Trustee Powers of Advancement

In this month’s CPD paper we will take a detailed look at the powers given to trustees in relation to trust capital under 32 of the Trustee Act 1925. This power is known as the statutory power of advancement and is an important part of the administration of a trust, whether created in lifetime or on death. An understanding of how this power works is integral to understand when drafting trusts.

# Overview

The statutory power of advancement is provided by section 32 TA 1925. This gives trustees powers to apply capital to or for the benefit of a beneficiary of a trust. This paper will only consider the power of advancement as it applies to trusts created after 1 October 2014.

Drafters also need to be aware of the statutory power of maintenance. This is provided by section 31 TA 1925. This gives trustees various powers over income, including powers to accumulate income or pay income to a beneficiary. This power will be examined separately in a future CPD paper.

# When does section 32 apply?

Section 32 applies to all trusts unless it is expressly excluded by a clause in the trust deed. This power allows trustees to pay or apply capital for the ‘advancement or benefit’ of any person who has a vested or contingent interest in the capital of a trust fund.

Previously, this power could only be used to advance up to one-half of a beneficiary’s interest. This was so frequently modified by draftsmen to allow the trustees to advance a beneficiary’s full entitlement that the Inheritance and Trustees’ Powers Act 2014 amended section 32 to remove this limit. You should note that the STEP Provisions (2nd edition) commonly incorporated into wills still refer to the previous section 32 and modifies it to remove the ‘one-half’ limitation. This is nothing to worry about as it just mirrors the statute.

As section 32 applies to beneficiaries with an interest or a presumptive interest in capital it will apply where someone has a vested interest, as well as someone who has an interest that is contingent on some event, commonly an age condition. Section 32 also applies where a beneficiary has a remainder interest, or where their interest could be reduced if further beneficiaries could be added to the class. An advancement is even acceptable where the beneficiary’s interest could be defeated entirely, for example because they never reach the age contingency.

Section 32 does not apply to a discretionary trust. In these types of trust the beneficiaries do not have an interest in the capital, only a *spes* (mere hope) of obtaining an interest. The trustees have a power of appointment and may choose to exercise their discretion in a beneficiary’s favour to benefit them.

The power of advancement does not apply to a life tenant of an interest in possession trust who only has an interest in the income. If they are given a separate interest in capital, then the trustees could make advancements in their favour; it is more common to include a power of appointment instead allowing the trustees to appoint capital to the life tenant at their discretion without giving them an interest in the capital.

It is important to note that the power of advancement is a discretionary power. It is totally up to the trustee’s own discretion whether they make an advancement or not, or what terms they make it on within the bounds of what the law allows. No beneficiary can compel the trustees to exercise this power in their favour.

The trustees may use the power to apply either money or other trust assets. This was clarified by the Inheritance Trustees’ Powers Act 2014 as this changed the wording to refer to capital money or any other property forming part of the trust fund. Prior to 1 October 2014 section 32 only referred to capital money. While case law already suggested that it was acceptable for the trustees to advance other trust assets this amendment gave this a clear statutory basis.

# Advancement or Benefit

**What is an advancement?**

 The trustees can advance capital for a beneficiary’s advancement or benefit. The term ‘advancement’ refers to both the act of bringing something forward, in this case the beneficiary’s entitlement to capital, as well as the act of somehow advancing the beneficiary’s position.

Originally this meant a distribution that was advancing the beneficiary in life in some way, or helping them take a significant step in life, for example by providing the funds for them to purchase a home, pursue an education or set up a business. The term ‘advancement’ is now thought to have a much wider meaning that this. In the case of *Pilkington v IRC* [1964] AC 612, the leading case on advancement, Lord Radcliffe described an advancement as ‘any use of the money which will improve the material situation of the beneficiary.

In the same case it was also said that an advancement doesn’t necessarily carry its ordinary meaning of paying something forward. In a lot of cases section 32 will be used to bring forward a person’s entitlement, however it is also possible to use the power to make a settled advance which actually defers the beneficiary’s entitlement to capital. An example of this in practice would be where a beneficiary has a contingent interest in capital and the trustees exercise their power of advancement to make a settled advance deferring the vesting date.

Example 1: Terry died leaving a share of his estate on a bereaved minor’s trust for his son Carl, so his interest will become vested at 18. When Carl is 17 the trustees consider that it would be beneficial to him if his interest was deferred until 25. Using their powers under section 32 they can make a settled advance to defer Carl’s entitlement to his 25th birthday instead.

**What do we mean by benefit?**

The second part of the power refers to its use for the beneficiary’s benefit. The words ‘or benefit’ were often added to trusts because the meaning of ‘advancement’ was originally thought to be quite narrow, as discussed above. Again, we have Lord Radcliffe to thank for his definition of ‘benefit’ as ‘any use of the money which will improve the material situation of the beneficiary’. This makes it a very wide power and has led to a wide range of advancements being allowed on the basis that they are of benefit to the beneficiary. Some notable uses are:

* To discharge the beneficiary’s debts (*Lowther v Bentinck* (1874) LR 19 Eq 166)
* To save tax (*IRC v Pilkington*)
* Paying maintenance (*Re Breeds’ Will* (1875) 1 Ch D 226)
* Making a payment to a charity to discharge a moral obligation felt by a wealthy beneficiary (*Re Clore’s Settlement Trusts* [1966] 1 WLR 955).

The widest possible use of the power is to provide a benefit to a beneficiary’s family, which in turn is a benefit to the beneficiary as it relieves them of a duty to make their own provision. In the case of *Re Hampden’s Settlement Trusts* [1977] TR 177 the courts provided a summary of previously decided cases on the use of the section 32 power to benefit a beneficiary. It can be broken down into three aspects allowing a trustee to apply capital in any way that:

a) viewed objectively, can be fairly regarded as being for the benefit of the beneficiary concerned.

b) viewed subjectively, they believe to be for the beneficiary’s benefit.

c) does not need to be a direct financial advantage to the beneficiary. It may be that they are benefited by provision for a near relation that relieves him of a moral responsibility.

It is important that the trustees consider the benefit objectively and subjectively. What could be subjectively considered a benefit to the beneficiary may not be viewed similarly objectively. Each case will turn on its own facts. For an example of this see the contrast between *Re Clore’s Settlement Trusts* and *X v A* (discussed below).

In *Re Hampden’s Settlement Trusts* the advance in question was a settled advance for the beneficiary’s own children. This was held to be acceptable and for the beneficiary’s benefit as it ‘relieved him of the considerable obligation in respect of making provision for their future’ that he would otherwise have owed to his children.

Example 2: Mary is the beneficiary of a trust giving her an interest in a share of her deceased parents estate contingent on her attaining the age of 25. She is currently 23 and has two young children who she is concerned about providing for. The trustees can exercise their powers under section 32 to advance funds to a settlement for Mary’s children.

# Limitations

The main limitation to be aware of is that the trustees may only exercise the section 32 power to advance up to the beneficiaries vested or presumptive share. So, each beneficiary will be treated fairly.

**Limitation on Benefit**

We saw in *Re Clore’s Settlement Trusts* that the power of advancement may be used to provide funds to a charity to discharge the beneficiary’s moral obligations. A limitation on the use of the power in this way is that the amount advanced cannot be excessive, baring in mind the size of the fund and the beneficiary’s own resources.

In the later case of *X v A* [2005] EWCH 2706 (Ch) a beneficiary with a life interest and an opposition to inherited wealth wished the trustees to advance the entire fund to charitable causes. The courts refused to direct that this would be an advance for the beneficiary in question’s benefit as it far exceeded the resources the beneficiary had available herself so could not relieve her of any obligation, she felt that she would otherwise need to discharge out of her own resources. They also found that there was no indication that even doing so would relieve her of the moral obligation she felt.

When varying the terms of a trust using the powers of advancement to defer entitlement there must be some justifiable reason that the trustees see the deferral to benefit the beneficiary. This must be based on actual facts, and may concern the personal circumstances of the beneficiary, the size of the trust fund, tax implications, or actual characteristics of the beneficiary such as disability.

This was demonstrated in the case of *Wright v Gater* [2011] EWHC 2882 (Ch). In this case consent was not granted to vary the terms of a trust to defer a beneficiary’s entitlement from 18 to 30. The beneficiary in question was 3 at the time, and there was no indication that the beneficiary would be incapable of managing his inheritance at the age of 18, so it could not be argued that an advance in this form would be for his benefit. If the trustees could have demonstrated that the beneficiary was likely to be unable to manage his inheritance without support, for example if it was known he had a mental disability, then it is likely that the advance would have been valid.

**Consent**

If there is a beneficiary with a prior interest in the trust fund, then they must give their consent for the trustees to make an advancement. This is because the advancement of capital to a remainder beneficiary would reduce the benefit that the beneficiary with the prior interest would receive. Only a beneficiary who is over 18 and has mental capacity can consent.

 Example 3: Johnathan is the life tenant of an Interest in Possession trust. He is entitled to receive all trust income as it arises. The trustees wish to use their power of advancement to advance funds to a remainder beneficiary. John must provide his consent to this as this will reduce the capital that is available to generate income for him.

The beneficiary receiving the advance in their favour does not need to consent to the advancement, even if the result of the advancement is to defer their entitlement to a later date. This allows the trustees to make advancements for the benefit of minors or beneficiaries lacking capacity.

**Bringing Advances into Account**

Also referred to as bringing advances into hotchpot. If the trustees exercise their power of advancement, then the amount advanced to a beneficiary must be brought into account when the beneficiary later becomes entitled to their share in the trust fund. The value brought into account will be the value of the advance at the date the advance was made, although the trustees can bring an advance into account on the basis of it representing a proportionate share of the beneficiary’s interest. The trustees should be clear on this point when making an advance.

While this has always been the case, the Inheritance Trustees’ Powers Act 2014 made this clear by inserting subsection 1A into section 32 TA 1925:

In exercise of the foregoing power trustees may pay, transfer or apply money or other property on the basis (express or implied) that it shall be treated as a proportionate part of the capital out of which it was paid, transferred or applied, for the purpose of bringing it into account in accordance with proviso (b) to subsection (1) of this section

Trustees may wish to bring advancements into account on a proportionate basis rather than a nominal one as calculating distribution on a nominal basis can lead to a beneficiary who has already received an advancement taking a disproportionate benefit if the fund increases in value between the date of the advancement and the date of distribution.

This amendment applies to all trusts whenever created.

 **Limitations on Settled Advances**

It is suggested that it is not possible for trustees to use the section 32 powers to advance assets to an immediate discretionary trust for the beneficiary. Although there is no logical reason that it would not be possible considering how wide the scope of ‘benefit’ is, there is a danger that a trustee would be found to have acted in breach of trust if they relied upon the power of advancement to create a discretionary trust. The argument against this use of the power was presented in d in short, stated that it went against the principal of *delegatus non potest delegare* (that a person to who power is delegated to cannot themselves delegate that power).

A trustee cannot rely on section 32 to advance to discretionary trusts, but if the trust itself gives them authority to do so it is fine, as long as it is for the beneficiary’s benefit of course. To avoid doubt and potential conflict may draftsmen opt to include an express power for the trustees to advance to discretionary trusts for one or more of the beneficiaries.

# When to apply, exclude or modify

Although the statutory power of advancement will apply to trusts automatically if it has not been expressly excluded it is still helpful to make it clear that it applies by including a statement in the will or trust.

It should be excluded if the trust contains express powers that conflict with section 32.

It is also possible to make minor modifications to the statutory power. The power can be amended to remove the requirement for trustees to bring any advancements into account when calculating a beneficiary’s share in the fund. It can also be amended to remove the requirement for a beneficiary with a prior interest to consent to an advancement.

# Conclusion

Trustees have many options available to them when considering how to provide for beneficiaries. The statutory powers of advancement grant a trustee a great degree of flexibility, but there is still much to consider when deciding whether an advancement can be made, how it should be made, and how it will then affect the beneficiary’s entitlement if or when they become absolutely entitled to their share of the trust fund. This paper has only examined one of the trustee’s major statutory powers.

**Important Reminder:**

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