

# TRUSTEE LIABILITY: WHEN WILL A TRUSTEE BE EXCUSED?

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## INTRODUCTION

When errors by a trustee cause losses to a trust, the question arises as to who should be forced to bear the weight of those losses: the beneficiaries or the trustees? On the one hand, it seems unfair that a beneficiary should lose because of the mistakes of someone who is in charge of administering the trust. On the other, there are obvious policy reasons for not wanting to make a trustee liable – if potential trustees believed they could be held liable for any mistake they made, would anyone be willing to accept their appointment?

The general rule is that when a trustee breaches his duty, he will be liable to the beneficiaries for any losses that occur as a result of that breach.<sup>1</sup> However, as a way of balancing the rights of beneficiaries with the interest to not overburden trustees, s. 35 of the *Trustee Act*<sup>2</sup> holds that when a breach of trust occurs, the court has the discretion to relieve the trustee of liability in cases where it believes that she has acted “honestly and reasonably and ought fairly to be excused.” When there are multiple trustees and the court believes that not all of them should be held liable for a breach of trust, it has the discretion to exempt the “innocent” trustee(s) from liability, thus departing from the general rule that trustees are jointly and severally liable for their acts or omissions. The effect of relieving a trustee from his or her breach of trust is that any losses that are sustained must be borne by the beneficiaries.

In situations where a breach of trust has occurred and the court refuses relief, then the trustee will generally be required to compensate the beneficiaries for the losses they suffered. If

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<sup>1</sup> See, for example, *Trusts & Guarantee Co. v. Brenner*, [1933] S.C.R. 656 (SCC).

<sup>2</sup> R.S.O. 1990, Ch. T. 23, *as amended*.

the finding occurs in the context of a civil action brought by a beneficiary, then a trustee can be held liable for damages in the usual way. If the finding occurs in the context of a passing of accounts, the court will usually deny or decrease the amount of compensation to which the trustee would otherwise be entitled. The court also has the additional, but infrequently used, option of ordering the trustee to reimburse the estate any losses that have occurred because of the breach of trust.

## **DUTIES OF A TRUSTEE**

There are five basic duties that a trustee, as a fiduciary, owes to the trust:

- The duty to obey the directions set out in the trust instrument, unless changes are authorized by the beneficiaries or the court;
- The duty to act impartially toward beneficiaries;
- The duty to exercise ordinary care and prudence;
- The duty to be loyal to the trust, including not profiting from its administration or allowing a conflict of interest to affect the decisions made in respect of it; and
- The duty to maintain and put forward accounts in respect of the trustee's financial dealings with the trust.<sup>3</sup>

These basic duties tend to be absolute and cannot be avoided by the terms of the trust instrument. However, the trust instrument can, and frequently does, impose additional obligations on the trustee in respect of the appropriate administration of the trust. The two powers most frequently described in trust instruments are the power to retain and the power to convert the trust's assets. The type of authority and the degree of discretion imposed on a trustee by the trust document can

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<sup>3</sup> Margaret O'Sullivan, "Breach of Trust and Its Consequences" in *Widdified on Executors and Trustees*, 6th ed. (Toronto: Carswell, 2002).

have important implications in situations where a trustee is being required to account for her actions. When considering whether that trustee has fulfilled or failed to fulfill her obligations, the court will inevitably examine the powers conferred on the trustee in the trust instrument. As such, it is essential that a trustee understand the scope of her powers, especially to either convert or postpone the conversion of the assets. In the event that a trustee fails to discharge her obligations or discharges them in an improper way and this failure results in the loss of estate assets, the trustee may be found liable to the beneficiaries of the trust for the damage caused and required to compensate them for the loss.

It is important to note that when the beneficiaries have a claim, they are generally limited to bringing it against the trustees, either in the course of objecting to the trustee's actions at a passing of accounts or else bringing a separate action for breach of fiduciary duty. Beneficiaries owe no duty of care to each other and, in the event a beneficiary (and non-executor) wastes trust assets, the harmed beneficiaries will not be able to name him or her as defendants in a claim. In the event a beneficiary wastes trust assets, the trustees will have a claim against them and the harmed beneficiaries will have a claim against the trustees.<sup>4</sup>

## **TRUSTEE LIABILITY**

With reference to the duties a trustee owes as a fiduciary, a breach of trust will occur any time the trustee fails to carry out the obligations he owes under either the directions in the trust instrument, the rules set out at common law, or the statutory authority in the province the trust

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<sup>4</sup> *Larsen v. Larsen*, [2004] B.C.J. No. 399 (B.C.S.C.).

instrument was executed.<sup>5</sup> If the trustee breaches any of those duties, he will generally be liable to the trust for any losses that occur and can be required to place the trust in the same position that it would have been in had no breach occurred.

Trustees have the obligation to act strictly within the parameters set out by the trust document. When this does not occur, the trustee is described as being in “breach of trust”. As a result, he can be found liable to the beneficiaries for any loss that has occurred. Because a finding of breach of trust rests on what the trustee did or did not do, it does not matter if he had no intention to depart from his obligations.

When trustees act together in discharging their duties and a breach of trust occurs, they will be held jointly and severally liable to the beneficiaries for any losses arising out of the breach. Providing that all the trustees have been found in breach of trust, the beneficiaries will be able to sue one trustee for the entire loss, or all of the trustees. Further, if a beneficiary does not sue all the trustees and is only able to recover part of her loss, then it is open to her to sue other trustees in order to recover the rest of it.

This standard of strict liability can be overly harsh in the consequences that are imposed on trustees and has the effect of making them provide absolute security for the trust. As a result, the important concept of a “technical breach of trust” has emerged, predicated on the belief that when a trustee has acted honestly and with reasonable prudence, compelling her to compensate beneficiaries for losses resulting from a breach of trust would be inequitable. In cases such as this, even if the trustee has acted outside the parameters of the trust document, courts will often decline to find that a breach of trust has occurred at all.

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<sup>5</sup> *Waters' Law of Trusts in Canada*, 3<sup>rd</sup> ed. (Toronto: Thomson Canada Limited, 2005) [*Waters*].

This was the result in the Ontario Court of Appeal's in *Dover v. Denne*.<sup>6</sup> In this case, the testator named three estate trustees and devised his estate to them in trust. In his Will, the testator specifically requested that the trustee, who was a solicitor, be permitted to receive compensation in the same way as he would if he were managing and administering the estate professionally, rather than as a trustee. Mr. Denne, another of the estate trustees, had been told by the testator that the solicitor-trustee would be responsible for managing the estate, and it was on the basis of this information that Mr. Denne consented to the appointment. Upon the death of the solicitor-trustee, it was discovered that he had misappropriated money from the estate.

In dealing with the question of liability on the part of Mr. Denne, the Court pointed out that trustees are not permitted to excuse their conduct by saying that the only reason they assumed their role is because they were not expected to do anything. If a trustee is not willing or able to fulfill her obligations, then she should decline the appointment. However, in respect of Mr. Denne's liability, the court found that during the testator's lifetime, he had always made it clear that he trusted the solicitor and that the solicitor was someone who was believed by others to be someone of honesty and integrity. On that basis, the court concluded that while Mr. Denne could not use his belief he did not have to actively participate in the administration of the estate as an excuse, he had acted honestly and reasonably when he relied on the solicitor-trustee to manage the trust and as such he could not be held responsible for any misappropriation of funds.

## **PROTECTION FROM LIABILITY**

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<sup>6</sup> [1902] O.J. No. 217 (Ont. C.A.) [*Dover*].

Once a breach of trust has been established, beneficiaries are usually entitled to be compensated by the trustee for the loss the trust incurred because of the breach. The exception will be when the trustee can convince the court that he should be excused for any breach that has occurred. There are three basic defences that are open to trustees seeking to have a breach excused:<sup>7</sup>

1. The beneficiary was a party to the breach by either instigating it or acquiescing to it;
2. The limitation period in which the beneficiary was required to bring his claim has expired; and
3. The court should provide the trustee with relief pursuant to its statutory power, if it is satisfied that the conduct was honest, reasonable, and should be excused.

#### **Acquiescence by Beneficiary**

In respect of the conduct of the beneficiary, in cases where she has approved of the breach before it occurred, or acquiesced to it after it has occurred, then it is not open to her to claim damages for any loss that has occurred. However, it is important to note that as it is the beneficiary's conduct which precludes her from claiming damages, it is open to other beneficiaries who have not consented to breach to sue the trustee.

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<sup>7</sup> *Waters, supra* note 6 at 1236.

### **Limitation Period**

As with any other type of claim, claims against trustees for loss are subject to limitation periods. The situation in Ontario is somewhat confusing, because the province's *Limitations Act, 2002*<sup>8</sup> does not include specific rules for breach of trust cases and, as such, it is not clear which limitation period runs. Nonetheless, a beneficiary who wishes to bring a claim would be prudent to assume that the basic limitation period of two years from the date of discoverability applies<sup>9</sup>. Further, beneficiaries with potential claims in Ontario should be mindful of s. 13(6) of the *Limitations Act* which provides that an acknowledgment by a trustee will be taken to be an acknowledgment by any other person who is or becomes a trustee of that trust.

### **Court's Statutory Power to Relieve Trustee**

The third and most frequent ground for requesting relief from liability is the statutory power provided to courts. This type of power extends back to nineteenth century England, when it was unusual for a trustee to apply to the court for advice, both because of the cost of doing so and because most estates were so small that it was not uncommon for the trustees to be required to bear the costs of the application themselves. In these circumstances, it was felt that if a trustee had made efforts to obtain advice from some other sort of expert and had acted honestly and reasonably on that basis, then he should not be penalized if a loss occurred.<sup>10</sup> Although, trustees now have the option of applying to court for advice, the court still has the option of providing them relief when breaches of trust occur.

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<sup>8</sup> S.O. 2002, Ch. 24, Schedule B., *as amended*.

<sup>9</sup> *Ibid.* at s. 6.

<sup>10</sup> *Waters, supra* note 6 at 1257.

While most jurisdictions have statutory sections that provide this type of relief, s. 35 of the *Trustee Act*<sup>11</sup> in Ontario is instructive. It provides that:

If in any proceeding affecting a trustee or trust property it appears to the court that a trustee, or that any person who may be held to be fiduciarily responsible as a trustee, is or may be personally liable for any breach of trust whenever the transaction alleged or found to be a breach of trust occurred, but has acted honestly and reasonably, and ought fairly to be excused for the breach of trust, and for omitting to obtain the directions of the court in the matter in which he committed the breach, the court may relieve the trustee either wholly or partly from personal liability for the same.

A number of observations about this section can be made. To begin with, it does not apply to situations where the loss arose from the investment of trust property.<sup>12</sup> If the breach arises from this type of investment, then a trustee seeking to be relieved from liability will be required to rely on section 28 of the Act.

Section 35 specifically applies to situations where the trustees have not previously applied to the court for directions relating to the matter that is the source of the breach. This is because when a trustee properly acts in reliance on the instructions of the court and a loss occurs, they will not be held liable, provided they have not acted fraudulently or misrepresented the court when seeking the directions.<sup>13</sup>

It is also of note that the party seeking relief does not have to be a named trustee. If they are in a position where they may be held to be “fiduciarily responsible” as a trustee, then the section still might apply. Additionally, the section does not require that a breach of trust be established in order for a trustee to be relieved. It is sufficient that the trustee *may* be liable in order for the court to rely on the section in excusing him or her. This also has the effect that the

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<sup>11</sup> *Trustee Act*, *supra* note 3.

<sup>12</sup> *Ibid.* at s. 28.

<sup>13</sup> *Ibid.* at s. 60(2).



trustee does not actually have to request the relief. The court has the discretion to relieve the trustee without being asked to do so. Nonetheless, if the trustee is actively seeking to be excused from liability, then the onus will fall on him to demonstrate that the circumstances are such that the court should exercise its discretion.<sup>14</sup>

Before a court relieves a trustee, there are two criteria, of which both must be satisfied. First, the trustee must have acted “honestly and reasonably.” Second, it is required that “he ought fairly to be excused...” Courts have avoided attaching strict definitions to the terms “honestly”, “reasonably”, and “fairly” and instead tend to rely heavily on the specific facts in each case. As a result, it is difficult to identify any situations where it is certain a trustee will be excused. Although there are certain types of situations where courts tend to be more willing to excuse the trustee, there is a sufficient level of conflict in the case law that in any given situation counsel representing the beneficiary or the trustee should both be able to find jurisprudence that will be of assistance to them.

### ***“Honestly and Reasonably”***

The honesty of the trustee is a fundamental requirement that is generally not at issue in cases where he or she is seeking to be excused. “Honestly” is generally given its usual meaning and also requires that the trustee not have been wilfully reckless or acted with gross negligence.<sup>15</sup> Although some courts have interpreted it to require an active involvement in the administration of the trust, it appears that this consideration is more properly included when determining whether the trustee has been reasonable.<sup>16</sup> Because it is generally obvious when a trustee has acted

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<sup>14</sup> *Lamport v. Thompson et al.*, [1940]

<sup>15</sup> *Waters*, *supra* note 6 at 1258.

<sup>16</sup> *Wagner v. Van Cleeff* (1991), 43 E.T.R. 115 (Ont.Gen.Div.) [*Wagner*].

honestly or not, on most occasions the decision will turn on either whether the trustee's behaviour was reasonable or whether he ought fairly to be excused.

When determining whether the conduct was reasonable, the Supreme Court of Canada has said that "the standard of care and diligence required of a trustee in administering a trust is that of a man of ordinary prudence in managing his own affairs..."<sup>17</sup> While the trustee is not considered to be infallible, nor is she expected to guarantee the trust assets, she is expected to use ordinary skill and prudence as well as apply common sense to the decisions she makes.<sup>18</sup> Relevant considerations have been found to include:

- The degree of sophistication possessed by the trustee;<sup>19</sup>
- Whether the trustee was paid for her services;<sup>20</sup>
- Whether the trustee was a professional trustee;<sup>21</sup>
- Whether the trustee relied on the professional advice of another party;<sup>22</sup>
- The degree to which the trustee had attempted to ascertain and understand his duties;
- In the event a third party was involved in the administration of the estate, whether the trustee adequately supervised that party;<sup>23</sup>
- Whether someone is a passive trustee (while generally not relevant when determining whether a breach of trust occurred, it can be used when seeking to be relieved from liability).<sup>24</sup>

Provided that the trustee's actions have been honest and reasonable, the court will then consider whether she can fairly be excused.

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<sup>17</sup> *Fales v. Canada Permanent Trust Co.* [1977] 2 S.C.R. 302 (S.C.C.) [*Fales*].

<sup>18</sup> *Ibid.*

<sup>19</sup> *Kinah v. Kurta* (1995), 8 E.T.R. (2<sup>nd</sup>) (Ont. Gen. Div.).

<sup>20</sup> *Ritzie v. Bint*, [1970] O.J. No. 123 (Ont. H.C.J.) at para 151.

<sup>21</sup> *Fales*, *supra* note 18.

<sup>22</sup> *Linsley et al. v. Kirstiuk et al.* (1986), 28 D.L.R. (4th) 495 (B.C.S.C.)

<sup>23</sup> *Wagner*, *supra* note 17.

<sup>24</sup> *Dover*, *supra* note 7.

***“Ought Fairly to be Excused”***

Fairness is “not a mere description of the discretion that is given. The court must consider how excusing the trustee will affect and can in all equity be permitted to affect, the interests of every party.”<sup>25</sup> Despite this, it is unclear that courts give all that much consideration to the effect that excusing the trustee will have on the other parties involved. The jurisprudence suggests that courts will usually only focus on whether it is fair to the trustee to hold him liable for a breach of trust. Even then, the question of whether a trustee ought fairly to be excused is not treated as a discrete question. It would appear that when a trustee’s behaviour has been both honest and reasonable, a court will usually automatically find that he ought to be relieved from liability.

**EXAMPLES FROM CASE LAW**

The following case law provides an overview of the application of s. 35 and illustrates examples of situations where relief has been granted and refused.

**Cases Where Relief Was Granted**

In *Re Faith Haven Bible Training Centre*<sup>26</sup>, a husband and wife had established a school dedicated to education and training in Christianity. They incorporated the school as a charity and in the letters patent provided that the directors and the employees were to serve without remuneration and receive no profit from the school. It was also provided that upon the dissolution of the charity, any remaining property would be distributed to charitable

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<sup>25</sup> *Wagner, supra* note 17.

<sup>26</sup> (1988), 29 E.T.R. 198 (Ont. Surr. Ct.)

organizations. Eventually, the school closed and when the directors were winding-up the charity they paid the employees stipends of \$1,000 for each year of service. The directors also gave themselves stipends ranging from \$10,000 to \$30,000. The Public Trustee took the position that the stipends were a serious breach of trust on the part of the directors, while the directors took the position that they were entitled, in the proper exercise of their rights and duties, to make those types of payments.

The court was of the view that the stipends constituted a breach of trust because the letters patent clearly said that remuneration would not be provided and that, on dissolution, the money would go to charity. It then considered whether the directors should receive relief on the basis of s. 35. In respect of the stipends given to the employees, the court held that they had been paid to the employees because of their devotion and dedication and that, on this basis, they were fair, reasonable, and morally justified. As such, the court determined that the directors were entitled to relief. However, in respect of the payments made by the directors to themselves, the court held that given the blatant conflict of interest and duty, they could not conclude that the conduct “ought fairly to be excused.”

Relief was also granted in *Laird v. Mulholland*.<sup>27</sup> This case involved the applications by the former attorneys of the deceased to pass their accounts. While still living, the deceased had given the attorney signing authority on two of her bank accounts and later executed a Power of Attorney in his favour. After her death, when the attorney was required to pass accounts, it was discovered that sums of money had been transferred from the deceased’s account to the attorney’s account, although they had later been paid back with interest. Additionally, he was unable to account for several disbursements that had been made using her funds. The court held

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<sup>27</sup> [1998] O.J. No. 855 (OCJ – Gen Div.)

that the inability of the attorney to document the transactions amounted to a breach of trust. However, it found that he deserved to be relieved because he acted honestly and reasonably. There was no evidence that the disbursements were not made for the deceased's benefits and significant evidence that the attorney performed many services entirely for her benefit and never sought compensation. Additionally, the court said it was satisfied that the gifts that had been made were keeping with the deceased's generous nature.

It is important to note that when the deceased executed the power of attorney, she was mentally capable and remained that way while the attorney was managing her property. It is likely that had she been incapable, the attorney would have had significantly more difficulty claiming his behaviour was "honesty and reasonable" and it is doubtful that the court would have granted him relief.

*MacDonald v. Hauer*<sup>28</sup> involved a similar statutory provision in Saskatchewan. In this case, one of three estate trustees opened a margin account for the purpose of trading in speculative securities. He then gave securities owned by the estate to the broker as security for the margin as well as executing a power of attorney in his favour, using which the broker sold the estate's securities and replaced them with speculative investments. The estate trustee and the broker planned to share the profits equally. At no point in time were the other two trustees aware of what he was doing. Eventually, the value of the investments substantially declined and one of the unaware trustees brought a claim against the other trustee and the broker. The broker cross-claimed against all of the estate trustees for indemnity against the damages. While the court held that the conduct of the trustee who engaged in the trading was dishonest and fraudulent, it found that the two passive trustees should be excused. The court found that for them to be liable it

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<sup>28</sup> (1976), 72 D.L.R. (3d) 110 (Sask. CA).

would have to find that they were jointly liable for the breach of trust and that given the fraudulent conduct by the third trustee, the liability should not be joint. In any event, the court found that the two passive trustees had, at all times, behaved honestly and reasonably and, as such, should be excused.

While *MacDonald v. Hauer* provides support for the contention that there are some cases where passive trustees will be excused, it is important to note the somewhat odd circumstances that led to their involvement in the claim. The trustee who committed the fraud admitted it and while he claimed against the broker for indemnity, he did not claim against the other trustees. It was the third-party broker, who had knowledge of the fraud, who was trying to claim against the passive trustees for indemnity. Under the circumstances, it seems implausible that a court would ever order the passive trustees to indemnify someone who knowingly participated in a fraud.

A final situation where relief was granted occurred in *Re Cooper (No. 2)*.<sup>29</sup> This involved a situation where two solicitors in at a law firm were both appointed estate trustees. While both applied for probate, only one of them was involved in administering the estate. The passive trustee had actually executed a resignation and given it to the other trustee, but it was never filed. The active trustee stole a substantial amount of money from the estate and was later convicted of fraud. The court found that the passive trustee was entitled to protection under s. 35. To begin with, he never had a reason to suspect the active trustee of dishonesty and acted as a prudent estate trustee would have acted under the circumstances. Further, it held that any loss that occurred was caused wholly by the wilful misconduct of the active trustee.

### **Cases Where Relief Was Refused**

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<sup>29</sup> (1978), 21 O.R. (2d) 579 (Ont. Surr. Ct.).

One of the more commonly referred to cases relating to the refusal to grant relief is the Supreme Court of Canada's decision in *Fales v. Canada Permanent Trust Co.*<sup>30</sup> This case dealt with a similar statutory provision in British Columbia. Here, the Canada Permanent Trust Company and the wife of the deceased were co-trustees. The trustees had purchased shares in a speculative investment. The corporation then went bankrupt before the shares had been exercised. The beneficiaries sued Canada Permanent, which then claimed against the co-trustee for indemnity and contribution. The court found that Canada Permanent had breached the duty it owed to the beneficiaries and failed to meet the standard of care and diligence required by a trustee when managing a trust. Among other things, the company had failed to track the performance of the shares, had made no attempt to sell them when their value declined, and failed to provide accurate advice about the shares' performance to the other trustee. The court held that the total inaction on the part of Canada Permanent that gave rise to the breach was such that the company's behaviour could never be described as reasonable. Exacerbating the situation was the fact that not only was the company getting paid for their work, but that it was a trust company that specifically provided the type of administration services that it managed to fail at performing.

For its part, Canada Permanent claimed indemnity and contribution against the other trustee. While the court found she, too, had committed a breach of trust by failing to exercise independent judgment and failing to sell the shares in a timely manner, she could fairly be excused from liability. She had acted honestly and reasonably and, despite her lack of sophistication, had tried to keep herself informed. The reason the breach occurred was not because of she neglected her duties, but because Canada Permanent had failed to give her the

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<sup>30</sup> *Fales*, *supra* note 19.

information she need to make an informed opinion. She never acted irrationally and made all decisions which she was asked to make within the limits of her experience and knowledge.

While *Fales* provides an example of a trustee being given relief because, in part, she was less experienced than the people whose advice she relied on, the court still requires that trustees make a degree of effort to inform themselves of their duties and obligations.

In *Wagner v. van Cleeff*<sup>31</sup> Wagner's sister had died and she came to Canada to help settle the estate. She spoke no English and relied on van Cleeff to help her. Van Cleeff was appointed trustee and executed powers of attorney to Mayhew so he could assist in the administration of the estate. Sometime later Mayhew misappropriated the bulk of the estate's assets. The court found that van Cleeff was not in breach of his duty in choosing Mayhew as estate solicitor, because he had no reason to believe that Mayhew would be dishonest. However, he did breach his duty by failing to adequately supervise Mayhew. The court then declined to offer relief under s. 35. It found that while van Cleef had acted honestly, his actions could not be called reasonable because he seemed completely ignorant of his duties as trustee. Unlike in *Fales v. Canada Permanent Trust Co.*, where the inexperienced trustee was excused from her breach of trust because she attempted to perform the duties of a trustee, in this situation not only did van Cleeff not know what a trustee's duties were, he also made no attempt to find out. In respect of the argument that he should be relieved because he was a gratuitous trustee, while the court did not deny this could be a factor that was taken into account, it also said that while a gratuitous trustee is entitled to a more lenient standard under s. 35, the test was not purely subjective. Irrespective of whether someone is being paid or not, there is still a standard under which no trustee can fall.

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<sup>31</sup> *Wagner, supra* note 17.



It is interesting to note that Wagner was not a beneficiary of the estate. Her sister had died intestate and at the time, their parents were still living. As such, Wagner stood to receive nothing. It was only when they died two years later that she became the beneficiary (and thus had standing to sue the trustee). As such, the court was unwilling to accept van Cleeff's argument that she had acquiesced to Mayhew's actions because at the material time she was not a beneficiary. The court concluded that she had no knowledge of the fraud that was occurring. In any event, her actions prior to the death of her parents were not relevant to van Cleeff's actions because she had no interest in the estate.

*Laird v. Lyne Estate*<sup>32</sup> is another situation where the court rejected the argument of two trustees that they should be relieved from a breach on the basis of their inexperience. In this case, the trustees sold an interest in six leases held by the estate and agreed to defend any actions commenced in respect of the leases. The sale of these leases resulted in extensive litigation. In rejecting their claim for relief, the court held that even those who lack education and business experience are still required to use ordinary skill and prudence when administering the estate. Rather than the trustees lack of experience excusing the breach, the court found that it exacerbated it. It held that in light of the respondents' lack of education and experience it was even less reasonable for them to have entered into the business deal and then participated in drawn out litigation. Ultimately, the trustees failed any test, no matter how low a standard was applied, in administering the estate.

Finally, *Re Smullen Estate*<sup>33</sup> provides a good example of the limits on the court's willingness to relieve a trustee who relied on professional advice. Here, the trustee was the deceased's son and the beneficiaries were the trustee's children. The trustee used trust funds to

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<sup>32</sup> [2004] B.C.J. No. 45 (B.C. S.C.)

<sup>33</sup> [1995] O.J. No. 675 (Ont. Gen. Div.).

pay for his daughter's day care expenses (which was not authorized by the trust instrument) as well as including interest payments from trust investments in his own income and then using trust funds to pay the taxes that arose from doing so. The trustee argued that if he was in breach of trust, he should be relieved because he relied on the advice of a qualified chartered accountant, notwithstanding the fact that the advice was bad. The court rejected this argument and said that it was factually wrong for the trustee to have described income of the trust as his own then use the trust funds to pay the tax. It further found it extraordinary that an accountant would have recommended this and that the trustee would have believed that it was an appropriate thing to do. Thus, it seems that while a court might be willing to excuse a trustee's conduct if he relied on professional advice, the advice itself must seem, on the surface, to be reasonable.

While the fact remains that courts will rely heavily on the facts when determining whether a trustee ought to be relieved, on the basis of the foregoing there are several principles that have emerged:

- The onus is on the trustee to prove that he acted honestly and reasonably;
- The test of whether a trustee should be relieved under s. 35 is not purely subjective. There is a minimum standard of ordinary skill, prudence, and common sense to which every trustee must adhere;
- While a trustee may rely on the fact that she received professional advice when requesting relief, a court is unlikely to grant it unless the advice appeared, on its face, to be reasonable;
- Even when a trustee relies on a co-trustee or a third party to administer a trust, the trustee still must take steps to understand her duties and obligations and should avoid completely relying on the other party;
- While a trustee may rely on his lack of sophistication or inexperience when requesting relief, the court is unlikely to grant it if it appears the trustee attempted to enter into transactions that were clearly beyond his/her level of knowledge; and
- Although a trustee may seek contribution and indemnification from a co-trustee, this will only be available to them when the co-trustee is also found in breach of trust.

## REMEDIES FOR BREACH

When a trustee has been found liable for causing a loss, and the court has declined to relieve him of that liability, he will then be required to compensate the beneficiaries for that loss. The objective is to reinstate the trust to the position it had been in had the breach not occurred. The objective is not to punish the trustee.<sup>34</sup>

The possibility that a trustee will be required to compensate the trust generally arises in two contexts. The first is when the beneficiaries bring a claim against the trustee for losses that they have incurred because of breach of contract. The measure of the trustee's liability will be the size of the loss caused to the trust by his acts or omissions.<sup>35</sup> The trustee might also be required to disgorge any profits received as a result of the breach of trust. In *Public Trustee v. Mortimer*, the trustee misappropriated more than \$200,000.00 from the estate. As some of the beneficiaries were charities, the Public Trustee commenced an action, claiming damages for the fraud. The court held the trustee liable for not only the funds that he stole, but also the amount of interest that they would have earned had they been properly held in trust.

The second context in which a trustee can be ordered to compensate the trust is during a passing of accounts. When a trustee applies to pass accounts, the beneficiaries have the right to raise objections to the accounts. It is then up to the court to determine whether the accounts should be passed or not. Section 49(3) of the *Estates Act*<sup>36</sup> holds that

The judge, on passing any accounts under this section, has the power to inquire into any complaint or claim by any person interested in the taking of the accounts

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<sup>34</sup> *Wakefield v. Wakefield* (1901), 2 O.L.R. 33 (Ont. C.A.).

<sup>35</sup> *Fales*, *supra* note 19.

<sup>36</sup> R.S.O. 1990, ch. E.21, as amended.

of misconduct, neglect, or default on the part of the executor, administrator or trustee occasioning financial loss to the estate or trust fund, and the judge, on proof of such claim, may order the executor, administrator or trustee, to pay such sum by way of damages or otherwise as the judge considers proper and just to the estate or trust fund, but any order made under this subsection is subject to appeal.

Thus, if the court decides that accounts should not be passed and that a breach of trust has occurred, it has a number of options available to it. One remedy is that the court can reduce the amount of compensation to which a trustee is entitled or can deny it altogether. In *Re Wood Estate*,<sup>37</sup> the trustee had, amongst other errors, filed tax returns late, resulting in penalties being incurred by the estate. As a result, the court reduced the amount of compensation to which he was entitled.

In the event that the trustee has pre-taken compensation or has also charged professional fees to the estate, the court can order those reimbursed. In *Fareed v. Wood*,<sup>38</sup> the estate trustee applied to pass accounts. One of the beneficiaries objected to both the accounts and the compensation claimed on the basis that the trustee had done nothing to administer the estate. He had not applied for a certificate of appointment, nor had any of the beneficiaries received their bequests. While the parties were in agreement that the trustee had not taken any money other than for fees and disbursements and had not attempted to convert the assets of the estate to his own use, the beneficiary objected to the fact the trustee had taken \$207,000 in fees and paid out \$161,055 of unidentified disbursements. At the time of the hearing, there was less than \$4,000 in the estate account and the testamentary gifts had not been paid. The court held that the trustee was so clearly negligent and in breach of his fiduciary duty that he was not permitted to benefit in

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<sup>37</sup> [1977] 2 W.W.R. 538 (Sask. Surr. Ct.).

<sup>38</sup> [2005] O.J. No. 2610 (Ont. S.C.J.).

any manner whatsoever for his involvement in the estate. The trustee was ordered to reimburse the estate for the full amount of legal fees he had taken and denied any form of compensation.

The court can also order the trustees to reimburse the estate for a loss it incurred because of their negligence. In *Re Proniuk Estate*,<sup>39</sup> the court found that the trustees had improperly failed to invest funds held in the estate trust fund, resulting in a loss in interest the estate otherwise would have received. Further, the court found that the trustees had improperly taken compensation prior to the passing and, as such, the estate was denied interest it would have received had those funds been retained by the estate and invested. The court ordered the trustees to pay to the estate the interest it would have received had the funds all been properly invested.

The liability that a trustee may encounter for breach of trust will extend past the death of the trustee. Section 56 of the *Trustee Act* holds that the estate of a trustee will be liable for any waste the trustee commits in the administration of an estate while still living.

## **CONCLUSION**

While it is clear that courts are willing to apply section 35 of the *Trustee Act*, trustees still have an obligation to exercise normal prudence and common sense when administering a trust. It is important that trustees maintain active involvement with the trust and avoid, wherever possible, becoming a passive trustee. In the event that one trustee is more involved in the trust than the other, the inactive trustee still has an obligation to ensure that she remains aware of how the trust assets are being handled. Although trustees are generally permitted to retain third-party assistance for certain aspects of the trusts administration, they still have an obligation to supervise

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<sup>39</sup> [1986] A.J. No. 686 (Alta. Surr. Ct.).

that third-party and to avoid suspending critical judgment when it comes to accepting professional advice.

As we have seen, in the event that a court is unwilling to relieve a trustee from a breach of trust, the consequences can be serious. While a finding of a breach of trust in an action brought by a beneficiary can obviously result in a trustee having to pay damages, in the context of a passing of accounts, the court's discretion extends past merely reducing compensation – it can also order the trustee to pay damages. This potential for liability should encourage every trustee to take the duties and obligations that come with the position very seriously.