The text below is an extract from the 7th edition of Drafting Trusts & Will Trusts (2004) para 15.20-15.22. It was written in the context of accumulation & maintenance trusts, which are obsolete from 2006, so the passage is not included in the current edition of DTWT. It is however included in this resource archive because the points discussed here might still be relevant to a discretionary trust which wishes to accumulate income after the expiry of the accumulation period. See DTWT 9th edition para 15.9 (strategies for trustees after the accumulation period expires). Eventually, hopefully, the enactment of the Law Commission proposals to abolish the rules against accumulation of income will put an end to this arcane and absurd area of law.

Income clause for class of beneficiaries including unborns

The rule against accumulations poses a serious problem for the A&M trust which is to cater for unborn beneficiaries. The drafter cannot use the form set out above for a closed class of beneficiaries. For even after the expiry of the accumulation period – 21 years from the date of the trust – the immediate beneficiaries of the trust may still be children, possibly very young children. The trustees may not wish to distribute all the income to them; but they cannot be authorised to accumulate the income.

The only solution to this problem is a tortuous one. Accumulation is permitted even after the accumulation period, if it is made under section 31 of the Trustee Act 1925.[1] This is the key to avoiding the rule against accumulations, for the benefit of beneficiaries born after the trust is made, who will still be minors when the accumulation period has expired.

How does the drafter direct accumulation under section 31 of the Trustee Act 1925? This is by no means simple. The drafter must steer a very delicate course here. One who is innocent of the technicalities and relies on common sense will fall into error. Section 31 reads as follows:

(1) Where any property is held by trustees in trust for any person for any interest whatsoever, whether vested or contingent, then, subject to any prior interests or charges affecting that property

(i) during the infancy of any such person, if his interest so long continues, the trustees may ... apply for or towards his maintenance, education, or benefit, the whole or such part, if any, of the income of that property as may, in all the circumstances be reasonable ...

(ii) if such person on attaining the age of 18 years has not a vested interest in such income, the trustees shall thenceforth pay the income of that property ... to him, until he either attains a vested interest therein or dies, or until failure of his interest;

[There follows a proviso, discussed below, but not of present interest.]

(2) During the infancy of any such person, if his interest so long continues, the trustees shall accumulate all the residue of that income ... and shall hold those accumulations as follows:

(i) If any such person

(a) attains the age of 18 years, or marries under that age, and his interest in such income during his infancy or until his marriage is a vested interest ...

the trustees shall hold the accumulations in trust for such person absolutely ...

(ii) In any other case the trustees shall, notwithstanding that such person had a vested interest in such income, hold the accumulations as an accretion to the capital of the property from which such accumulations arose, and as one fund with such capital for all purposes....

*(i) Accumulation under **statutory** power*

Accumulation must be under the statutory power, not under any non statutory power. It is essential to incorporate section 31 of the Trustee Act 1925 by reference to the statutory provision itself. One should not set out the terms of section 31 expressly, either in a paraphrase or even verbatim. In such cases the accumulation would not be under the Astatutory power@. The accumulation would be under an express power, and may be void for breaching the rule against accumulations.

Section 31 may apply by implication; but it is better to say expressly that the provisions of the section are to apply.

It is common practice for the drafter to incorporate section 31 but to tinker with its terms. Two amendments are standard.

The first concerns section 31(1)(i). The words Aas may, in all the circumstances, be reasonable@ are replaced with the words Aas the trustees in their absolute discretion think fit.@ This amendment has no practical effect, because there is an overriding principle that trustees must exercise their powers reasonably. In this book, this amendment is not made. If it is made, no harm is done.

The second standard amendment is to delete the proviso to section 31(1). The proviso reads:

> Provided that, in deciding whether the whole or any part of the income of the property is ... to be paid or applied for the purposes aforesaid, the trustees shall have regard to the age of the infant and his requirements and generally to the circumstances of the case, and in particular to what other income, if any, is applicable for the same purposes; and where trustees have notice that the income of more than one fund is applicable for these purposes, then, so far as practicable, unless the entire income of the funds is paid or applied as aforesaid or the Court otherwise directs, a proportionate part only of the income of each fund shall be so paid or applied.

The first limb of the proviso (up to the semicolon) is harmless surplusage: of course trustees should Ahave regard to the circumstances of the case@.

The second limb requires trustees of different trusts to share the costs of maintenance. This may well restrict the freedom of the trustees to act in the most advantageous way. The second limb of the proviso should therefore be deleted. The easiest way to do this is to delete the entire proviso. It does not matter that by deleting the whole proviso one has deleted both of its limbs, since the first limb is in any event superfluous.

This common amendment to section 31 does raise a question. Accumulation is only to be countenanced under the Astatutory power@. Is one applying Athe statutory power@ if it is amended in this way? It is considered that no problem arises. The practical effect of the common amendments is trivial. This is the standard practice of conveyancers to which the courts can and should have regard.[2]

The same does not, however, apply to more substantial amendments to section 31. One sometimes sees this form:

> Section 31 of the TA 1925 shall apply with the substitution of A25" for A18" wherever it occurs.

This drafting technique is not effective. The effect of the amendment is so to alter section 31 that the trustees cannot be said to be accumulating under the Astatutory power@.[3] A clause of this sort may therefore breach the rule against accumulations.

The same objection applies to a form such as this:

> Section 31 of the TA 1925 shall apply but so that the Trustees may pay or apply income pursuant to subsection (1)(i) for the maintenance education or benefit of any Beneficiary for the time being under the age of 18 years.

It is unlikely that such wording is applying the Astatutory@ power; if that is correct, then the clause may breach the rule against accumulations.

(ii) The statutory power must be applied in the right way

The statutory power must be applied in the right way. The statutory power cannot be applied in isolation; it only applies where property is held by trustees in trust for any person for: (i) any vested interest or (ii) any contingent interest.[4] At first sight this raises no problem: the A&M beneficiary will always have some interest vested or contingent: for the income will be payable to him when he attains the age of 25.

However, section 31 operates in different ways, depending on whether the interest is vested or contingent:

(1) If the interest is vested, the beneficiary will become entitled to accumulated income on attaining the age of 18 (or marriage).

(2) If the interest is contingent, the beneficiary will not become entitled to the accumulated income, unless he becomes entitled to trust capital.

Which of these alternatives does the drafter want? Clearly, the second. If the trustees accumulate income, the last thing they will want is that the beneficiary suddenly becomes entitled to all the accumulations at the age of 18.[5] So the drafter should make sure that the beneficiary's interest is contingent, not a vested one. The usual form is to make the interest contingent on attaining the age of 25. The form used in this book is:

> The Trustees shall pay the income of the Share to the Principal Beneficiary during his life if he attains the age of 25.

Next, section 31 only applies to a contingent interest if it carries the intermediate income.[6] It has recently become fashionable to include a specific clause to the effect that:

> *All contingent gifts in this trust shall carry the intermediate income.*

The aim is to make it clear that section 31 will apply. It is desirable to avoid such jargon and in fact it is unnecessary. There is an express direction that section 31 is to apply. It is therefore plain that the Principal Beneficiary's contingent life interest carries the intermediate income from the expiry of the accumulation period[7] until the contingency is satisfied, *i.e.* until the Principal Beneficiary attains 25. Otherwise the provision has no effect, which can hardly be right.[8]

The form used in this book is therefore as follows:

> (1) While a Principal Beneficiary is living and under the age of 25:
> (a) The Trustees may apply the income of his Share for the maintenance, education or benefit of any of the Principal Beneficiaries who have not attained the age of 25.
> (b) Subject to that, the Trustees shall accumulate the income of the Share during the Accumulation Period. That income shall be added to the Trust Fund.
> (c) Subject to that, Section 31 of the Trustee Act 1925 shall apply to the Share (but with the deletion of the proviso to section 31(1).)

(2) The Trustees shall pay the income of the Share to the Principal Beneficiary during his life if he attains the age of 25.

1LPA. 1925, s.165. This section is a little obscure. It does not refer to s.31 expressly: it authorises accumulation of income under Aany@ statutory power. S.31 is clearly the statutory power referred to. S.165 took this form so as to include statutory powers now obsolete: Conveyancing and Law of Property Act 1881, ss.42, 43 (which applied to trusts made before 1926).

2*Blathwayt v. Baron Cawley* [1976] AC 397.

3The view is supported by *obiter dicta* of Knox J. in *Begg-MacBrearty v. Stilwell* [1996] STC 413 at 438-439.

4This follows from the opening words of s.31(1), which clearly also govern s.31(2).

5Not to mention the difficulties this raises for trust accounting, and the possible charge under TCGA 1992, s.71.

6For the concept of Acarrying the intermediate income@ see Snell's *Equity* (30th ed., 1999) or one of the standard textbooks on trusts. In a nutshell, a contingent interest Acarries the intermediate income@ if the beneficiary is contingently entitled to income arising before the contingency is satisfied.

7During the accumulation period, the income is dealt with under the express provisions of the clause, discussed above.

8In the case of a will trust a contingent interest will be assumed to carry the intermediate income unless the contrary intention is expressed. It is submitted that the same applies to lifetime trusts. There is no authority on this point: the cases are all concerned with wills, and LPA 1925, s.175 is restricted to wills. But the principle underlying the will cases applies equally to lifetime trusts. Where a settlor makes a contingent gift Ahe makes, as it were, an immediate appropriation of the property in question for the benefit of the person, born or unborn, to whom he gives it contingently, and it is in accordance with his probable intention that the gift should carry the intermediate income@; see *Re Geering* [1964] Ch 136 at 144.