

## **F3:2.1: CERTAINTY OF OBJECTS & DISCRETIONARY TRUSTS**

### 1. Introduction: The Purpose of the Certainty of Objects Requirement

- For a Trust to exist, A must: (i) hold a specific claim-right or power; and (ii) be under a duty to B not to use that claim-right or power for A's own benefit (unless and to the extent that A is also a beneficiary of the Trust). In other words, for a Trust to exist, A must be under the core Trust duty.

The **certainty requirements** for a Trust simply reflect the fact that A must be under a duty to B in relation to a specific right. The **certainty of objects** requirement ensures that: (i) A owes a duty to a specific person; and (ii) A's duty is certain enough to be enforced.

The certainty of objects requirement can sometimes be seen as an inconvenient obstacle that can trip up a party (A0) trying to set up a Trust. However, it serves a vital purpose: a court cannot enforce a duty unless that duty is adequately defined. This point is not peculiar to Trusts. For example, an agreement between A and B can only impose a contractual duty on A to B if it satisfies a certainty test: the nature of A's duty to B must be adequately defined.<sup>1</sup>

In understanding the certainty of objects requirement, it is important to ask *what information the court needs* in order to enforce A's supposed duty to B. If that information is lacking, A's supposed duty cannot be enforced; so A will be under no duty to B; so there can be no Trust.

### 2. Discretionary Trusts

- A discretionary Trust is a form of Trust (see p 222-4 of the book): it can exist only if A is under the core Trust duty.

**Example 1a:** A0 transfers £100,000 to A subject to a duty: (i) not to use that money for A's own benefit; and (ii) to invest the money prudently; and (iii) at the end of 21 years, to pay any unspent part of the £100,000 and its income to Oxfam. A0 also stipulates that, during that 21 years, A can, if he wishes, pay all or any of the £100,000 and its income to all or any of A0's children or grandchildren.

In such a case, there is clearly a Trust: A is under the core Trust duty. And Oxfam is a beneficiary of that Trust: A owes the core Trust duty to Oxfam. A0's children and grandchildren are *not*, however, beneficiaries of a Trust: A does not owe them the core Trust duty. Rather, A has a power: A can, *if he wishes*, give all or any of the money to all or any of A0's children and grandchildren.

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<sup>1</sup> See eg *G Scammell & Nephew Ltd v Ouston* [1941] AC 251.

- A discretionary Trust is a particular form of Trust: it exists where A, in addition to being under the core Trust duty, has a power to choose how to distribute the benefit of the right A holds on Trust.

**Example 1b:** A0 transfers £100,000 to A subject to a duty: (i) not to use that money for A's own benefit; and (ii) to pay the money, in equal shares, to all of A0's children and grandchildren.

In such a case, there is clearly a Trust: A is under the core Trust duty. There is no discretionary Trust: A does not have a power to choose how to distribute the benefit of the £100,000. Rather, there is a **fixed Trust**: A is under a duty to distribute the benefit of the right held on Trust in a specific way.

**Example 1c:** A0 transfers £100,000 to A subject to a duty: (i) not to use that money for A's own benefit; and (ii) to invest the money prudently; and (iii) by the end of 21 years, to have distributed that £100,000 and its income, as A sees fit, amongst all or any of A0's children or grandchildren.

In such a case, there is a discretionary Trust. A does owe the core Trust duty to A0's children and grandchildren; but A has a power to choose how to distribute the benefit of the £100,000.

### 3. Discretionary Trusts & Certainty of Objects: The "Any Given Person" Test

**Example 2:** A0 transfers £100,000 to A subject to a duty: (i) not to use that money for A's own benefit; and (ii) to invest the money prudently; and (iii) by the end of 21 years, to have distributed that £100,000 and its income, as A sees fit, amongst all or any of A0's relatives.

In **Example 2**, there seems to be a problem. A0 has attempted to set up a discretionary Trust. However, such a Trust depends on A being under a duty not to pay any of the money to a person who is *not* a relative of A0. But can a court enforce that duty? For example, let's say A chooses to pay out £5,000 to X. Is there a meaningful test the court can use to decide if X really is a relative of A0? If not, a key part of A's intended duty cannot be enforced; in that case, the intended discretionary Trust cannot exist. And, if that occurs, A will hold the £100,000 on Resulting Trust for A0 (or, if A0 has died, for A0's estate).

We can sum up this point by saying that, for a discretionary Trust to exist, it must pass the "any given person" test: a court must be able to tell of any given person (eg X) whether or not that person falls within the class of those to whom A is permitted to distribute the benefit of the right A holds on Trust.<sup>2</sup> That "any given person" test is often referred to as the "given postulant" test. In *re Baden (No 2)*,<sup>3</sup> the Court of Appeal considered whether a discretionary Trust for A0's relatives could pass that test.

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<sup>2</sup> See *per* Lord Wilberforce in *McPhail v Doulton* [1971] AC 424 at 456.

<sup>3</sup> [1973] Ch 9.

Stamp LJ held that the discretionary Trust was valid. His Lordship reached that conclusion by taking a very narrow view of relatives as including only A0's statutory next of kin (ie those close relatives specified by statute as being able to acquire A0's rights if A0 dies without making a valid will).<sup>4</sup> Sachs and Megaw LJJ took a much broader approach to the term "relative", defining it as anyone sharing an ancestor with A0.<sup>5</sup> That definition seems to cause a problem: if X claims that he and A0 had the same great-great-great-great-great grandmother, can the court really test that claim? Sachs and Megaw LJJ both dealt with that point by saying that the onus is on X to prove that claim; until X does so, it must be assumed that X does *not* share an ancestor with A0.<sup>6</sup>

The approach of Sachs and Megaw LJJ (assuming X is out of the permitted class, unless and until X can show otherwise) seems to make the "any given person" test redundant. For example, if A0 tries to set up a discretionary Trust in which A has a power to distribute the benefit of a right to anyone who is a "good person", we might expect A0's attempt to fail: there is no way for a court to tell if X is or is not a "good person". However, on the approach of Sachs and Megaw LJJ, we could instead say that the discretionary Trust is valid – it is just that, if X cannot prove he is a "good person", it will be assumed that he is not such a person.

It seems that neither Sachs LJ nor Megaw LJ wanted to leave the law in such a way as to permit there to be a discretionary Trust in favour of anyone who is a "good person". So each judge added a further certainty requirement. Sachs LJ stated that the class of those to whom A can distribute the benefit of A's right must be "conceptually certain": that is, it must be possible to come up with a definition of the class.<sup>7</sup> Practical, evidential problems as to whether X is or is not within that definition can be dealt with by applying the simple rule that X is out of the class until he proves otherwise. So the "good person" discretionary Trust will be invalid as there is no clear way of defining that term: it is *conceptually* uncertain. In contrast, whilst it may be difficult, or even impossible, to tell if X is or is not a relative of A0, that *evidential* uncertainty will not defeat the discretionary Trust.

Megaw LJ added a different requirement, stating that a discretionary Trust can only be valid if there are a "substantial number" of people who are clearly within the class to whom A can distribute the benefit of A's right.<sup>8</sup> Again, that requirement can be used to mean that a "good person" discretionary Trust is invalid, whereas a "relatives" discretionary Trust is not.

The extra requirements imposed by Sachs and Megaw LJJ do not assist in fulfilling the purpose of the "any given person" test: making sure the court can tell if A distributes the benefit of the right to a person outside the permitted class. It may be that each requirement instead aims to ensure that the discretionary Trust makes some practical

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<sup>4</sup> [1973] Ch 9 at 28-29.

<sup>5</sup> *Ibid* at 21-22 (following the lead of the first instance judge, Brightman J).

<sup>6</sup> Here, again, the lead of Brightman J was followed.

<sup>7</sup> *Ibid* at 20.

<sup>8</sup> *Ibid* at 24.

sense: for example, if it is not possible to give a conceptually certain definition to the class, it may well be that *no-one* can show he is within that class. Megaw LJ's requirement for a "substantial number" to be within the class is of course quite vague: the point seems to be that, for a discretionary Trust to make sense, A must have a genuine choice to make as to who will receive the benefit of A's right. However, that point is not always correct: for example, the discretion in a discretionary Trust could come from A having a power to decide *how much* of the benefit of A's right a particular individual should receive.

#### 4. Discretionary Trusts & Certainty of Objects: Further Tests

##### 4.1 The "full list" test?

At one point, it was suggested that a discretionary trust could be valid only if the court could draw up a full list of the people to whom A is permitted to distribute the benefit of a right. On that view, in **Example 2**, a discretionary trust would arise only if it is possible to draw up a full list of A0's relatives. However, in *McPhail v Doulton*, the House of Lords rejected that view.<sup>9</sup> It was based on the idea that, if A failed in his duty to distribute the benefit of the right, a court would have to step in and decide how to distribute. And, to avoid favouring any one person, the court would have to order equal division of the benefit of the right amongst *all* members of the class. On that view, a discretionary trust would become, in effect, like the fixed Trust in **Example 1b**: so a full list would be necessary.

In *McPhail v Doulton*, Lord Wilberforce pointed out that, if A fails in his duty to distribute the benefit of a right, a court does *not* have to order equal division.<sup>10</sup> After all, such equal division could be one of the worst ways of distributing the benefit of a right: for example, splitting up a fund of £100,000 equally among 1,000 people would mean that no one person gains a substantial benefit from the discretionary trust. So, given the other means by which the court can step in to execute a discretionary trust, there is no need to apply the "full list" test.

##### 4.2 The "administrative workability" test

The fact that a court may need to step in and execute a discretionary trust does *not* mean that a discretionary trust must pass the "full list" test. Nonetheless, it may have some impact. For example, if the terms of the attempted discretionary trust mean that there is *no* sensible plan a court could adopt to execute that supposed trust, then A0's attempt to set up a discretionary trust must fail. This point may explain the (rarely relevant) "administrative workability" test.<sup>11</sup>

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<sup>9</sup> [1971] AC 424.

<sup>10</sup> *Ibid* at 456-7.

<sup>11</sup> That test is referred to by Lord Wilberforce in *McPhail v Doulton*: [1971] 1 AC 424 at 457.

For example, in one case,<sup>12</sup> A0 (a council shortly to disappear as part of a re-organisation) attempted to set up a discretionary trust (of a large sum of money) for the benefit of all the former residents of the area covered by that council. The class of people to whom A could distribute the benefit of its right would thus include over 2 million people. It was found that the council's attempt to set up a discretionary Trust failed: the planned Trust was "administratively unworkable". The problem here may be that, if A fails to perform his duty to distribute, the court will have to step in. And is there any sensible way order a court could make to distribute the benefit of A's right? We have to bear in mind the need for a court to avoid making the type of contentious political decision which it is ill-suited to make and which may cause resentment.<sup>13</sup> Of course, in most cases, no such problems arise: the "administrative workability" test rarely prevents an intended discretionary trust from arising.

This explanation of the "administrative workability" test explains why it applies to discretionary trusts but not to attempts to give A a power (as in **Example 1a**). If A chooses not to exercise a power to distribute the benefit of a right then, as A is under no duty to do so, a court does not need to step in and order some form of distribution. There is thus no risk of a court facing the dilemma that would arise if an administratively unworkable discretionary trust were allowed to be valid.

#### 4.3 The "non-capricious" test

Although the "administrative workability" test does not apply to powers, that does not mean that powers are free from certainty tests. For example if A has a power to distribute the benefit of a right to all or any of a certain class of people then, as is the case with a discretionary trust, A is under a duty not to distribute outside that class. So, with a power as with a discretionary trust, the "any given person" test applies:<sup>14</sup> the power is only valid if a court can tell, should A exercise the power in favour of X, whether or not X is in the permitted class.

Sometimes, when accepting a power, A also comes under a duty to act loyally and responsibly when considering whether to exercise that power. In such a case, for example, A (as is the case if A holds a right on a discretionary trust) cannot simply ignore the power: he is under a duty to members of the class of potential recipients to consider periodically whether or not to exercise the power.<sup>15</sup> In these cases, A can be said to have a "fiduciary power": A is not just under the negative duty not to distribute outside the permitted class; he also has some positive duties in relation to the power.

It has been held that A0's attempt to set up such a power will fail if the intended power is "capricious": if there are no sensible criteria A can apply in considering whether and how

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<sup>12</sup> *R v District Auditor, ex p West Yorkshire MCC* [1986] RVR 24 (noted by Harpum [1986] CLJ 391).

<sup>13</sup> For example, would the money be better spent on paying for a new school, or a new hospital, or new sports facilities?

<sup>14</sup> See eg *re Gulbenkian* [1970] AC 508.

<sup>15</sup> For a discussion of A's duties in such a case see eg *per Megarry V-C in re Hay* [1982] 1 WLR 202, esp at 210.

to exercise his power.<sup>16</sup> This does not mean that, when giving A the intended fiduciary power, A0 needs to spell out what factors A should take into account. However, it does mean that if the supposed power is “capricious” (ie there is no sensible scheme A can come up with) then A0’s attempt to give A the power must fail.

Two points are worth noting about this “non-capricious” test. First, if it is linked to A0’s attempt to impose a duty on A to act loyally and responsibly when considering whether to exercise a power, it must apply to an attempt to set up a discretionary trust: such a duty is a key part of a discretionary trust. Second, in practice, it is very unlikely that this test will present a problem: people rarely go round setting up bizarre powers that cannot be considered in a sensible way.

#### 4.4 The “one person” test

**Example 3:** A0, an owner of a large number of paintings, dies. In his will, he instructs A (his executor) to allow “each of my friends” to purchase one of those paintings each, at half its market value.

In such a case, A0 does *not* attempt to set up a discretionary Trust: A has no power to choose how to distribute his rights. Rather, each friend of A has a fixed entitlement. A0 is attempting to make a *conditional gift*: if X satisfies a particular condition (if he is a friend of A0) he has a specific right. Nonetheless, it may seem that there is still a certainty problem: how can A (or the court) tell if X is or is not a friend of A0?

However, in *re Barlow*, the essential facts of which were identical to **Example 3**,<sup>17</sup> Browne-Wilkinson J held that the conditional gift was valid. His Lordship noted that an attempt to set up a discretionary Trust for “friends of A0” would fail: applying Sachs LJ’s test in *re Baden (No 2)*, the term “friends of A0” is conceptually uncertain. However, a conditional gift should be treated differently: if there was just one person who could clearly show he was, on any reasonable test, a friend of A0, that person is entitled to acquire one of the paintings.<sup>18</sup>

The test applied in *re Barlow* has been criticised.<sup>19</sup> However, it can be defended. If an attempted discretionary Trust (eg in favour of “friends of A0”) fails a certainty test, then someone who could have benefitted from A’s power (eg a clear friend of A0) will miss out. But, in any case, that person only had a *chance* of receiving a benefit; he had no legal guarantee. In contrast, if a conditional gift is found to be invalid when there is a person who definitely stands to benefit from it, that person is deprived of a definite entitlement: a right given to him by A0. To avoid that deprivation, the conditional gift must be valid as long as one person clearly falls within the class of intended recipients.

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<sup>16</sup> See *re Manisty* [1974] Ch 17, esp *per* Templeman J at 27.

<sup>17</sup> In *re Barlow*, any friend of A0 was permitted to buy a painting at a valuation given to it in 1970: A0 died in 1975 and the paintings had increased in value since 1970

<sup>18</sup> See too *re Allen* [1953] Ch 810.

<sup>19</sup> See eg McKay [1980] Conv 263; Emery (1982) 98 LQR 551.