Addressing the Requirement to Consider Tax Consequences Under the Prudent Investor Rules

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DUTY

At this point it is useful to foreshadow the recommendation we are going to make in the succeeding section on trustee liability. In order to fix a trustee with liability for a loss, it will be necessary to do more than show that the trustee has failed to take account of some factor that they should have taken into account. It will be necessary to show that their failure to take account of the factor has led them to take an investment approach that a prudent trustee would not have adopted under comparable circumstances. If, for example, a trustee's investment approach was determined without paying any ***overt attention to the impact of taxation***, this could lead to the trustee being held liable for a loss to the trust. ***But the trustee will only be liable if it is established that their failure to take account of taxation led them to an investment approach that a trustee who did pay due regard to this matter would not have taken***.[1] [emphasis added]

Therefore, where a trustee's investment conduct is called into question, the appropriate question is not whether another trustee applying the standards of prudent investment could have realized higher returns than were actually realized. The question should be whether a reasonably skilled and prudent trustee applying the standards of prudent investment in the circumstances actually faced by the trustee could have invested in the manner that the trustee actually invested.[2]

A trustee is not liable for a loss in connection with the investment of trust funds that arises from a decision or course of action that a trustee exercising reasonable skill and prudence and complying with section 3 could reasonably have made or adopted.[3]

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1 "*Trustee Investment Powers*" Report No. 80, Alberta Law Reform Institute, February 2000 ("**Report**"), page 63.

2 *Ibid*, page 72.

3 ***Trustee Act***, R.S.A. 2000, c. T-8 ("***Trustee Act***"), section 4(1). Unless otherwise expressly noted, all references to specific legislative provisions are references to provisions of the ***Trustee Act***.

Sections 2 through 8 of the ***Trustee Act***, referred to in this paper as "**Alberta's Prudent Investor Rules**" or the "**APIR**" and forming Appendix "A" hereto, provide trustees with guidance regarding the selection, monitoring and rebalancing of investments under administration. One of the requirements of the APIR is to consider the tax consequences of potential investment decisions. This paper:

1. describes the APIR;
2. discusses that portion of the APIR which requires a trustee to consider tax consequences in respect of an investment approach; and
3. proposes an approach which practitioners and their trustee - clients might find useful in discharging their responsibility to consider such tax consequences.

Why must lawyers advising trustees be concerned with these matters? In addition to the observation that failure to properly advise a trustee - client in respect of a statutory obligation may rise to the level of negligence, there is a less obvious basis for concern. That concern relates to a lawyer's potential liability for breach of trust, when a trustee - client commits a breach of trust.[4]

The de Vries article discusses the Supreme Court of Canada decision in ***Citadel General Insurance Co.*** v. ***Lloyd's Bank of Canada*** [1997] 3. S.C.R. 805. The essence of de Vries' argument is that:

1. a "stranger" to a trust, such as the solicitor for the trustee, who merely acts as agent of a trustee, is not liable for his client's breach of trust; and
2. this decision stands for the proposition that a "knowing assister" in the trustee's breach of trust may be liable as a constructive trustee for breach of trust.

As de Vries notes on page 7 of the de Vries article:

> A *knowing assister* is a stranger to the trust who, with knowledge, assists the trustee in the trustee's dishonest and fraudulent breach of trust. It is anxiomatic that a knowing assiter will be liable to the beneficiaries for losses sustained and/or profits made. The knowledge requirement of the knowing assister can

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4 For an excellent discussion of the basis for this exposure, see "*Representing the Estate Trustee - What to Know and What to Avoid*" de Vries, Justin W., OBA Annual Institute 2010 Trusts and Estate Law ("**de Vries article**"). See also the decision of the British Columbia Supreme Court in ***Winslow*** v. ***Richter and Munro Crawford*** 39 B.C.L.R. (2d) 83, where the Court noted at paragraph 34 that, "I conclude that in Canada honest negligence will not serve to render a solicitor, who acts as agent of a trustee, liable as a constructive trustee if, by reason thereof, he unwittingly assists in a breach of trust but willful blindness or actual knowledge will".