

The Navigator

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Trustee Investment Powers

General Overview

A trustee holds legal title of trust assets for the benefit of the trust beneficiaries. With the legal ownership over trust assets comes a fiduciary obligation that the assets should be properly invested. In general, when authorized either by the terms of the trust instrument or legislation, the trustee has a duty to invest the assets as would a “prudent investor” in similar circumstances.

The power to invest trust assets is usually set out in the trust instrument (e.g. trust agreement or Will). The trust instrument must therefore always be reviewed to determine what the trustee can or cannot do with regards to investing, prior to relying on the investment powers set out under the governing provincial trustee legislation or the Civil Code of Quebec (CCQ) [“provincial legislation”]. It is possible that the trust instrument may provide more extensive or restrictive investment powers than those set out under the provincial legislation. If the trust instrument extends the trustee’s investment powers beyond the scope of the provincial legislation, this will override the investment powers authorized by law. The trustee must nevertheless be guided by the prudent investor standard. If the trust instrument limits the trustee to certain kinds of investments, the trustee is bound by the provisions set out in the trust instrument with regards to the investment of trust assets, even if other investments allowable by law might provide a higher return.

Where the trust deed is silent with respect to the trustee’s investment powers, the trustee may rely on the statutory investment powers that governs the trust. A trust instrument may subject the trust to the applicable provincial legislation or due to specific circumstances (such as the trustee’s residency), the provincial legislation may apply. In general, the law of the place where trustee decisions are made govern the trust.

If a trustee makes an unauthorized or imprudent investment, he or she



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may be found to be in breach of trust and personally liable to the beneficiaries of the trust for any losses to the trust property that results and may be required to reimburse the trust for the shortfall.

It is important to note that regardless of whether a trustee's investment powers are derived from a trust instrument or statute, a trustee, in exercising his or her power, must be guided by the following principles when making investment decisions:

- a. Unless otherwise specified in the trust instrument, the trustee should always try to be even-handed in investing the trust assets for the income and capital beneficiaries (if different persons). There is always a tension between these two parties because the income beneficiaries want the trustee to generate as much income as possible and the capital beneficiaries want to preserve the purchasing power of the capital;
- b. The trustee must act honestly. The trustee has been selected by the settlor to manage and distribute the trust assets in accordance with the settlor's wishes as provided for in the trust instrument;
- c. The trustee must not select speculative or unduly risky investments; and

- d. The trustee must avoid personal conflicts of interest at all times and must act for the benefit of the beneficiaries.

Legal List Approach

Most provincial legislation provided for a list of authorized investments in which the trustee could invest. These lists have been gradually replaced by a "prudent investor" standard, which essentially permits a trustee to purchase, retain and dispose of any assets as a prudent investor should.

The CCQ still contains a codified list of investments; however, it is not restrictive. The CCQ provides that the trustee *"has the control and exclusive administration of the trust [assets] and ... may take any proper measure to secure its appropriation" and are to "act with prudence and diligence... honestly and faithfully in the best interest of the beneficiary..."*, and to perform any necessary or useful act including "any form of investment". The CCQ presents a list of presumed sound investments, which include federal and provincial bonds, certain common shares, preferred shares, and mutual funds (see article 1339 of CCQ for additional details). If a trustee invests within this legal list, the trustee will be presumed to be acting with prudence and diligence. A trustee may invest outside of the list, but may then need to prove prudence and diligence.

Prudent Investor Approach

All provinces (except Quebec) use some variation of the "prudent investor" rule. Under this rule, a trustee is required to exercise care, skill, diligence and judgment that a "prudent investor" would when making investment decisions. This approach offers more flexibility than the rigid legal list approach in that it permits a greater latitude of investment types.

In certain provinces¹, the general standard of prudent behaviour is further refined in the province's trustee legislation to include a specific list of criteria for a trustee's investment consideration.

For example, under Ontario's Trustee Act, the trustee, in making his or her investment decisions, must consider the following criteria in addition to any other factors that are relevant in the circumstances:

1. general economic conditions;
2. the possible effect of inflation or deflation;
3. the expected tax consequences of investment decisions or strategies;
4. the role that each investment or course of action plays within the overall trust portfolio;
5. the expected total return from income and the appreciation of capital;

¹) Alberta, Newfoundland, Ontario, Prince Edward Island and Saskatchewan

6. needs for liquidity, regularity of income and preservation or appreciation of capital; and
7. an asset's special relationship or special value, if any, to the purposes of the trust or to one or more of the beneficiaries.

Where such statutory criteria are provided, the trustee must carefully consider them in his or her investment selection. A trustee that chooses to disregard these criteria will not be protected from personal liability.

Delegation and Mutual Funds

Historically, the ability of trustees to invest in mutual funds was uncertain. This is because a trustee is prohibited under common law from delegating his or her trust powers. By investing in a mutual fund, the trustee can be viewed as improperly delegating his or her decision-making authority to a mutual fund manager. If a trustee has delegated a duty that he or she should have performed personally, then the trustee may be held liable to beneficiaries for any loss caused by the trustee's reliance on the authority of an agent.

Given today's complex and sophisticated investment market, there has been some recognition by the provincial legislators that there is a need to expand the range of services that may be entrusted to specialists by trustees. Allowing trustees to access mutual funds as an important investment

vehicle has been considered by the legislator. Several provinces² have clarified this matter by providing that mutual funds are permitted investments by the trustees.

Further, a series of provincial statutes even permit the trustee, subject to certain conditions, to delegate his or her investment decision making power to agents. In Ontario or British Columbia, for instance, if a trustee delegates his or her investment power to an agent, there must be a written investment plan or strategy put in place. The investment plan must set out a strategy for the investment of the trust property, comprising reasonable assessments of risk and return which a prudent investor would

have adopted under comparable circumstances. The investment policy must be in the best interest of the beneficiaries of the trust. The trustee must also enter into a written agreement with the agent which requires that the agent comply with the investment plan or policy and report to the trustee at regular stated intervals. The trustee must exercise prudence in his or her selection of an agent, in establishing the terms of an agent's authority, and in monitoring the agent's performance to ensure compliance with applicable terms.

Table 1 summarizes the investment powers of a trustee as set out under the provincial statutes:

Table 1

	Legal List	Prudent Person/ Investor Standard	Mutual Funds	Ability to delegate investment decisions
Alberta		Yes	Yes	Yes
British Columbia		Yes	Yes	Yes
Manitoba		Yes	No ³	No
New Brunswick		Yes	Yes	Yes
N.W.T./Nunavut		Yes	No	No
Nova Scotia		Yes	Yes	Yes
Ontario		Yes	Yes	Yes
Prince Edward Island		Yes	Yes	Yes
Quebec	Yes	No	Yes	Yes
Saskatchewan		Yes	Yes	Yes
Yukon		Yes	No	No

2) Alberta, British Columbia, Nova Scotia, Ontario, Prince Edward Island, Quebec and Saskatchewan

3) Manitoba Trustee Act appears silent on the question.

Trustee's Indemnity

Unless otherwise provided under a trust instrument, a trustee who adheres to the “prudent investor” rule will be relieved from liability resulting from loss to the trust fund. For example, under Ontario legislation, a trustee will not be liable if the investment is consistent with an investment plan or strategy that a prudent investor would have adopted in comparable circumstances. In general, an exemption clause in the trust instrument would not be able to exempt a trustee from gross negligence in the exercise of his power.

Conclusion

A power to invest trust assets by a trustee must be an authorized power, either pursuant to the trust instrument, including a trust agreement or a Will, or the relevant provincial legislation that governs the trust. In making investment decisions, a trustee should act in a reasonable and prudent manner and should take into account the interests of all of the trust's beneficiaries as described under the trust instrument or the statute. In most common law jurisdictions, investment in mutual funds is now permitted and does not necessarily, for the purpose of law, constitute an illegal delegation of investment power by a trustee. Similarly, in most common law provinces, a trustee is now permitted to delegate day-to-day investment decisions to expert agents. In general, a trustee should exercise care in the selection of expert agents, establish the terms and limits of the authority delegated and monitor the agent's activities to ensure compliance with the terms of the delegation. A prudent trustee, particularly one who is not knowledgeable in investment matters, should seek professional investment advice to assist him or her in developing an investment strategy with respect to trust property.

› Please contact us for more information.

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