to limit transactions with related parties where the transactions are in the best interest of beneficiaries *and permitted under the general law*."

These parts of the Memorandum confirm the ordinary meaning of section 52(2) (d), given that it does not expressly abolish the no-conflicts rule in its application to superannuation funds, and particularly when one takes into account the context provided by section 350 *SIS Act*. Thus resort to them for the purpose of interpretation is permitted. Alternatively, if one takes the view that there is ambiguity or obscurity about whether s 52(2) (d) does away with the no-conflicts rule, resort to these parts of the Memorandum is likewise permitted.

4.2.4 Consequences of Possibility of General Law No-conflicts Rule Applying

One consequence of it being sometimes possible that the general law no-conflicts rule might apply to a regulated superannuation fund is that it is not possible to say categorically that the law concerning conflicts that govern such a fund is proscriptive, or prescriptive. The

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[112] Section 15AB (2) (e) *Acts Interpretation Act 1901 (Cth)*
[113] Explanatory Memorandum for the *Superannuation Legislation Amendment (Trustee Obligations and Prudential Standards) Bill 2012*

statutory covenants impose prescriptive obligations, but if the general law no-conflicts duty applies to a particular fund there will be a proscriptive duty as well.

Another consequence concerns remedies. In those situations where the equitable no-conflicts rule applies to a superannuation trustee one effect will be that a wider range of remedies is available than would be available under the *SIS Act* for breach of its deemed covenants. An account of the profits made by trustee by reason of a breach of the no-conflicts duty may well yield a larger sum of money than would an award of damages under s 55. As well an action seeking an account of profits could be brought by a representative of the beneficiaries, and result in the trust fund having the amount of the profits added to it.

By contrast, section 55 contemplates that the remedy of damages will be for the individual damage that any plaintiff suffers in consequence of a breach of a covenant. While representative actions could be brought for breach of section 55 by beneficiaries under the rules of court concerning representative actions, or class actions, they would still be ones to recover the loss that individual plaintiffs had suffered. The remedies granted by the *SIS Act* do not include one of account of profits, or one that required a sum of money to be added to the trust fund.

4.2.5 Effect of section 52 (2) (d) on Possibility of Trust Deed, Consent or Judicial Order Ousting No Conflicts Rule

The possibility of the no conflicts rule being made inapplicable either by the terms of the trust deed, by an informed consent, or by judicial order arises pursuant to either the general law, or state or territory legislation. The amended definition of “governing rules”, in conjunction with section 7, makes clear that the covenant concerning conflicts in section 52 (2) (d) provides obligations that cannot be removed by any of these methods. Any clause in a trust deed, or any beneficiarys’ consent or judicial order that had been made in the past and that purported to remove all obligations concerning conflicts would be ineffective if its wording was wide enough to cover removal of the obligations under s 52(2) (d). A question that would require examination, but is beyond the scope of this paper, concerns whether any such clause or consent or order would be read down so that it was treated as ineffective to the extent that it conflicted with section 52(2) (d) but was otherwise good, or whether it was completely ineffective because it claimed more than is now legally permissible.

4.2.6 Amending Trust Deeds to Remove No-Conflict Duty?

The discussion so far may well give rise to a question of whether it would be possible for a trust deed that did not already exclude the no conflicts duty could be amended so as to exclude that duty for the future. In some circumstances it might be possible, but in other circumstances it might not.

It is fairly common for superannuation trust deeds to vest a power to amend the deed in the trustee rather than in anyone else. If, atypically, the deed vested the power to amend in someone other than the trustee, any amendment must comply with section 60 *SIS Act*. Relevantly for present purposes, section 60 forbids any amendment to the governing rules unless made with the consent of the trustee or trustees[114].

[114] It also forbids any amendment that would make the fund other than one whose sole or primary purpose was the provision of old-age pensions, or whose trustee anyone was a constitutional corporation, and a few other types of amendment not presently relevant.

In deciding whether to grant any such consent, or to exercise any power to amend that was vested in the trustee, the trustee would be obliged to comply with all of the various statutory covenants, including in particular the obligation "to perform the trustee's duties and exercise the trustee's powers in the best interests of the beneficiaries"[115]. That obligation requires any decision to amend the trust deed to be characterised as being objectively one that is in the best interests of the beneficiaries. As well the trustee would be subject to the general law requirement that it exercise any power bona fide for the purpose for which it was conferred. That obligation includes consideration of the subjective purpose and motivation of the trustee in effecting the change. If any part of its motivation was to lessen its own potential liability, or to make life easier for itself, it would be likely to fail the bona fides test. As well, if there were to be any conflict involved in deciding whether to amend the trust deed the trustee would also have to comply with the various covenants concerning conflict in s 52 (2) (d).

For employer-sponsored funds there is a requirement of equal numbers of member and employee representatives[116] among the trustees, or the directors of a corporate trustee. If there were any divergences of interest between employer and members concerning the desirability of the amendment there might be a practical difficulty in obtaining a majority for a resolution to amend. For all these reasons, it would depend on the particular amendment proposed, the circumstances in which it was proposed, and the reasons why it was proposed whether all these requirements for a resolution to amend the rules could be met.

4.2.7 The 2020 Exposure Draft

An exposure draft of proposed legislation[117], originally planned to take effect from 1 July 2020[118], would impose an additional condition on the licence of a corporate RSE licensee:

> "that the RSE licensee must not have a duty to act in the interests of another person, other than a duty that arises in the course of:
>
> (a) performing the RSE licensee's duties, or exercising the RSE licensee's powers, as a trustee of a registrable superannuation entity; or
> (b) providing personal advice"

A proposed transitional provision says that this amendment to the *SIS Act*:

> "applies in relation to any duty that exists on or after the commencement of this item, whether the duty arose before, on or after that commencement."

No such legislation had been passed by 1 July 2020. A media release by the Treasurer dated 8 May 2020 said in general terms that legislation to give effect to the Royal commission's recommendations would now have its commencement date extended by 6 months.

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[115] Section 52 (2) (c)
[116] Section 86 – 93A *SIS Act*
[117] The *Financial Sector Reform (Hayne Royal Commission Response – Protecting Consumers (2020 Measures)) Bill 2020*
[118] As a new s 29E(5) *SIS Act*. The legislation is recommendation 3.1 of the Final Report of the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry, at p 228 - 9

If legislation to this effect is enacted it will still not by implication oust the possible application of the general law no conflicts rule. It will, in practice, destroy the utility of the trust instrument freeing an RSE licensee from the no conflicts duty to any greater extent than the new licence condition enables the RSE licensee to have a duty to act in the interests of another person. It will require any RSE licensee who is, for example, the responsible entity of a managed investment scheme to stop performing one or other of those roles.

4.3 The Section 52(2) (d) Covenant Concerning Conflicts

4.3.1 Types of Conflicts to which the Covenant Applies – Construction of the Chapeau

A few miscellaneous remarks can be made about construction of the new covenants in section 52 (2) (d). The syntax of the chapeau of section 52 (2) (d) is not a model of clarity. The preferable meaning is that each of the paragraphs in section 52(2) (d) (i) – (iv) applies when there is a conflict between:

(a) either

(i) the duties of the trustee to the beneficiaries, or

(ii) the interests of the beneficiaries

and

(b) either

(i) the duties of the trustee to any other person or

(ii) the interests of either the trustee or of an associate of the trustee

An "associate" is defined, after a fashion, in section 12 *SIS Act*, by adopting the definition of "associate" in the *Corporations Act 2001*, subject to a few alterations[119]. The result of making those alterations to the text of the definition in the *Corporations Act* is too convoluted to go into here. Suffice to say that it results in a broad definition, that would catch most types of association between people that might cause one of those people to be in a situation of conflict under the general law. The consequence is that, for most practical purposes, the chapeau to s 52(2) (d) will catch all the situations of actual conflict that fall within the conflicts rule of the general law, but not merely potential conflicts.

The expression "duties to the beneficiaries" in the chapeau is not defined. As a matter of ordinary English, it would be all the duties that the trustee owed to the beneficiaries, from whatever source those duties arose. Thus, they include duties under the *SIS Act*, duties under the trust instrument, duties under the general law, and duties under any applicable legislation.

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[119] The *Corporations Act* definition of "associate" is spread over section 10 to 17 of that Act.

4.3.2 Consequences of Being Applicable Only to Actual Conflicts

Justice Sackville has pointed out some of the consequences of section 52 (2) (d) not extending to merely potential conflicts:

> " … s 52 (2) (d) does not of itself prevent a corporation acting as the trustee of two or more funds, provided that the multiple appointments do not create an actual conflict of the kind identified by the provision. However, this is quite a different proposition than accepting that a trustee can comfortably place itself in a position of potential conflict of interest or duty. If the potentiality for conflict is in fact realised, the trustee may find it impossible to comply with its duties. If, for example, a trustee is responsible for two separate funds and the interests of the respective beneficiaries are in conflict because of a common investment made on behalf of both funds, it may be impossible for the trustee to give priority to the interests of each set of beneficiaries as it is obliged to do by s 52 (2) (d) (i). There may therefore be cogent reasons why a prudent trustee, despite the circumscribed language of s 52 (2) (d) of the SIS Act, will be well advised to follow the strictures of equity warning against possible conflicts[120]."

I respectfully agree, and add that the possibility of an actual conflict arising from a trustee having some additional role is not confined to the trustee being trustee of two different superannuation funds. For example, section 601FC (1) (c) *Corporations Act 2001* imposes an obligation on the responsible entity of a registered managed investment scheme to "act in the best interests of the members and if there is a conflict between the members' interests and its own interests, give priority to the members' interests". If the trustee of a superannuation fund were to invest trust assets in a scheme of which the trustee was the responsible entity a situation could easily arise in which there was an actual conflict between the obligations of the trustee to the members of the superannuation fund and its obligations to the members of the scheme[121], and it would be impossible for the trustee to give priority to both groups[122].

If there were to be a realistic possibility of a conflict arising from a trustee having two roles, in which it might become impossible to perform the duties owed in both roles, there is an additional risk for the trustee. It is that there may be a question about whether undertaking the second of those roles, with the possibility that the unresolvable conflict might arise, involved exercising the same degree of care skill and diligence as prudent professional superannuation trustee would exercise. If it would not, the trustee would be in breach of the covenant concerning taking care[123].

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[120] The Hon Ronald Sackville AO QC "Duties of Superannuation Trustees: From Equity to Statute" (2013) 37 Australian Bar Review 1 at 13, reproduced in M Scott Donald and Lisa Butler Beatty, *The Evolving Role of Trust in Superannuation* (The Federation Press Sydney 2017) 308 at 320

[121] While section 601FC talks of a conflict between the interests of the members of the scheme and the *interests* of the responsible entity, the responsible entity would fairly clearly have an interest in performing legal obligations it owed to people other than scheme members. The proposed legislation considered at Section 3,2,6 of this paper would do away with some of the ways in which a trustee could be in a situation of conflict as a result of occupying two or more different roles.

[122] If legislation in terms of the exposure draft discussed at section 4.2.7 above is enacted this particular risk would no longer arise.

[123] That covenant is discussed further at Section 5.4.1, "the obligation to exercise care, skill and diligence", below

4.3.3 "Give Priority to the Duties to and Interests of the Beneficiaries"

The obligation to "give priority to the duties to and interests of the beneficiaries over the duties to and interests of other persons" is quite a stringent one. The "other persons" whose interests are to be subordinated are all persons other than the beneficiaries – thus the interests to be subordinated include both those of the trustee, and the interests of anybody else. That would include the interest of any related corporation of the trustee.

The "duties to the beneficiaries" in section 52(2) (d) (i) are those duties and interests concerning which the conflict exists. That is a sensible grammatical meaning of the phrase, so that "the" duties and interests refers back to the duties and interests identified in the chapeau. As well, a question of giving priority arises only when there is a conflict between certain duties of the trustee to the beneficiaries or the interests of the beneficiaries, and other duties or interests.

In construing the "interests of the beneficiaries":

> "the word "interests" has a broad general meaning which, on any view, includes the concern of the members with the due administration of the trust"[124]

Concerning the analogous duty under section 601FC (1) (c) *Corporations Act 2001* to "act in the best interests of the members and, if there is a conflict between the members' interests and its own interests, give priority to the members interests" the High Court has said that the duty[125]:

> "is narrower in one respect than the equitable rule concerning conflict of interest and duty. It does not proscribe acts of a director that put herself or himself in a position of conflict. It only proscribed acts in the course of that conflict that do not give priority to the members interests. Nevertheless, the duty is not satisfied by an honest and reasonable belief. A contravention occurs when a director prioritises her or his own interests over those of the members, no matter how honest or reasonable the director was in doing so."

Those remarks would be equally applicable to the duty under section 52 (2) (d) (i) of the *SIS Act*.

The covenant in section 52(2) (d) (i) must be read in a way that is consistent with section 52 (2) (b) (ii) and (iii). "Giving priority to" the duties to and interests of the beneficiaries therefore requires that the duties to the beneficiaries are performed *totally*, and the interests of the beneficiaries are *in no way* harmed. It follows that "giving priority to" the duties and interests of the beneficiaries is not merely a matter of engaging in a "balancing" process in which the trustee gives those duties and interests greater weight than the duties or interests with which they are in conflict.

4.3.4 "To ensure that"

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[124] *Australian Securities and Investments Commission v Lewski* [2018] HCA 63, 362 ALR 286 at [50] per Kiefel CJ, Bell, Gageler, Keane and Edelman JJ

[125] *Australian Securities and Investments Commission v Lewski* [2018] HCA 63, 362 ALR 286 at [72]

The covenants in section 52 (2) (d) (ii) and (iii) both start with the words "to ensure that". In ordinary English those words are ones that impose an obligation to achieve an outcome. They are words with a history so far as the *SIS Act* is concerned. The original 1993 version of section 52 (2) (c) contained a covenant "to ensure that the trustee's duties or powers are performed and exercised in the best interests of the beneficiaries". In *Manglicmot v Commonwealth Bank Officers Superannuation Corporation Pty Ltd*[126] Giles JA[127] held that the words "to ensure that", in that covenant, added nothing to the general law obligation of a trustee to perform and exercise its duties and powers in the best interests of the beneficiaries[128].

> "The words: "to ensure" add nothing: an obligation is an obligation. Again, the respondent was exercising a discretionary power, and "to ensure" does not turn the question of exercise of a discretionary power into one of strict liability. There is liability if the discretionary power is exercised improperly, but otherwise there is not."

The same argument could apply concerning the words "to ensure that" in section 52 (2) (d)(ii): if the trustee has a duty to the beneficiaries it has an obligation to meet that duty regardless of whether there is a conflict.

However, the argument is not applicable concerning the covenant in section 52 (2) (d) (iii). The general law does not impose on the trustee, in so many words, a duty not to affect adversely the interests of the beneficiaries. Many situations where the trustee was in breach of a duty would be ones that did adversely affect the interests of the beneficiaries, but that is not the same thing. An obligation to ensure that the interests of the beneficiaries are not adversely affected by the conflict is an additional *obligation* on the trustee, even though in many situations it would not require any different *action* to what was required by the trustee's other duties.

4.3.5 "To Ensure that the Duties to the Beneficiaries are Met Despite the Conflict"

The duties to the beneficiaries that are the relevant ones for the covenant in section 52(2) (d) (ii) are not the full range of duties that the trustee owes to the beneficiaries. Rather, they are those duties that are referred to in the chapeau to section 52 (2) (d), namely the duties of the trustee to the beneficiaries *that are in conflict* with the duties of the trustee to any other person or the interests of the trustee or an associate of the trustee. This is because:

- As with section 52(2)(d)(i) it is a sensible grammatical reading for "the duties to the beneficiaries" in section 52 (2) (d) (iii) to refer back to the duties that were identified in the chapeau to section 52(2) (d).

- As well, the requirement for the duties to be met *despite* the conflict suggests that the duties being talked about are ones that must be met *even though there is* a conflict. It is only duties that are one of the ingredients of the conflict that are of that type.

- If any wider construction were adopted of the duties involved, the provision would operate to impose a covenant, with the consequential possibility of an action for

[126] [2011] NSWCA 204; 282 ALR 167
[127] Young and Whealey JJA agreeing
[128] At [121], That holding is probably the reason why the new s 52(2) (c) does not start with "to ensure that".

damages under s 55 for breach, whenever a trustee was in a situation of conflict and failed to meet any duty whatever owed to the beneficiaries, even though that duty had nothing to do with the conflict. It would be as though a penalty for being in a situation of conflict was that extra sanctions were available against the trustee concerning the full range of its duties to the beneficiaries. This legislature should not have ascribed to it an intention to achieve so arbitrary a result.

4.3.6 "To Comply with the Prudential Standards in Relation to Conflicts"

4.3.6.1 Content of Prudential Standard 521

APRA has issued Prudential Standard SPS 521[129] concerning conflicts of interest. Unlike the covenants in s 52 (2) (d) (i) (ii) and (iii), the concern of the prudential standard is not to provide extra requirements for what a trustee is to do when it is in a particular situation of conflict. Rather, it is to require that certain management structures and procedures be adopted in the business of any RSE licensee. These structures and procedures are ones that aim to;

- identify and record in writing *all* potential and actual conflicts[130] that the licensee might face,
- ensure that all relevant officers and staff know about the actual and potential conflicts,
- ensure that the licensee has thought in advance about how it will deal with any situations of actual or potential conflict that it might encounter, and
- ensure that these structures and procedures are reviewed periodically.

Consistently with the analysis put forward in this paper, the Prudential Standard recognises that there can be occasions when the general law no-conflicts rule applies to a particular superannuation trustee or in a particular situation, and thus that it requires that not only an actual conflict, but also a realistically possible conflict, be avoided. Clause 18(b) of the Standard says that one of the things a conflict management policy must include is have controls and processes for "avoiding conflicts when required to do so". A footnote to that provision says:

> "Nothing in this Prudential Standard authorises a person to manage a conflict if the general law requires the person to avoid it."

4.3.6.2 Scope of the obligation "to comply with the prudential standards in relation to conflicts"

There is a question of construction about the scope of the obligation to comply with "the prudential standards in relation to conflicts". Clearly it includes an obligation to comply with SPS 521, but in my view the scope of the obligation is wider than that.

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[129] Superannuation (Prudential Standard) Determination No 7 of 2012

[130] Clause 9 of the Standard is explicit that the conflict management framework adopted by the licensee must be one that "identifies all potential and actual conflicts in the RSE Licensee's business operations and takes all reasonably practicable actions to ensure that they are avoided or prudently managed"

The expression “in relation to” is capable of having a wide meaning, and of indicating any sort of connection between two things, but in a particular occurrence in a statute that wide meaning can be cut down by the context and purpose of the statute[131]. It is hard to find anything in either the context or the purpose of s 52(2((d)(iv) to cut down the potential width of meaning of “in relation to”.

Thus, it is fairly clear that the covenant will apply to any obligation in a prudential standard other than SPS 521 that refers in express terms to a conflict. There is an example of this in the Outsourcing Standard SPS 231[132]. It is also strongly arguable that the covenant will apply to an obligation in a prudential standard that does not mention a conflict in express terms, but applies to a situation of conflict[133].

4.3.7 Interests and Duties Contrasted with “Relevant Interests” and “Relevant Duties”

The Prudential Standard defines the term “conflict” in terms of conflict between interests or duties, regardless of whether those interests or duties are recognised by the trustee as ones that could give rise to a conflict[134]. It requires the conflicts management framework adopted by the RSE licensee to be one that “identifies *all* potential and actual conflicts” [135] - not just those that the licensee has identified or recognised.

Notwithstanding this absoluteness, the Standard also has narrower concepts, of a “relevant duty” and a “relevant interest”[136]. The “relevant duties” and the “relevant interests” are what staff must be informed about[137], and what the licensee must record in a register of relevant duties and relevant interests[138]. As well a periodical comprehensive review of the conflicts management framework must consider whether all relevant duties and all relevant interests have been identified and are being addressed[139]. It must also address the level of compliance with the conflict management policy, including reporting on the registers of relevant duties and relevant interests[140].

Being a ‘relevant duty” or a “relevant interest” is dependent on the RSE licensee *having determined* that the duty or interest in question is relevant. The test that a licensee must

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[131] *Law Society of New South Wales v. Bruce* (1996) 40 NSWLR 77 at 84; *Travelex Ltd v FCT* [2010] HCA 33, 241 CLR 510 at [25]; and concerning the analogous expression “in connection with” see *Claremont Petroleum NL v Cummings* (1992) 9 ACSR 1 at 42; *Boylan Nominees Pty Ltd v Williams Refrigeration Australia Pty Ltd* [2006] NSWCA 100; 65 NSWLR 717 at [54] – [59]; *Thomas v State of New South Wales* [2008] NSWCA 316 74 NSWLR 34 at [19] – [21], and see generally DC Pearce, *Statutory Interpretation in Australia* (9th ed LexisNexis Butterworths Australia 2019) at [12.7] – [12.9]

[132] Clause 17: “An RSE licensee’s outsourcing policy must set out the RSE licensee’s approach to conflicts that may arise through outsourcing, including how all risks arising from such a conflict will be identified, monitored, managed and mitigated”

[133] Considered further at Section 5.3, “The outsourcing prudential standard”, below

[134] Cl 7.

[135] Cl 8 (emphasis added). Other provisions imposing absolute obligations, not dependent on anyone's opinion, concerning conflicts are found in clause 9, 11, 15 (a) and (b), 18, and 19

[136] Cl 6

[137] Cl 12

[138] Cl 15

[139] Cl 22(a)

[140] Cl 22 (b).

apply in deciding whether a duty or interest is a "relevant duty" or a "relevant interest" is that the duty or interest:

> "is one that might reasonably be considered to have the potential to have a significant impact on the capacity of the RSE licensee, the associate of the RSE licensee or the responsible person with the relevant duty or holding the relevant interest, to act in a manner that is consistent with the best interests of beneficiaries"[141]

The expression "significant impact" is ambiguous. One possible meaning is that it means an impact that is real or of substance, as opposed to being insignificant or nominal. Another possible meaning is that it is a large impact or an important one [142]. When the identification of the "relevant interests" and the "relevant duties" is a means of enabling the licensee to carry out its absolute obligations to identify and manage *all* potential and actual conflicts, a purposive construction of the Standard would lead to the first of these meanings being adopted.

4.3.8 Effect on Trustees' Obligations and Liability of Prudential Standard concerning Conflicts

An RSE licensee has a clear legal obligation to comply with all of the prudential standards[143], and to notify APRA of any significant breach. Failure to comply with the standard could ultimately lead to the licence being cancelled.

The prudential standard is relevant to the potential civil liability of a trustee concerning conflicts in two ways. One is that, to the extent that section 58B frees the trustee from the general law no-conflicts duty, it does so conditionally on, among other things, the trustee having complied with the prudential standards.

The other way in which the prudential standards are relevant to the trustee's potential civil liability concerning conflicts is that if a person suffers loss by reason of breach of any of the prudential standards relating to conflicts, an action for damages will be available to that person for breach of the covenant in s 52(2) (d) (iv).

4.4 Other Statutory Modification of the Law Concerning Conflicts

4.4.1 Prohibiting One Way a Trustee could be Permitted a Conflict – the New Section 58A

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[141] Cl 16

[142] Compare the ambiguity of "substantial" considered in cases collected in *Guthrie v Spence* [2009] NSWCA 369, 78 NSWLR 225 at [144]-[153]

[143] A prudential standard is one of the items in the RSE licensee law: Definition of *RSE licensee law* in section 10 *SIS Act*. Compliance with the RSE licensee law is a condition of every RSE licence: section 29E (1)(a) *SIS Act* [143]. A licensee is obliged to notify APRA of any significant breach that has occurred of its licence: section 29JA *SIS Act*. Failure to give such notification is a criminal offence with strict liability: section 29JA(2) and (3) *SIS Act*. Breach of a licence condition could lead to a direction from APRA to comply with the condition: section 131D(2)(b) *SIS Act*. Alternatively, it could lead to cancellation of the licence: section 29G *SIS Act.*

The 2013 legislation also introduced a new s 58A into the *SIS Act*, applicable to all regulated superannuation entities.[144] The new section 58A was enacted against the background that under the general law a trustee would not be in breach of trust if it acted in a way that was permitted by the trust instrument.

Consider the situation where there was a provision in the trust deed that

- identified a person from whom the trustee either could, or must, acquire a service, or
- identified an entity in or through which the assets of the fund could, or must be invested, or
- identified a financial product in which any of the assets of the fund could or must be invested.

A trustee who acted in accordance with such a provision would not be in breach of any of its general law obligations as trustee. There would be no breach of those obligations even if the transaction that the trustee entered was one concerning which there was a conflict between the interest of the trustee and the interests of the beneficiaries. However, the covenant in section 52 (2) (d) could still apply, because there was a conflict between those two interests.

If the transaction was one concerning which there would have been a conflict between the trustee's duty and either the interests of the beneficiary or the duty of the trustee to someone else if the trust deed lacked that provision the situation is slightly different. Because a trustee who acted in accordance with such a provision in the trust deed would not be in a situation of conflict between its duty and either the interest of the beneficial, or the duty to someone else, the covenants in section 52 (2) (d) would not come into operation.

The new section 58A no longer allows trustees to avoid being in a situation of conflict because of such a provision in the trust deed. It recognises the commercial reality that often it is the intended trustee of a superannuation fund, or someone associated with the intended trustee, who drafts the trust instrument, and thus may be motivated to lessen the obligations on the trustee. It prevents any such motive from being carried into effect by making void any provision in the trust instrument that conferred on the trustee a power or duty to acquire services from, or make investments in or through, any identified person or entity or financial product. It probably strikes at any identification that is in general terms, such as allowing acquisition of services from, or investment of trust assets in a financial product of, "any related entity of the trustee"[145]. Section 58A has the effect of requiring the trustee, or some agent of the trustee, actually to decide from whom services are to be acquired, and what investments are to be made. Any decisions of that type that the trustee made would have to comply with the various controls on trustee's decision making. All such decisions are therefore required to be in the best interests of the members, and in accord with every other covenant in section 52 (including section 52 (2) (d)) and every prudential standard.[146]

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[144] And thus not to self-managed superannuation funds

[145] The wording is "To the extent that it specifies a person (whether by name or in any other way, directly or indirectly)", and cognate words.

[146] The same device, of making void provisions in the governing rules of a trust, was also used to prevent the trust deed from excusing the trustee from a variety of other obligations whose connection to conflicts is not so clear – see sections 55B, 55C, 55D. Section 68C and 68D also made void any provision in the governing rules that precludes a director of a corporate trustee from voting, or a natural person trustee from voting, except (broadly) where such a prohibition is consistent with the obligations of the trustee or the director concerning conflicts.

The Explanatory Memorandum for the 2013 legislation was quite explicit that this was the purpose of the legislation:

> Schedule 1 to this Bill amends the *Superannuation Industry (Supervision) Act 1993 (SIS Act)* to over-ride any provisions in a fund's governing rules that require the trustee to use a specified service provider, investment entity or financial product. …
>
> The Review[147] was concerned that some trust deeds require a trustee to use a particular service provider, investment entity or financial product, effectively removing a trustee's discretion to ensure such arrangements are in the best interests of fund members. The Review recommended (recommendation 2.14) that any such provisions in trust deeds should be over-ridden.
>
> The Act will be amended to over-ride any provision in the governing rules of a registrable superannuation entity (RSE) that requires the trustee to use a specified service provider, investment entity or financial product…
>
> The amendments will restore a trustee's discretion to act in the best interests of members when entering into relevant arrangements.
>
> The section overrides provisions that state that the RSE licensee `may' use a particular entity as well provisions that state the RSE license `must' do so. This is to ensure that the requirements of the provision cannot be avoided through a clause that confers power to use particular named entities which might have the effect of encouraging or sanctioning the use of those entities instead of considering other options in the market.[148]

4.4.2 Tougher Requirements for Defence to Section 55 Claim

Another provision of the 2012 legislation that bears upon the trustee's obligations concerning conflicts is that the defence available to a trustee to an action for damages under section 55 of the SIS Act was made more stringent. The 1993 version of section 55 contained a section 55(5), which made it a defence to an action under section 55 for loss or damage suffered by a person as a result of the making of an investment by or on behalf of the trustee that the trustee shows that the investment was made in accordance with an investment strategy formulated under the covenant in section 52 (2) (f)[149]. It also contained section 55 (6), under which it was a defence to an action for loss or damage suffered by a person as a result of the management of any reserves by the trustee if the defendant established that the management of the reserves was in accordance with the covenant required by section 52 (2) (g)[150].

The 2012 legislation replaced the original section 55 (5) and (6). The new section 55 (5) made the availability of the defence to an action for loss arising concerning an investment

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[147] The review into the governance, efficiency, structure and operation of Australia's superannuation system or the Super System Review (Cooper Review)

[148] There was also a Supplementary Explanatory Memorandum which explained an amendment to the Bill as being one that "limits section 58A so that a governing rule is only void to the extent it is contrary to that section. That is, to the extent it provides that the trustee may or must use a particular service provider or investment entity, or invest in a particular financial product." That does not affect the objective of the section

[149] The terms of section 55 (2) (f) are set out at footnote 91 above

[150] The terms of section 55 (2) (g) are set out at footnote 91 above

dependent upon the defendant establishing that it had complied with *all of* the covenants that applied to that defendant in relation to the investment. The new section 55 (6) made the availability of the defence to an action for loss arising from management of reserves dependent upon the defendant establishing that it had complied with *all of* the covenants that applied to the defendant in relation to the management of the reserve. Thus, if one of the conflicts covenants applied to the defendant concerning the making of an investment, or the management of the reserve, the defendant would have a defence to an action for loss or damage arising from breach of any covenant concerning that investment, or that reserve, only if the conflict covenant had been complied with.

4.4.3 Adding Civil Penalty Remedies

In 2019 there was still further legislation[151] that added a new section 54B to the Act. It prohibits contravention of any of the covenants required by section 52, and makes breach of that prohibition a civil penalty provision. This gives rise to additional remedies for breach of (inter alia) any of the conflicts covenants, but does not affect the existing remedy of damages under section 55[152].

Breach of any civil penalty provision can result in the Court imposing a monetary penalty not exceeding 2400 penalty units[153], provided it is satisfied the convention is a serious one[154]. As well the court can make an order for payment to the superannuation entity of any loss or damage it has suffered by reason of the contravention[155]. A contravention of a civil penalty provision that is dishonest and with intent to gain an advantage, or with intent to deceive or defraud someone, is a criminal offence[156].

PART 5 - PRINCIPLES THAT RELATE TO SITUATIONS OF ACTUAL OR POSSIBLE CONFLICT BUT DO NOT USE THE WORD 'CONFLICT'

There are principles of both the general law and of the statute-based law that are capable of applying to a trustee who is in a situation of actual or possible conflict, where the statement

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[151] *Treasury Laws Amendment (Improving Accountability and Member Outcomes in Superannuation Measures No 1) Act 2019* (No 40 of 2019), effective from 5 April 2019. Other changes effected by that legislation are that it added new section 52(9), (10), (10A), (11) (12) and (13) broadly relating to disclosure of benefits and outcomes of the operation of the fund, comparison of the outcomes of that fund with the outcomes of other funds and publicising an assessment of the outcomes of the fund against certain benchmarks.

[152] Section 54B(5). The 2019 legislation repealed sections 55(1) and (2), and amended section 55 (3) and 55 (4A) (a) so that they related to any contravention of section 54B (2) or 54C (1), but this does not change the substance of the action for damages available under section 55.

[153] A "penalty unit" in Commonwealth legislation is the amount of $210, which will be indexed from 1 July 2020 by reference to the All Groups Consumer Price Index published by the Australian Statistician - section 4AA *Crimes Act 1914 (Cth*). Thus, the maximum civil penalty for breach of a civil penalty provision in the *SIS Act* is $504,000, prior to any indexation.

[154] Section 196. Only the Regulator can bring proceedings to seek the penalty – section 197 *SIS Act* – but the trustee has a limited right of intervention – section 215 *SIS Act*. The body who brings civil penalty proceedings does not have an obligation of fairness akin to that of a prosecutor in a criminal case: *Morley v ASIC* [2010] NSWCA 331, 274 ALR 205 at [678] - [700]. It would be subject to the "model litigant" requirements of governmental entities.

[155] Section 215

[156] Section 202

of the principle does not include the word “conflict”. It is not possible to identify these exhaustively. The rest of this paper shall give a few examples.

Outsourcing to a related company is a type of situation that could sometimes give rise to an actual or possible conflict for a superannuation trustee, in the eyes of the general law. As the Regulation Impact Statement for the Superannuation Prudential Statements said[157]:

> The superannuation industry relies heavily on outsourcing. Many core functions are often outsourced, including administration, custody, investment management and other support functions such as secretariat and information technology.

I will therefore draw the examples from outsourcing.

5.1 General Law Obligations on a Trustee even when Excused from the No-conflicts Rule

The trustee might be freed from the no-conflicts rule, or from liability for a breach of it, by either a provision in the trust deed, or court order, or through the operation of section 58B. However, that by itself would not free the trustee from other equitable obligations under the general law. Those equitable obligations include that even if a trustee is entitled to exercise a power in a way that benefits itself or a related entity, it must still act in accordance with the rule that the power be exercised bona fide for the purpose for which it was conferred[158]. The power must be exercised after giving real and genuine consideration to how it is to be exercised[159]. The trustee must act, concerning the affairs of the trust, with reasonable skill care and diligence[160].

There is also an additional general law duty if a fiduciary is in a situation of potential conflict through acting for two different principals, but the fiduciary is not thereby in breach of the no-conflicts rule because both principals have consented to his acting in the double capacity. Millett LJ in *Bristol and West Building Society v Mothew* [1998] Ch 1 CA, 19[161] said:

> “Even if a fiduciary is properly acting for two principals with potentially conflicting interests he must act in good faith in the interests of each and must not act with the

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[157] *Regulation Impact Statement, Superannuation Prudential Statements* OBPR ID: 14155 p 20

[158] *Hordern v Hordern* [1910] AC 465 at 475; *Ngurli v McCann* (1953) 90 CLR 425 at 445 per Williams ACJ, Fullagar and Kitto JJ; *Metropolitan Gas Co v Federal Commissioner of Taxation* (1932) 47 CLR 621 at 633

[159] *Karger v Paul* [1984] VR 161 at 164-5. Which includes the trustees applying their own mind to the question, not merely adopting what someone else suggests: *Turner v Turner* [1984] 1 Ch 100.

[160] *Speight v Gaunt* (1883) 9 App Cas 1 at 19; *Permanent Building Society (in liq) v Wheeler* (1994) 11 WAR 187 at 237; *Breen v Williams* (1996) 186 CLR 71 at 137. The general law obligation to act with care and skill has now been modified, so far as registrable superannuation funds are concerned, by the statutory covenants requiring care skill and diligence – see section 5.4.1, “The obligation to exercise care, skill and diligence”, below.

[161] A passage repeatedly quoted with approval by Australian judges: *Macedone v Collins* (1997) 7 BPR 15,127 at 15,133 (though incorrectly attributed to a “Lord Staughton”) per Cole JA (Beazley JA and Abadee AJA agreeing); *Beach Petroleum NL v Abbott Tout Russell Kennedy* (1997) 26 ACSR 114 at 264 per Rolfe J (and apparently not challenged in the unsuccessful appeal from the decision of Rolfe J – *Beach Petroleum NL v Abbott Tout Russell Kennedy* [1999] NSWCA 408, 48 NSWLR 1 at [155]); *Re Moage Ltd (in liq) v Jagelman* (1998) 153 ALR 711 at 718-9 per Burchett J; *Honeychurch Management Pty Ltd v Deloitte Touche Tohmatsu (a firm)* [2005] Tas SC 13 at [78] per Blow J; *Rigg v Sheridan* [2008] NSWCA 79 at [46] per Handley AJA, Beazley and Giles JJA agreeing; *McCourt v Cranston* [2009] WASC 56 at [160] per Templeman J, and *Anthony v Morton* [2018] NSWSC 1884 at [620] per Ward CJ in Eq

> intention of furthering the interests of one principal to the prejudice of those of the other … I shall call this 'the duty of good faith'. But it goes further than this. He must not allow the performance of his obligations to one principal to be influenced by his relationship with the other. He must serve each as faithfully and loyally as if he were his only principal.
>
> Conduct which is in breach of this duty need not be dishonest but it must be intentional. An unconscious omission which happens to benefit one principal at the expense of the other does not constitute a breach of fiduciary duty, though it may constitute a breach of the duty of skill and care. This is because the principle which is in play is that the fiduciary must not be inhibited by the existence of his other employment from serving the interests of his principal as faithfully and effectively as if he were the only employer. I shall call this 'the no inhibition principle' … Finally, the fiduciary must take care not to find himself in a position where there is an *actual* conflict of interest so that he cannot fulfil his obligation to one principal without failing in his obligation to the other."

5.2 The Power to Outsource

Quite separately to whether a particular outsourcing would involve a conflict, there is a question of whether the trustee had power to outsource at all.

The default rule of the general law allowed a trustee to engage other people to perform tasks concerning the administration of the trust only to a very limited extent. A trustee was permitted to act through an agent only concerning the performance of tasks that were purely instrumental and involved no exercise of discretion, concerning tasks for which there was a practical necessity to engage an agent[162], or for which it was common business practice to engage an agent[163]. That default rule could be widened, narrowed or made totally inapplicable to a particular trust by express provision in the trust deed.

The default rule concerning the power for a trustee to engage other people was widened, subject to any contrary provision in the trust instrument, by legislation in all Australian States and Territories[164]. There are significant differences in the extent to which the legislation of the different States and Territories permits trustees to appoint other people to act for them[165]. However, none of the State and Territory legislation confers a complete power on trustees to engage others to act on their behalf.

The way the NSW *Trustee Act* s 53 puts it is that the trustee can employ an agent:

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[162] Eg to sell stock that could be sold only on the stock exchange, and where only stockbrokers were permitted to enter contracts for the sale and purchase of stock on the exchange

[163] Eg it is common business practice to engage a real estate agent to find a purchaser for a parcel of land, notwithstanding that it is possible to sell land by a private sale without any involvement of an agent. See generally *Speight v Gaunt* (1883) 22 Ch D 727, (1883) 9 App Cas 1

[164] S 53 *Trustee Act 1925 (NSW)*, s 28 *Trustee Act 1958 (Vict)*, s 54 *Trusts Act 1973 (Qld)*, s 53 *Trustees Act 1962 (WA*), s 24 *Trustee Act 1936 (SA)*, s 20 *Trustee Act 1898 (Tas*), s 53 *Trustee Act 1925 (ACT)* and s 17 *Trustee Act (NT)*.

[165] A detailed explanation and comparison of the relevant provisions of the States and Territories is in *Jacobs on Trusts* at [17-24] – [17.31]. Section 11 *Trustee Act 2000 (UK)* confers a much wider power of appointing agents than the legislation of any of the Australian States or Territories, so recent English cases on the topic are of limited use. Ascertaining what power a trustee has to appoint an agent is one area where identification of the proper law of the trust is necessary – see footnote 88 above

> "to transact any business or do any act required to be transacted or done in the execution of the trust or in the administration of the estate."[166]

Section 53 enables the trustee to engage others to perform particular types of tasks, but not to exercise discretions vested in the trustee that are central to the operation of the trust. Slattery J has held that

> Section 53 enables a trustee to delegate to any person all the trustee 's powers and duties, other than his discretionary powers and the receipt and payment of money… The Trustee could nevertheless probably delegate his discretion in minor matters of administration.[167]

In New South Wales the default rule conferring power for a trustee to delegate tasks including the exercise of significant discretions arises from a different section of the *Trustee Act* to section 53, namely s 64. Delegation is permitted only when the trustee is absent from the state or about to leave it, and can only be for two years[168]. An appointment of an agent under s 53 is made on the basis that "The trustee shall not be responsible for the default of any such agent if employed in good faith"[169], but a delegation under s 64 is on terms that the trustee remains liable for the acts of the delegate. Thus, the *Trustee Act* itself draws a distinction between appointment of an agent under s 53, and delegation. Delegation under s 64 will be irrelevant to most superannuation funds, because the preconditions for the operation of s 64, namely being absent from the state or about to leave it, are ones that only a natural person could satisfy, and these days most superannuation funds have corporate trustees[170].

The *SIS Act* does not in terms confer on a superannuation trustee any power to appoint an agent or a delegate. Section 52(2)(h) is a covenant by the trustee:

> "not to enter into any contract, or do anything else, that would prevent the trustee from, or hinder the trustee in, properly performing or exercising the trustee's functions and powers"

One of the implications of that covenant is stated by s 52(5) *SIS Act*:

> "A covenant referred to in paragraph (2)(h) does not prevent the trustee from engaging or authorising persons to do acts or things on behalf of the trustee."

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[166] This language repeats that of s 23 of the *Trustee Act 1925 (UK)*, analysed in Gareth Jones, "Delegation by Trustees: A Reappraisal" (1959) 22 *Modern Law Review* 381. The NSW section is narrower than the 1925 English one in limiting the classes of agents who can be empowered to receive trust money.

[167] *Robert Thomas Grant as trustee of the Grant Family Testamentary Trust* [2013] NSWSC 1603 at [58]

[168] If the trustee has delegated, and returns to the state before two years has expired, he can then delegate for a maximum of another two years – s 68(4).

[169] S 53 (3) *Trustee Act 1925 (NSW)*

[170] Other States and Territories also have a separate statutory power to delegate to the statutory power to appoint an agent - s 30 *Trusts Act 1958 (Vic)*, s 56 *Trusts Act 1973 (Qld)*, s 54 *Trustee Act 1962 (WA)*, s 17 and 17A *Trustee Act 1936 (SA)*, s 25A Trustee Act (Tas). The precise circumstances in which delegation is permitted differ, in ways explained in *Jacobs on Trusts* at [17-33]. However, all of them have preconditions for delegation that are capable of being satisfied only by natural persons.

But section 52 (5) does not itself confer any power on the trustee to appoint agents or to delegate. All it does is say that the section 52(2) (h) covenant *does not stop* the trustee from appointing others or delegating. Any power actually to appoint an agent or delegate must be found somewhere else.

If the trustee is to have the power to outsource functions to any greater extent than is permitted under the trustee legislation of whichever State or Territory provides the proper law that governs the trust, the power to do so would ordinarily have to be contained in the trust instrument, or conferred by the court under the advantageous dealings section[171]. If a trustee purported to outsource functions to a greater extent than it had power to do, it would be acting in breach of trust, and at risk of general law equitable remedies being ordered against it to require the trustee to make good any loss that the trust fund suffered as a result of the unauthorised outsourcing. As well it would probably be in breach of the covenant to take due care, and so potentially liable to an action for damages under s 55. These risks would apply regardless of whether the outsourcing was to a related company.

5.3 The Outsourcing Prudential Standard

APRA has made a Prudential Standard[172] that relates specifically to outsourcing of material business activities[173]. It is like SPS 521 concerning conflicts of interest in that it requires certain management structures and procedures to be adopted in the business of an RSE licensee. However, it is unlike SPS 521 in also containing many detailed provisions concerning the manner in which any particular instance of outsourcing is conducted. It applies regardless of whether the outsourcing is to a related company, and so is capable of applying to those situations where there is an actual or potential conflict. Full discussion of the requirements of the Standard is beyond the scope of this paper. However, they include:

- " The Board is ultimately responsible for any outsourcing of a material business activity undertaken by an RSE licensee. Although outsourcing may result in the service provider having day-to-day managerial responsibility for a business activity, the RSE licensee is responsible for complying with all prudential requirements and all other non-delegable legal obligations[174] that relate to the outsourced business activity[175]." This provides a significant limit on the terms of any outsourcing agreement.

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[171] discussed at footnote63 above.
[172] *Prudential Standard SPS 231 Outsourcing* dated November 2012.
[173] The Standard defines a "material business activity" as being "one that has the potential, if disrupted, to have a significant impact on an RSE licensee's business operations, its ability to manage risks effectively, the interests, or reasonable expectations, of beneficiaries or the financial position of the RSE licensee or any of the RSE's or its connected entities, having regard to such factors as" [a list of six varied matters]: cl 9. While the presence of other characteristics could be enough to make a business activity a material one, it is sufficient if it is one that has the potential if disrupted to have a significant effect on the interests or reasonable expectations of the beneficiaries. This definition presents a problem of construction concerning the word "significant" analogous to that considered at footnote 142 above.
[174] The Standard does not itself identify those non-delegable legal obligations.
[175] Cl 13

- That the RSE licensee has "undertaken a tender or other selection process for selecting the service provider"[176]. That goes some way towards assisting the trustee to act in the interests of the beneficiaries[177].

- That the RSE licensee can demonstrate that in deciding to outsource a particular activity and entering the outsourcing agreement the trustee has determined that its conduct in relation to the outsourcing agreement is in the best interests of beneficiaries[178]. Given the breadth of meaning of "in relation to"[179], the "conduct in relation to the outsourcing agreement" would include deciding to outsource the particular function at all, deciding whether the function is best outsourced on its own or as part of a package and (and if so what package) of other functions, the range of potential suppliers considered, the choice of criteria by reference to which to choose the supplier, the process through which the supplier was to be chosen, and the depth of investigation or research that was gone into concerning each of these matters.

  This requirement is more stringent than the covenant in section 52 (2) (c) *SIS Act*. The *IOOF Case* has held that whether a trustee has breached that covenant can be decided by considering whether it can be shown, at the time of the trial of any allegation of breach of the covenant, that the course of action that the trustee adopted was not to be in the best interests of the beneficiaries, regardless of whether the decision-making process by which the trustee came to that decision is defective[180]. The *IOOF Case* has also held that the "test is objective and is to be applied prospectively, that is, from the position of the trustee at the time of the decision, without impermissible hindsight."[181]. Further, in alleging a breach of the covenant in section 52(2) (c) a plaintiff would bear the onus of proving that the action of the trustee was not in the best interests of the beneficiaries. By contrast, this requirement of the outsourcing standard places an onus on the trustee. It requires the trustee to be able to demonstrate that it made a decision ("has determined"), at the time of deciding to outsource the activity, and also at the time of entering the outsourcing agreement, that its conduct was in the best interests of the beneficiaries. This requirement of the outsourcing standard goes quite a way towards assisting the trustee to act in the interests of the beneficiaries.

- If the outsourcing arrangement is with an associated entity the RSE licensee must be able to demonstrate that the arrangement is conducted on an arm's length basis and

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[176] Cl 19(b).
[177] The expression "or other selection process" probably cannot be read down using the *eiusdem generis* rule to refer only to a selection process like a tender, because the better view is that there must be two or more terms before general words like "or other thing" to enable the *euisdem generis* rule to operate: see D Pearce, *Statutory Interpretation in Australia* (9th ed LexisNexis Australia 2019) at [4.37]. However, a purposive construction, and reading the requirement in conjunction with the requirement that trustee has determined that its conduct in relation to the outsourcing agreement is in the best interests of the beneficiaries would limit the type of selection process that was permitted.
[178] Cl 19 (k).
[179] See footnote 131 above
[180] *Australian Prudential Regulation Authority v Kelaher* [2019] FCA 1521; 138 ACSR 459 ("*IOOF Case*") at [53]
[181] *IOOF Case* at [55]

> in the best interest of beneficiaries[182]. By being applicable whenever the outsourcing arrangement is with an associated entity, this requirement will be applicable in many of the situations that would be covered by the no-conflicts rule of the general law, and assists in protecting and promoting the interests of the beneficiaries. In *Jones*[183] Thomas J had held that the trustee "was not placed in the position of having to figuratively detach itself from AMP in order to question its relationship with that company." That remark could not be made concerning a trustee that was obliged to comply with this outsourcing standard.

When a trustee is contemplating outsourcing to a related entity, and thus is at risk of being in a conflict situation, all the requirements of that outsourcing standard must be complied with, in addition to the requirements of the conflicts covenant. If there is a breach of any Prudential Standard whatsoever (including, therefore, both the outsourcing standard and the conflicts standard) the trustee would lose the protection from the general law concerning conflicts that is conferred on it by s 58B.

Breach of this prudential standard can give rise to the same serious regulatory consequences as could arise from a breach of the Conflicts Prudential Standard [184]. It does not of itself give rise to any civil liability on the part of the trustee, except to the extent that the breach amounts to a breach of the covenant in section 52 (2) (d) (iv). However, liability for breach of the prudential standard can arise by an indirect route. If the Regulator has sought an undertaking from the trustee about complying with a prudential standard, and that undertaking has been breached, the Court has power to make orders for compensation of any person who has suffered loss or damage as a result of the breach[185]. As well, failure to comply with a prudential standard could be a potentially powerful piece of evidence in an action alleging the trustee had failed to comply with the covenant requiring it to exercise due care skill and diligence.

5.4 Other Duties Relevant to Conflict Situations

The legislation passed in 2012 introduced a new section 51A into the *SIS Act*. It provided:

> To avoid doubt, each covenant referred to in sections 52 to 53 or prescribed under section 54A, and each obligation referred to in sections 29VN and 29VO, that applies to a trustee of a superannuation entity, or a director of a corporate trustee of a superannuation entity, applies in addition to every other covenant or obligation referred to in those sections that applies to the trustee or director.

While section 51A does not mention any obligations of the trustee under the general law, it would also be the case that all of the general law obligations of the trustee (which might in

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[182] Cl 16
[183] At 711
[184] See text at footnote 143 above.
[185] Section 262A *SIS Act*

some circumstances include the general law no-conflicts duty) apply in addition to the statutorily required covenants[186].

This is consistent with the construction of the covenants in section 52(2) (d) (i) and (ii), which require a trustee who is in a conflict situation to perform *all* the duties that the trustee owes to the beneficiaries and that are one of the ingredients of a conflict. And, of course, those duties could include complying with all the statutory covenants, as well as any other duties that the trustee owes under the general law.

5.4.1 The obligation to exercise care, skill and diligence

Without wanting to downplay the significance of the other duties, one duty that is of particular importance when a trustee is in a conflict situation is the duty arising under the covenant in section 52 (2) (b):

> to exercise, in relation to all matters affecting the entity, the same degree of care, skill and diligence as a prudent superannuation trustee would exercise in relation to an entity of which it is trustee and on behalf of the beneficiaries of which it makes investments

5.4.2 Construction of the Covenant to Exercise Care, Skill and Diligence

In construing that covenant, the obligation of the trustee to exercise care skill and diligence is not restricted to the trustee's activity in making investments. Rather, the covenant expressly requires the trustee to exercise care skill and diligence "in relation to *all matters* affecting the entity". The standard of care skill and diligence that the trustee is required to exercise is the same standard as a prudent superannuation trustee would exercise in relation to a certain type of *entity*, not in relation to a certain type of decision. That entity has two characteristics – it is one of which the notional prudent superannuation trustee is a trustee, and one on behalf of the beneficiaries of which the prudent trustee makes investments[187].

The extent of the obligation of the trustee to exercise care skill and diligence is made clearer by section 52 (3), which provides:

> In paragraph (2)(b), a superannuation trustee is a person whose profession, business or employment is or includes acting as a trustee of a superannuation entity and investing money on behalf of beneficiaries of the superannuation entity.

In other words, the standard of care skill and diligence required by the covenant in section 52 (2) (b) is that of a professional superannuation trustee who has active investment duties to perform. It is well established that a higher standard of care is expected from a

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[186] As the introductory phrase "to avoid doubt" shows, it was arguable, and in my view correct, that even before s 51A was enacted every one of the statutory covenants and obligations of the trustee applied cumulatively.

[187] Putting this into the language of grammatical analysis, the words "on behalf … of which it makes investments" is an adjectival phrase, that describes "the beneficiaries". The phrase "on behalf of the beneficiaries of which it makes investments" is an adjectival phrase that describes "entity"

professional trustee than from an ordinary person who becomes a trustee[188]. However if there were to be litigation about whether a trustee had breached this duty it may well be necessary to have evidence of precisely what the trustee had done or failed to do in the transaction that was alleged to be a breach, evidence about what reasonably practicable alternatives were available to the trustee, and evidence about the costs and other advantages and disadvantages of the possible alternatives. As well, expert evidence may sometimes be required to establish how a professional superannuation trustee would act in a comparable situation[189].

If the *SIS Act* imposed just a covenant to exercise care and skill that might arguably require care in only those positive acts that the trustee engaged in[190]. The inclusion of an obligation to exercise diligence makes clear that as well the trustee must give regular and persevering attention to whether any positive action is called for.

5.4.3 Application to outsourcing of the covenant to exercise care

When a trustee is outsourcing some task, whether to an associated entity or not, the covenant will require the trustee to exercise care in negotiating the terms of the agreement. For the appointment to be one made in accordance with the standards of a professional trustee, one would expect that agent who is appointed be one who has the necessary qualifications and experience to carry out the task that it is given[191], and who is not going to be in a position of conflict[192].

A particular difficulty is that there will often be a question about whether the terms on which the entity is appointed will impose liability for negligence or other malperformance of that task, or will exclude liability[193]. When the appointment is of an associated entity there will often be the potential for a conflict of interest between the trustee and the beneficiaries concerning whether there is such an exclusion clause. It could be in the interest of the

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[188] *Bartlett v Barclays Bank Trust Co Ltd (No 1)* [1980] Ch 515 at 534; *Gill v Eagle Star Nominees Ltd* (Supreme Court of New South Wales Equity Division, 22 September 1993, unreported) at 13 per Gleeson CJ; *Nestle v National Westminster Bank plc* [1993] 1 WLR 1260 at 1282; *Australian Securities Commission v AS Nominees Ltd* (1995) 62 FCR 504 at 517-18; *Wilkinson v Feldworth Financial Services Pty Ltd* (1998) 29 ACSR 642 at 692-3; *Australian Securities and Investments Commission v Australian Property Custodian Holdings Ltd (recs and mgrs. Apptd) (in liq) (controllers apptd) (No 3)* [2013] FCA 1342 at [536] – [542]; *Australian Securities and Investments Commission v Drake (No 2)* [2016] FCA 1552, (2016) 340 ALR 75 at [272]-[276] per Edelman J; *Australian Prudential Regulation Authority v Kelaher* [2019] FCA 1521; 138 ACSR 459 at [27]-[29], [37] per Jagot J

[189] Evidence that acting in a particular way was common practice for professional trustees would be relevant to show that a failure to follow that practice involved taking insufficient care. Conversely, evidence that a common practice of professional superannuation trustees was followed would be relevant to, but not decisive of, a conclusion that the trustee had exercised due care.

[190] Any such argument would start under the handicap that the general law duty of a trustee applies not only to positive acts that the trustee engages in – as well the trustee must consider from time to time whether careful management of the trust property and exercise of the trustee's discretions requires some action to be taken: *In Re Hay's Settlement Trusts* [1982] 1 WLR 202 at 210; *Turner v Turner* [1984] 1 Ch 100 at 109-110.

[191] *Re Earl of Lichfield* (1737) 1 Atk. 87, 26 ER 57; *Ghost v Waller* (1846) 9 Beav. 497, 50 ER 435; *Fry v. Tapson* (1884) 28 Ch.D. 268; *Re Gasquoine* [l894] 1 Ch. 470.

[192] *Wilkinson v Feldworth Financial Services Pty Ltd* (1998) 29 ACSR 642 at 694

[193] From the first enactment of the *SIS Act* section 116 has made void any provision in the governing rules, or in an agreement between the trustee and an investment manager that purports to exclude or limit the liability of the investment manager. But outsourcing can occur concerning many tasks besides investment management.

trustee for there to be an exclusion of liability, because such a clause would tend to improve the profitability of the associated entity, to the benefit of the trustee, or because it was in the interests of the trustee to be a loyal and helpful member of its group. It could be in the interests of the beneficiaries for there not to be any such exclusion, to maximise the extent to which the trust funds would avoid depletion as a result of any errors of the associated entity.

Entering an agreement with an associated entity, that contained an exclusion or limitation of liability could be a breach of the trustee's obligation under the conflicts covenant, because it was failing to give priority to the interests of the beneficiaries, and because it was failing to ensure that the interests of the beneficiaries are not adversely affected by the conflict. As well, if a prudent superannuation trustee in analogous circumstances would not enter an outsourcing contract containing such an exclusion clause, or would only enter a contract with an exclusion clause if certain other conditions were met, the trustee might be in breach of its obligation under the duty of care covenant[194]. Further, if there has been a breach of any covenant or any provision of the outsourcing standard the trustee will be denied any relief under section 58B SIS Act from the general law no-conflicts rule that might apply to it.

The legislation of the States and Territories other than South Australia, Tasmania and the Northern Territory contains a provision to the effect that, if the trustee appoints an agent within the ambit permitted by that statute, "the trustee shall not be responsible for the default of any such agent if employed in good faith"[195]. What that means is that the trustee is not to be vicariously liable for losses that the beneficiary suffers through default by the agent. It does not mean that a superannuation trustee cannot be in breach of the statutory covenant requiring it to take care in its initial appointment of the agent, even if the appointment is made in good faith[196].

There are two respects in which the recent *IOOF case*[197] might now provide an inadequate guide to how trustees could legitimately act when outsourcing functions to a related entity[198]. One of the reasons why the trustee in that case was not liable for having failed to sue a

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[194] It is not inevitable that it is failing to act in the best interests of the beneficiaries, or lacking in the required degree of care, to enter an outsourcing contract containing an exclusion clause – for example services under a contract without the exclusion clause might cost $(X + Y), services under a contract with the exclusion clause might cost $X, and insurance against the excluded risks might be obtainable for less than $Y. As with all questions of negligence, close analysis of the facts of the situation that the allegedly negligent person was in, and the reasonably practicable alternatives that were open is required before the conclusion of negligence can be drawn.

[195] S 53 (3) *Trustee Act 1925 (NSW*), s 28 (1) *Trustee Act 1958 (Vic)*, s 54(1) *Trusts Act 1973 (Qld)*, s 53 (1) *Trustees Act 1962 (WA)*, s 53 (1) *Trustee Act 1925 (ACT)*. The legislation in South Australia, Tasmania and the Northern Territory excludes liability of a trustee only by saying "a trustee is not chargeable with breach of trust by reason only of his having made, or concurred in making, any such appointment": section 24 (2) *Trustee Act 1936 (SA)*, s 20 (1) *Trustee Act 1898 (Tas)*, s 17 (1) *Trustee Act (NT)*. A provision so worded is probably not enough to stop the trustee from being vicariously liable for negligence or other default on the part of the agent.

[196] Even if, contrary to my view, the State legislation were to be construed as protecting the trustee from liability for having made a careless appointment, the State legislation would be overridden to that extent pursuant to s 7 *SIS Act*, and perhaps also s 109 *Constitution*, so that the *SIS Act* covenant requiring care prevailed. .

[197] *Australian Prudential Regulation Authority v Kelaher* [2019] FCA 1521; 138 ACSR 459 (*"IOOF Case")*

[198] It is not useful to engage in detailed analysis of the *IOOF* decision itself, partly because many of the events with which that case was concerned occurred before present-day legislative standards were operative, and because the case was beset by such severe inadequacies of proof that the judge found that "APRA's case fails at the hurdle of proof" (*IOOF Case* at [46]).

related service company was because the terms on which it engaged the service company imposed "reciprocal and overlapping obligations" on the trustee and the service company, so that it was hard to attribute a loss to a breach of one obligation by one party to the agreement, rather than to breach of a different obligation by the other party to the agreement[199]. The Judge accepted that:

> "…the very nature of the Service Engagements, providing as they did for a series of reciprocal and overlapping obligations and contemplating such a high degree of cooperation and shared responsibility for the performance of the Services, would have made it inherently difficult to isolate and attribute liability to IOOF Service Co for any perceived deficiencies in the Services"[200]

While ultimately it would be a matter of what alternative drafting was practical and reasonable in the circumstances, it is at the least a question for examination whether a reasonably careful superannuation trustee would now enter agreements that had the potential for raising that type of problem. It was not an issue in the *IOOF Case* whether a reasonably careful professional superannuation trustee would have appointed the service company on terms that divided up the responsibilities of the trustee and the agent in terms that made it likely that it would be impossible to tell who was at fault when the trust fund or a beneficiary suffered a loss, so the case provides no authority concerning that question.

In the *IOOF Case* another source of difficulty, in the trustee being able to hold the service entity liable, was that the terms of the exclusion clause that was entered were themselves unclear. It excluded liability on the service company for "indirect or consequential loss". The scope of that exclusion is quite debateable[201]. Again, it is at least a question for examination whether a reasonably careful superannuation trustee could now enter agreements containing a similar lack of clarity.

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[199] *IOOF Case* at [97] – [106], [109] – [111]
[200] *IOOF Case* at [110]
[201] *IOOF Case* at [107] – [108]