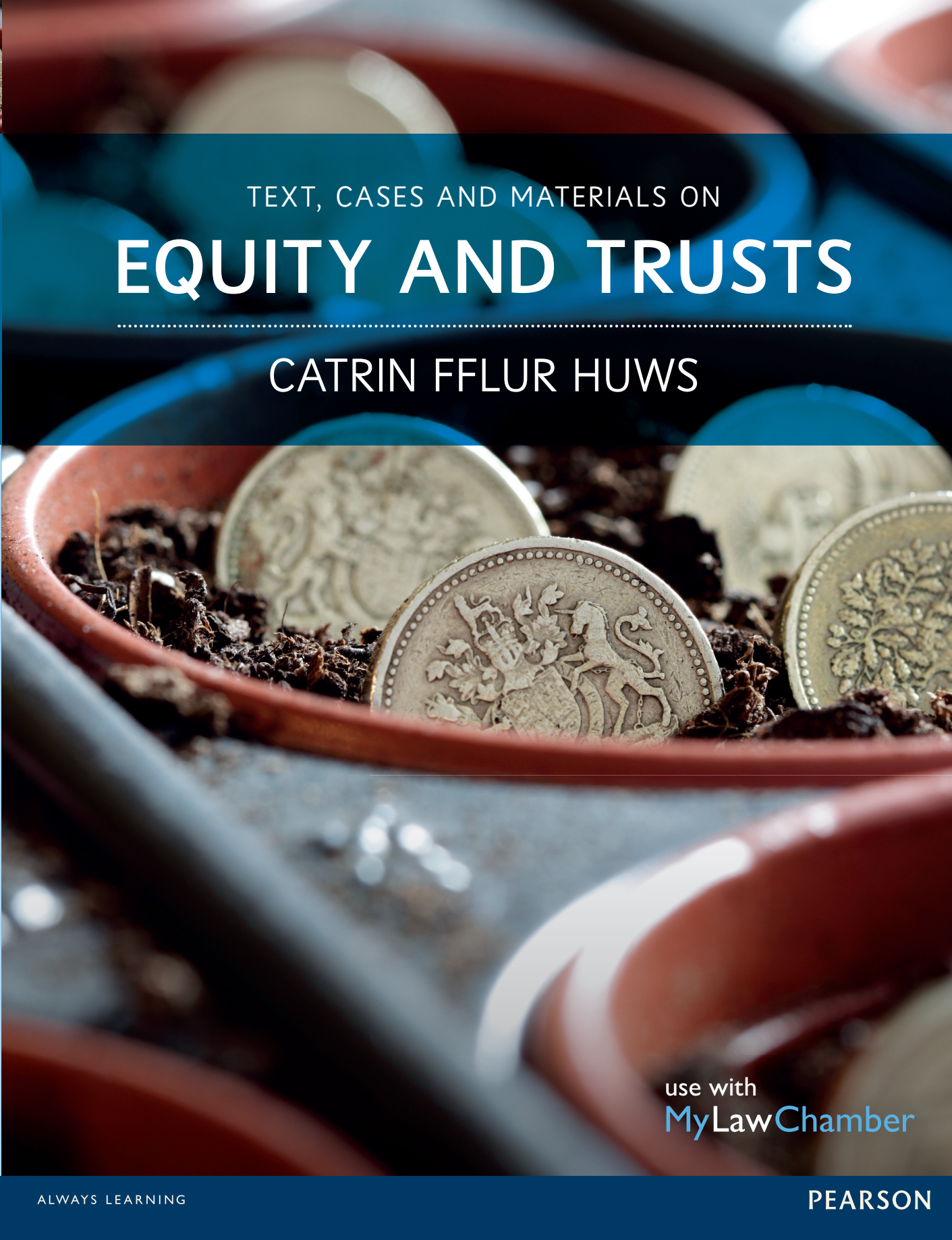

TEXT, CASES AND MATERIALS ON

EQUITY AND TRUSTS

CATRIN FFLUR HUWS

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Text, Cases and Materials on Equity and Trusts

Catrin Fflur Huws

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Introduction

Equity and trusts is a subject that seems to straddle all three years of an undergraduate degree. Some institutions regard equity and trusts as a foundation subject, and it is therefore taught as a first-year subject. Others view it as a nebulous subject, lacking in clear statutory provisions, and it is therefore the last foundation subject a student will study – in the final year of his or her degree.

Accordingly this book seeks to cater to a wide knowledge base. It is a text, cases and materials book, which means that the primary materials are largely permitted to speak for themselves, with the text providing a commentary on the features that are being emphasised in the article or the judgment. The book also includes excerpts from non-legal material – examples from literature, examples from charities' statements of objectives, examples from real situations, as well as more traditional resources such as cases and statutes. The book also uses non-legal materials that serve to inform the law – extracts from Hansard and the Charity Commission's guidelines for example.

The emphasis in this book is on the contextual nature of the law. Many of the cases were decided as they were because of the particular situations that came before the courts – in *Lloyds Bank* v *Rosset* [1991] 1 A.C. 107, Mr Rosset's trust fund had specifically sought to prevent Mrs Rosset from being entitled to a share of the matrimonial home and therefore it would have been surprising if the House of Lords had given judgment in her favour. Accordingly, students are encouraged to think about how differences of facts could have led to a different outcome. The book also encourages students to realise that there is no 'right answer' necessarily – equity's flexibility means that there is considerable scope for developing a counter-argument to the received wisdom.

Nevertheless, there is a tendency in the law to obfuscate and render complex what is in essence often a fairly straightforward question. Accordingly, the book seeks to avoid lengthy discussions of how a particular principle developed, and focuses instead on what the law is now. The emphasis is also on considering – outside of the law – what would be a rational thing to do. Often, what the law does is what the reader would regard as sensible in a real-world situation, and it is only when these social questions are couched in legal terms that the issue becomes confusing. Accordingly, the question of 'When should a person be entitled to a share of property that they do not own?' is far more readily – and easily answered than 'Should the court consider a holistic approach when determining whether a constructive trust should be imposed?' There is therefore an emphasis on considering the real people behind the litigation, and to consider whether they ought to have the entitlement they claim.

A number of activities are included. These can be used as the basis for independent thinking and discussion, but may also provide useful springboards for group discussion both within and outside structured teaching time. The book also includes pointers for further research and additional questions that may be asked. These aim to provide students with possible topics for assignments and projects, as well as topics that may form the basis of dissertation and extended essay modules.

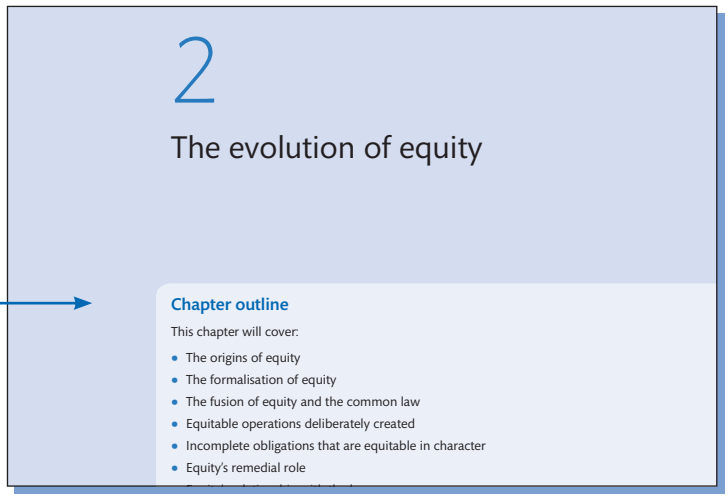
The book also seeks to provide some useful material for students who have already studied equity and the law of trusts, as well as those who have yet to do so. Students taking contract law and land law often find equity daunting if they have not yet studied it, and students taking commercial law, torts and land law may have already studied equity, but may feel the need to be reminded of some of the equitable concepts as these concepts arise in relation to other subjects. Accordingly, Part 1 of this book focuses on equity as a discrete area, and may therefore provide useful reading for students of land law, contract law, commercial law, torts and criminal law.

Parts 2–5 have a tighter focus on trusts. Part 2 focuses on the trust relationship and the parties to the trust, beginning with the trust institution, and then dealing with the formalities and the ways in which the parties interrelate. Part 3 addresses the different contexts of the trust – domestic and commercial, public and private, express and implied. Part 4 focuses on the variation and termination of the trust, while part 5 focuses on tracing, and in particular its application to situations where money belonging to a trust has been misappropriated.

Finally, of course, the aim of this book is to make equity and trusts interesting. Perhaps it lacks the glamour of criminal law. Yet, it is hard to imagine that someone could have a career in law without dealing with equity at some point. Furthermore, equity, no less than criminal law, has its share of colourful characters, situations worthy of a play or a novel, and intriguing questions accompanied by beautifully logical answers. In this respect more than any other, I hope that this book fulfils its aims.

Guided tour

Chapter outlines located at the start of each chapter explain what topics are covered to help you focus your learning.



2

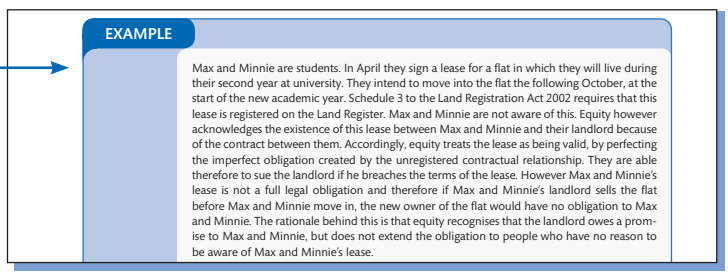
The evolution of equity

Chapter outline

This chapter will cover:

- The origins of equity
- The formalisation of equity
- The fusion of equity and the common law
- Equitable operations deliberately created
- Incomplete obligations that are equitable in character
- Equity's remedial role

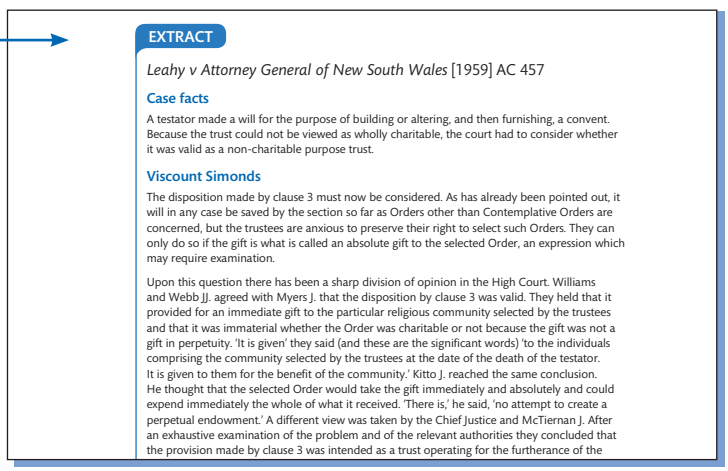
Examples throughout provide possible case scenarios to explain how the law operates in practice and help you to understand legal processes.



EXAMPLE

Max and Minnie are students. In April they sign a lease for a flat in which they will live during their second year at university. They intend to move into the flat the following October, at the start of the new academic year. Schedule 3 to the Land Registration Act 2002 requires that this lease is registered on the Land Register. Max and Minnie are not aware of this. Equity however acknowledges the existence of this lease between Max and Minnie and their landlord because of the contract between them. Accordingly, equity treats the lease as being valid, by perfecting the imperfect obligation created by the unregistered contractual relationship. They are able therefore to sue the landlord if he breaches the terms of the lease. However Max and Minnie's lease is not a full legal obligation and therefore if Max and Minnie's landlord sells the flat before Max and Minnie move in, the new owner of the flat would have no obligation to Max and Minnie. The rationale behind this is that equity recognises that the landlord owes a promise to Max and Minnie, but does not extend the obligation to people who have no reason to be aware of Max and Minnie's lease.

Case extracts explain and illustrate legal principles through real-world cases showing how and why judgments were made.



EXTRACT

Leahy v Attorney General of New South Wales [1959] AC 457

Case facts

A testator made a will for the purpose of building or altering, and then furnishing, a convent. Because the trust could not be viewed as wholly charitable, the court had to consider whether it was valid as a non-charitable purpose trust.

Viscount Simonds

The disposition made by clause 3 must now be considered. As has already been pointed out, it will in any case be saved by the section so far as Orders other than Contemplative Orders are concerned, but the trustees are anxious to preserve their right to select such Orders. They can only do so if the gift is what is called an absolute gift to the selected Order, an expression which may require examination.

Upon this question there has been a sharp division of opinion in the High Court. Williams and Webb JJ. agreed with Myers J. that the disposition by clause 3 was valid. They held that it provided for an immediate gift to the particular religious community selected by the trustees and that it was immaterial whether the Order was charitable or not because the gift was not a gift in perpetuity. 'It is given' they said (and these are the significant words) 'to the individuals comprising the community selected by the trustees at the date of the death of the testator. It is given to them for the benefit of the community.' Kitto J. reached the same conclusion. He thought that the selected Order would take the gift immediately and absolutely and could expend immediately the whole of what it received. 'There is,' he said, 'no attempt to create a perpetual endowment.' A different view was taken by the Chief Justice and McTiernan J. After an exhaustive examination of the problem and of the relevant authorities they concluded that the provision made by clause 3 was intended as a trust operating for the furtherance of the

Activities allow you to use the knowledge you have acquired to develop and cement your understanding of the topic.

ACTIVITY

1. If you were acting for the claimant in an application for an interim injunction, what would be the advantages to your client of obtaining a freezing injunction or a search order?
2. Think of five types of situation where applying for a freezing injunction might be appropriate. You might find it helpful to search for cases containing the key words 'freezing injunction'.
3. Think of five types of situation where applying for a search order might be appropriate.
4. You might find it helpful to search for cases containing the key words 'search order'.

Diagrams and flowcharts. These visual aids will make complex legal processes easier to follow and understand.

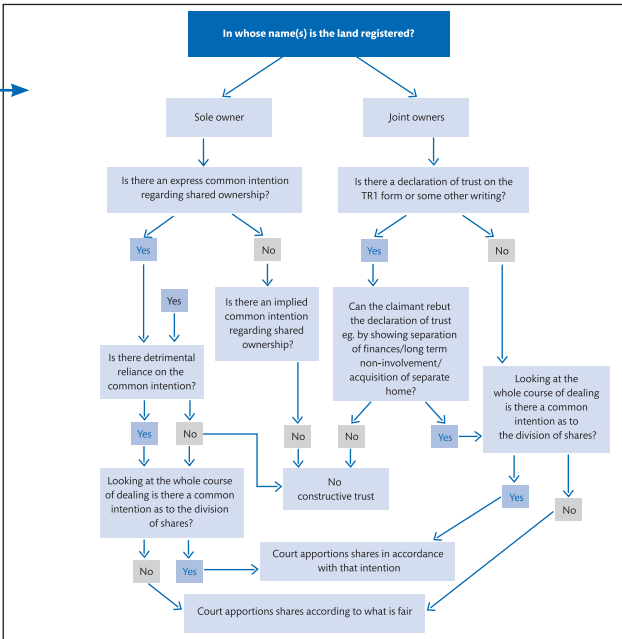


Figure 14.2 A flowchart for deciding validity

Chapter summaries located at the end of each chapter suggest areas of assessment and assignments for which the chapter provides useful insight.

Chapter summary

This chapter may be useful for assignments and assessments on:

- The personal nature of equitable obligations
- The proprietary nature of equitable obligations
- The maxims of equity
- Equity's approach to remedying legal disputes
- Equity's relationship with the law.

Suggestions for **further reading** at the end of each chapter encourage you to delve deeper into the topic and read those articles which could help you to gain higher marks in both exams and assessments.

Further reading

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Part 1

Equity

1

The concept of equity

Chapter outline

This chapter will cover:

- What is equity?
- Equity's contribution to the legal system
- Equity's relationship with the law.

What is equity?

This book is about equity and the law of trusts. The idea of why equity exists is sometimes a difficult notion to understand, and matters are probably not helped by complex ideas such as the distinction between 'legal ownership' and 'equitable ownership'. At this point the law student is likely to argue, 'Surely ownership is an absolute concept – one either owns something or one does not. Why do we need ownership to be legal or equitable?' Consequently, the law student is likely to feel that equity is a subject that is unnecessarily abstruse and complicated. Be assured that it is not. Equity is a simple concept, albeit with far-reaching ramifications. Equity is simply the name given to the way the law works when a strict application of the rules would create an absurdity because reliance on those legal rules would permit the very purpose of that rule to be undermined. Often this is assumed to be just part of the way the law works, and it is only when we try to divide 'law' and 'equity' into two separate things that it appears initially to be rather confusing.

EXAMPLE

Ted, Fred and Ned agree to buy a birthday present for Jed. Both Ted and Fred give Ned £10 and Ned promises to buy a suitable present and give it to Jed. Ned buys the present using the money Ted and Fred have given him but keeps the present for himself.

If we look at this scenario from the viewpoint of the law of contract, Ned's actions are perfectly legitimate. The shopkeeper has sold goods to Ned and Ned is now the owner of those goods. But this overlooks the fact that Ted and Fred have relied on Ned's promise in giving him the money, and that the money was given to Ned in order to buy a present for Jed. There should be no difficulty in appreciating that the law would be unsatisfactory if it could not offer any remedy regarding this situation. This is where equity intervenes.

The law as a system of rules

Imagine therefore that the law is a system of rules. One of the law's rules is to say that Person A (Ned from our scenario above) is allowed to own Item X (Jed's present). It then follows that if Person B (let us call him Rob) deprives Person A of Item X, the law should be able to restore Item X to Person A. For this reason, the law of contract seeks to defend Person A's entitlement to the acquisition of goods as a buyer, and to the retention of title to those goods as the seller unless suitable consideration is forthcoming. Similarly, criminal law and the torts of trespass and conversion are also means of bringing those who deny Person A of his or her goods to account. From a political perspective, these rules may be viewed as unfair in that they may be viewed as perpetuating social inequalities whereby some people have a great deal of property while others have very little. However, the law is not concerned with the moral rightness of the rules. Rather its concern is to ensure that such rules as there are, are applied consistently. In particular, the law is concerned that the rules are not misused so as to create a situation where adherence to the rules undermines the primary purpose of the law.

What happens when those rules are applied too rigidly?

When rules are created, it is impossible to foresee the situations to which those rules will need to be applied. It may be that a rule is appropriate in most circumstances, but it is possible that in some situations, the blind application of a legal rule may lead to an unintended outcome; for example rules that protect A from being deprived of his property may overlook the fact that A has used money belonging C and D (Fred, and Ted in our scenario) to purchase such property. Here it may be considered that to allow A to retain the property he has bought would be an unjust deprivation of C and D's claim to the property that arises from the fact that they are the true owners. Person A has acquired the title to the property, but it cannot 'rightfully' be said to belong to him, as we saw in the example above with Ned and his present.

A rule cannot therefore take into account every possible circumstance in which it will need to be applied. Nevertheless, it may be that in most situations – or at least in most foreseeable situations – the rule will be legitimate. For example, if a school requires that a uniform is worn when pupils are at the school, that rule will be consistently applied to all pupils. Some pupils may view this rule as being unfair, but it will nevertheless be a rule that is of general application, and one that is applied equally to all. The uniform policy may even cause hardship in individual circumstances, such as where a family can ill afford the cost of buying a school uniform. Nevertheless, individual hardship is unlikely to justify an exception being made.

However, such a rule may not have been intended to apply to a situation where a child's parent is also a teacher at the school, and the child goes with her parent to the school during the school holidays to help the parent tidy the store cupboard. Applying the uniform rule in this situation would be an absurd application of the rule, and would justify the rule being applied in a modified way – in that the rule only applies when the child is attending the school as a pupil and not as the offspring of a schoolteacher. It is this type of modification that equity performs in relation to law, where the legal rule is applied in a modified form in specific situations in order to prevent an unreasonable application of the law.

An example of a situation where reliance on the strict application of legal rules is demonstrated in the court scene in Shakespeare's *The Merchant of Venice*. In the play, Shylock contracts with Antonio for the loan of 3000 ducats. When the loan is not repaid, Shylock demands a pound of Antonio's flesh, and demands that the bond be strictly interpreted. Portia arrives at the court in order to defend Antonio, and explains that Shylock can neither cut more nor less than a pound in weight of Antonio's flesh, and neither must he spill a drop of Antonio's blood, thus demonstrating to Shylock the consequences of adhering too strictly to the letter of the law when doing so would result in injustice.

EXTRACT

William Shakespeare, *The Merchant of Venice*, Act IV, Scene 1

SHYLOCK

My deeds upon my head! I crave the law,

The penalty and forfeit of my bond.

PORTIA

Is he not able to discharge the money?

BASSANIO

Yes, here I tender it for him in the court;

Yea, twice the sum: if that will not suffice . . .

And I beseech you,

Wrest once the law to your authority:

To do a great right, do a little wrong,

And curb this cruel devil of his will.

PORTIA

It must not be; there is no power in Venice

Can alter a decree established:

'Twill be recorded for a precedent,

And many an error by the same example

Will rush into the state: it cannot be . . .

I pray you, let me look upon the bond.

SHYLOCK

Here 'tis, most reverend doctor, here it is . . .

PORTIA

Why, this bond is forfeit;

And lawfully by this the Jew may claim

A pound of flesh, to be by him cut off

Nearest the merchant's heart. Be merciful:

Take thrice thy money; bid me tear the bond.

SHYLOCK

When it is paid according to the tenor . . .

ANTONIO

Most heartily I do beseech the court

To give the judgment.

PORTIA

Why then, thus it is:

You must prepare your bosom for his knife . . .

SHYLOCK

Ay, his breast:

So says the bond: doth it not, noble judge?

'Nearest his heart:' those are the very words . . .

PORTIA

Have by some surgeon, Shylock, on your charge,

To stop his wounds, lest he do bleed to death . . .

SHYLOCK

I cannot find it; 'tis not in the bond . . .

PORTIA

A pound of that same merchant's flesh is thine:

The court awards it, and the law doth give it . . .

SHYLOCK

Most learned judge! A sentence! Come, prepare!

PORTIA

Tarry a little; there is something else.

This bond doth give thee here no jot of blood;

The words expressly are 'a pound of flesh:'

Take then thy bond, take thou thy pound of flesh;

But, in the cutting it, if thou dost shed

One drop of Christian blood, thy lands and goods

Are, by the laws of Venice, confiscate

Unto the state of Venice . . .

SHYLOCK

Give me my principal, and let me go.

BASSANIO

I have it ready for thee; here it is.

PORTIA

He hath refused it in the open court:

He shall have merely justice and his bond . . .

SHYLOCK

Shall I not have barely my principal?

PORTIA

Thou shalt have nothing but the forfeiture,

To be so taken at thy peril, Jew.

Rather than accepting the repayment of the loan, Shylock demands that the bond is performed according to its terms, with the result that because the repayment is late, Shylock is entitled to his pound of flesh even though its extraction will cause serious

harm, resulting in the probable death of Antonio. This scene dramatises the fact that a rigid adherence to the law of Shakespeare's fictional Venice would mean that it could be used to condone murder. Therefore, what this scene demonstrates is that although rules may be viewed as being necessary in order to govern what is acceptable and what is unacceptable behaviour in society, following these rules mechanistically is not always appropriate. The scene also makes another important point about the function of equity, namely that equity will not assist the person who refuses to behave in an equitable manner. Therefore, because Shylock refuses to accept anything other than that which is provided in the bond, the court will not permit him to rely on equity once it becomes apparent that it is impossible for the bond to be performed in accordance with its terms.[1] This scene therefore explains the underlying objective of equity. It does not exist to make the law (of contracts in this case), but merely to apply the rules of the law in a slightly modified form where that is necessary, such as where the law of contract might be misused to permit a greater wrong.

How does equity intervene?

In essence, equity is the modification of legal rules and principles with the objective of ensuring that the purpose of those rules is not defeated by their own application. One way in which equity intervenes is by not permitting a rule which exists in order to prevent fraud (in its wider sense of depriving someone of something to which they are entitled rather than the criminal offence as defined in ss.2–4 of the Fraud Act 2006)[2] to be used as an instrument of fraud. Equity originated in the Courts of Chancery as a means of '*alleviat[ing] the rigidity, the inflexibility and the inadequacy of common law remedies*'.[3] This is why it may be possible at some level to state that equity is concerned with notions of fairness and justice, because it exists in order to ensure that an injustice does not arise from the strict application of legal rules, as is explained in the *Earl of Oxford's Case* (1615) 21 ER 485:

> The cause why there is a Chancery is for that men's actions are so divers and infinite that it is impossible to make any general law which may aptly meet with every particular act and not fail in some circumstances. The office of the Chancellor is to correct men's consciences for frauds, breaches of trusts, wrongs and oppressions for whatever nature soever they may be and to soften and mollify the extremity of the law.

However, this is an overly simplistic evaluation of equity's role. Modern equity does not exist to circumvent a law or a principle that is regarded as unjust, and neither does it exist to create new rules where the existing rules are felt to be unfair. Indeed, the courts often

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[1] Further reading on the concept of dramatisation of equity in *The Merchant of Venice* may be found in: Billelo, T.C. (2004) 'Accomplished with what she lacks: law, equity and Portia's con' 16 *Law and Literature* 11; Carpi, D. (2004) 'Law, discretion, equity in *The Merchant of Venice* and *Measure for Measure*' 26 *Cardozo Law Review* 2317; Cohen, S.A. (1994) 'The quality of mercy: law, equity and ideology in *The Merchant of Venice*' 27(4) Mosaic 35; Hapgood, R. (1967) 'Portia and *The Merchant of Venice* and the gentle bond' 28(1) *Modern Language Quarterly* 19; McKay, M. (1964) '*The Merchant of Venice:* a reflection of the early conflict between the courts of law and the courts of equity' 15(4) *Shakespeare Quarterly* 371.

[2] (2006 c.35).

[3] Mason, A. (1997–98) 'Equity's Role in the Twentieth Century' 8 *King's College Law Journal* 1 at p.1.

recognise that the operation of law results in an injustice to an individual, and the failure to correct that injustice not infrequently causes controversy.[4] However, it may be argued that intervening in this way would involve an usurpation of Parliament's role by the courts, and would mean that what is just is decided according to individual notions of morality, something that Portia explains in the scene from *The Merchant of Venice* reproduced above. She explains that the court cannot refuse to apply the law simply because its observance results in an injustice. Her response to Bassanio's request that she does this is to state:

> It must not be; there is no power in Venice
>
> Can alter a decree established:
>
> 'Twill be recorded for a precedent,
>
> And many an error by the same example
>
> Will rush into the state: it cannot be.

In other words, she explains that she cannot refuse to apply the rules because 'many an error' would ensue if everyone wishes to have their case tried on the basis that they should be able to escape the contractual obligations to which they voluntarily agreed. Equity is not therefore concerned with the sort of 'palm-tree justice' alluded to by Lord Neuberger in *Revenue and Customs Commissioners v Total Network SL* [2008] 2 All ER 413 at p.476 in the form of '*relying on a general sense of morality or indignation, without regard to principle or the rule of law*'. Instead it operates on the basis of a set of principles that allows the court to recognise and remedy an unjust deprivation of a legitimate expectation, where some detriment has been incurred in reliance on another's words or conduct.

Furthermore, an individualistic approach of this nature would depart from the principle that similar cases should be decided in a similar manner. If the outcome of a case depended on what an individual case considered to be fair, then similar fact cases may be decided differently in different cases because what would be fair would depend on the individual judge's sense of right and wrong and not upon what the law requires.

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[4] In the case of *R (on the application of Age UK) v Secretary of State for Business Information and Skills* [2009] All ER (D) 141 (Sep) where Blake J acknowledges that a designated retirement age of 65 may be a source of disappointment for many older workers, but this does not affect the validity of the law. He explains:

> Given that Regulation 30 is direct discrimination that will result in considerable numbers of older members of the workforce who want to continue in employment not being able to challenge an employer's decision to the contrary, I accept that its adoption has an adverse impact on the dignity on autonomy of members of this class. The question is therefore whether a fair balance has been achieved in pursuit of the legitimate aim, whilst recognising the particular competence of government to make these choices. I recognise that any bright line based upon age will leave classes of persons aggrieved, and in the context of human rights litigation the courts have recognised that that is of itself not something that makes the claims disproportionate. I have not drawn particular assistance from the cases where the Strasbourg court have considered these matters because circumstances in each case were different from the present issue and more significantly age discrimination as an aspect of Article 14 of the European Convention on Human Rights has never been identified as a particularly weighty consideration.

EXAMPLE

Jack and Jill live in a house owned by Jack. Jill makes no contribution to the purchase of the house. Jack and Jill split up, and Jack asks Jill to move out. Jill argues that she is entitled to a share of the house. The case comes before Judge Brown who believes that Jill should be entitled to a share of the house because Jack and Jill's relationship was a joint venture, and that they should share everything. A significant factor in Judge Brown's decision is that Jill is a very nice person who was very upset when Jack asked her to move out. Judge Brown therefore feels that Jill deserves to have a share in the house.

Two weeks later, the case of Peter and Jane comes before the court. Peter and Jane live in a house owned by Jane. Peter makes no contribution to the purchase of the house. Peter and Jane split up, and Jane asks Peter to move out. Peter argues that he is entitled to a share of the house. The case comes before Judge Green who believes that Peter should not be entitled to a share of the house because it is Jane's house and there is no reason for Peter to have a share in something he has not paid for. A significant factor in Judge Green's decision is that Peter is a waster who has sponged off Jane for years. Judge Green therefore feels that Peter does not deserve to have a share in the house.

In this scenario, if distribution on the basis of what was considered to be fair in an individual case were permitted, then different courts would divide property in different ways, resulting in further injustice. Furthermore, it would not allow people in Peter, Jane, Jack and Jill's situation to predict when a cohabitant will be entitled to a share of the house. Peter and Jill would have to guess what conduct would suffice to entitle them to a share of the house, and Jack and Jane would not be certain as to what they own, even though they have the necessary documentation.

Accordingly, over time, equity has developed its own system of rules for determining when it would be unjust to follow the law strictly, and how that injustice ought to be remedied. In other words, it does not exist to determine what is fair in individual circumstances, but instead to determine when the law is being misused. Therefore, although on one level equity may be viewed as a means of resolving a frustration of legitimate expectations in individual circumstances, or what Hudson terms '*a reservoir of general moral principles*'[5] equity is more properly viewed as a substantive body of law with its own set of rules. Equity's relationship with the law therefore is to make rules for those circumstances where the legal rules do not extend appropriately. It is the legal system's mechanism for those contingent situations where the legal rules do not recognise or resolve the dispute. An analogy may be seen in the rules of football. The ordinary rules of football provide that the winner of the game is decided on the basis of which team has scored the highest number of goals after 90 minutes of game play. Usually, this suffices, and either a clear winner will emerge, or the game will be declared a draw if both teams score an equal number of goals. However, in a tournament setting, a winner will need to be identified in order to permit a team to progress to the next round. Accordingly, a different set of rules will apply, allowing for extra time and a penalty shoot out. Even though these provisions do not apply to every match, they nevertheless operate according to specific rules. Thus equity is the legal system equivalent of the extra time and penalty shoot out provisions.

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[5] Hudson, A. (2010) *Equity and trusts.* 6th ed. Routledge: London, p.4.

Equity's contingency rules apply in a broad range of circumstances, usually characterised by someone being led to believe in an entitlement, and acting to their detriment in reliance on that expectation by acting in a way that causes them either financial loss, or loss that may be quantifiable in financial terms. Accordingly, equity is commonly employed in the branches of law that relate to the acquisition of property, and the law of contracts, land law and the law of succession are all areas where the scope for equity to intervene is significant. All these subject areas are likely to involve situations where one individual acts in such a way as to give another the expectation of an entitlement to property. If the person in whom an expectation has been created can be shown to have acted to their detriment in reliance on that expectation, then it may be appropriate for equity to intervene. This is best illustrated by way of some examples.

EXAMPLES

Contract law

Bob and Terry enter into a contract whereby Bob agrees to pay Terry £1000 if Terry will paint Bob's house. Because the completion of the work is delayed, Terry agrees to accept £900 for doing the work. Terry cannot then rely on the original terms of the contract and demand that Bob pays the remaining £100 owed. This is a principle known as estoppel, which will be discussed further in Chapter 22.

Land law

Bob buys a house and is registered as its proprietor. The purpose of land registration is to prevent fraud by ensuring that it is possible to identify who owns the title to a piece of land. Terry contributes half the purchase price of the house. If Bob sells the house, few would wish to dispute that half the sale proceeds legitimately belong to Terry. A strict adherence to the law would mean that Bob, despite having benefited from protection against fraud, is nevertheless able to deny Terry his entitlement. This is known as a trust, and will be discussed further in Part 2.

Succession

Bob writes a will leaving his artwork to Terry. This obligation is imposed on Terry who has a duty to transfer Bob's artwork to June and not to keep it for himself. If Terry does not transfer the artwork to June, Terry would be in breach of the promise made to Bob. This is another example of the trust in operation.

In all these examples, what we see is that a mechanism is needed to ensure that the law is not applied in such a way as to thwart its own objectives. In England and Wales, and in other jurisdictions whose legal system has evolved from the common law, the mechanism that achieves this is equity. However, in the same way as legal rules have evolved over time, so too have equity's rules and, as will be shown in later chapters of this book, equity, like the common law has also developed formal relationships with clearly defined parties, and does not exist solely as a means of remedying unconscionable conduct and recognising a person's legitimate expectations of entitlement to property. Accordingly, rather than seeing equity as a mechanism that addresses individual injustice, instead it should be viewed as a complementary system of rules that permits the law to operate effectively.

Historically, equity was administered separately from the common law (see Chapter 2), and this may cause it to be perceived as being separate from the law. It is more accurate

however to view equity as being a part of the law that employs the principles of law in a modified way when the circumstances of a situation require it. Accordingly, equity tends not to contradict the law. Instead it develops solutions within the existing legal framework. A particularly clear example of this may be seen in the context of land. The legal framework of land ownership is one whereby the legal owner of an estate in land is identified either on the deeds or on the Land Register. Equity does not contradict this. Instead, equity recognises that this framework is appropriate in the vast majority of cases and that those who wish to acquire an interest in land should take responsibility for recording that entitlement in the manner required by the Land Registration Act 2002.[6] In essence therefore, equity does not intervene where a person should take the expected steps to safeguard his or her own interests. However, where circumstances dictate such as a contribution to purchase or an assurance that another's entitlement will be recognised, equity intervenes by identifying that the legal owner owns the land for the benefit of another person.

Because equity operates in this way, by declaring the legal owner of property to own it for the benefit of the person who has established an entitlement, equity is said to act on the conscience of the wrongdoer, as is explained in an early authority on the role of equity; the *Earl of Oxford's Case*.[7] What this means is that whereas third parties who have no reason to be aware of a person's legitimate expectation of entitlement may deal with the owner as though he were the absolute owner, the owner's conscience is affected in such a way that requires him to acknowledge his obligation. In other words, one person will be the legal owner of property but will own it for the benefit of the 'rightful' owner.

To return to the example considered earlier in this chapter, Ned buys a present for Jed (let us say it is a watch) using Ted and Fred's money. Ned is regarded as the owner of the watch in law – the contract for the sale and purchase of the watch was concluded between the jeweller and Ned and title to the watch was transferred from the jeweller to Ned. Equity does not intervene with this. However, equity acknowledges that the rightful owners of the watch are Ned, Ted and Fred – it is their money that has been pooled and then used by Ned to buy the watch. Therefore Ned owns the watch for the benefit of himself, Ted and Fred. Ted and Fred's entitlement therefore is said to be on Ned's conscience, meaning that an obligation is owed by Ned, but does not affect the contractual relationship that exists between Ned and the jeweller, the latter of whom owes no obligation to Fred and Ted, and has no responsibility arising from the fact that he has received Fred and Ted's money in payment for the watch. Equity's role in affecting the conscience of the wrongdoer is explained in the case of *Westdeutsche Landesbank Girozentrale v Islington London Borough Council* [1996] 2 All ER 961.

EXTRACT

Westdeutsche Landesbank Girozentrale v Islington London Borough Council [1996] 2 All ER 961

Case facts

This case is concerned with what is known as an interest rate swop. The parties agree to what is in effect a hypothetical loan. They agree on a sum of money that is to be loaned, but no actual

[6] (2002 c.9).
[7] *Earl of Oxford's Case* (1615) 1 Ch Rep 7.

money changes hands. However, the parties also agree that the purported borrower will pay interest on that loan at a fixed rate. The interest on the fictional loan is paid to the lender. The lender agrees to pay interest on the loan to the purported borrower. This is paid at a variable rate. Swops are a useful way of spreading the risk of liability. Such transactions became very popular with local authorities, because they were thought to be without significant risk. It was later decided that these transactions were *ultra vires*, i.e. beyond the powers of the local authorities. The other party to the transaction, the variable rate interest payer (who was effectively a lender), therefore sought to recover the money that had been paid to the local authorities. Although it would seem that this is a straightforward problem (the local authority had borrowed money as a result of a transaction that was void because the authority had no power to enter into it), with a straightforward solution (the local authority should repay that money to the lender), the House of Lords discovered that the case was more problematic than had initially been assumed. The first problem was that the law of restitution, i.e. of putting the parties back in the situation in which they would have been had the transaction not occurred, only applied where there had been a total failure of consideration. In this case however, the local authority had given consideration for the money it had received. Secondly, even though the transaction was void, the local authority could be recognised as a trustee of the money. Thirdly, the law as regards interest payments was unsatisfactory. The issue for their Lordships to consider therefore was whether Islington Borough Council had to repay the money it had received from Westdeutsche Landesbank Girozentrale. In general, the discussion centred around the finding of an authority that would allow the House of Lords to order the money to be repaid, as it was conceded it ought to be, and whether the interest should be calculated on a simple basis or on a compound basis. However, their Lordships also engaged in a discussion of what equity's role was.

Lord Goff of Chieveley

Equitable proprietary claims

Ever since the law of restitution began . . . , the role of equitable proprietary claims in the law of restitution has been found to be a matter of great difficulty. The legitimate ambition of restitution lawyers has been to establish a coherent law of restitution . . . Equity lawyers, on the other hand, have displayed anxiety that in this process the equitable principles underlying these institutions may become illegitimately distorted; and though equity lawyers in this country are nowadays much more sympathetic than they have been in the past towards the need to develop a coherent law of restitution, and to identify the proper role of the trust within that rubric of the law, they remain concerned that the trust concept should not be distorted, and also that the practical consequences of its imposition should be fully appreciated. There is therefore some tension between the aims and perceptions of these two groups of lawyers, which has manifested itself in relation to the matters under consideration in the present case.

In the present case, however, it is not the function of your Lordships' House to rewrite the agenda for the law of restitution, nor even to identify the role of equitable proprietary claims in that part of the law. The judicial process is neither designed for, nor properly directed towards, such objectives. The function of your Lordships' House is simply to decide the questions at issue before it in the present case . . . I myself incline to the opinion that a personal claim in restitution would not indirectly enforce the *ultra vires* contract, for such an action would be unaffected by any of the contractual terms governing the borrowing, and moreover would be subject (where appropriate) to any available restitutionary defences. If my present opinion were to prove to be correct then *Sinclair v. Brougham* [1914] A.C. 398 will fade into history. If not, then recourse can at least be had to *Sinclair v. Brougham* as authority for the proposition that, in such circumstances, the lender should not be without a remedy. Indeed,

I cannot think that English law, or equity, is so impoverished as to be incapable of providing relief in such circumstances . . .

I shall begin by expressing two preliminary thoughts. The first is that, where the jurisdiction of the court derives from common law or equity, and is designed to do justice in cases which come before the courts, it is startling to be faced by an argument that the jurisdiction is so restricted as to prevent the courts from doing justice. Jurisdiction of that kind should as a matter of principle be as broad as possible, to enable justice to be done wherever necessary; and the relevant limits should be found not in the scope of the jurisdiction but in the manner of its exercise as the principles are worked out from case to case. Second, I find it equally startling to find that the jurisdiction is said to be limited to certain specific categories of case. Where jurisdiction is founded on a principle of justice, I would expect that the categories of case where it is exercised should be regarded not as occupying the whole field but rather as emanations of the principle, so that the possibility of the jurisdiction being extended to other categories of case is not foreclosed . . .

I turn next to the question whether the equitable jurisdiction can be exercised in aid of common law remedies such as, for example, a personal remedy in restitution, to repair the deficiencies of the common law. Here I turn at once to Snell's Equity, 29th ed. (1990), p. 28, where the first maxim of equity is stated to be that 'Equity will not suffer a wrong to be without a remedy.' The commentary on this maxim in the text reads:

> 'The idea expressed in this maxim is that no wrong should be allowed to go unredressed if it is capable of being remedied by courts of justice, and this really underlies the whole jurisdiction of equity. As already explained, the common law courts failed to remedy many undoubted wrongs, and this failure led to the establishment of the Court of Chancery. But is must not be supposed that every moral wrong was redressed by the Court of Chancery. The maxim must be taken as referring to rights which are suitable for judicial enforcement, but were not enforced at common law owing to some technical defect.'

The question which arises in the present case is whether, in the exercise of equity's auxiliary jurisdiction, the equitable jurisdiction to award compound interest may be exercised to enable a plaintiff to obtain full justice in a personal action of restitution at common law.

I start with the position that the common law remedy is, in a case such as the present, plainly inadequate, in that there is no power to award compound interest at common law and that without that power the common law remedy is incomplete. The situation is therefore no different from that in which, in the absence of jurisdiction at common law to order discovery, equity stepped in to enable justice to be done in common law actions by ordering the defendant to make discovery on oath. The only difference between the two cases is that, whereas the equitable jurisdiction to order discovery in aid of common law actions was recognised many years ago, the possibility of the equitable jurisdiction to award compound interest being exercised in aid of common law actions was not addressed until the present case . . .

I therefore ask myself whether there is any reason why the equitable jurisdiction to award compound interest should not be exercised in a case such as the present. I can see none. Take, for example, the case of fraud. It is well established that the equitable jurisdiction may be exercised in cases of fraud. Indeed it is plain that, on the same facts, there may be a remedy both at law and in equity to recover money obtained by fraud: see *Johnson v. The King* [1904] A.C. 817, 822, per Lord Macnaghten. Is it to be said that, if the plaintiff decides to proceed in

equity, compound interest may be awarded; but that if he chooses to proceed in an action at law, no such auxiliary relief will be available to him? I find it difficult to believe that, at the end of the 20th century, our law should be so hidebound by forms of action as to be compelled to reach such a conclusion.

For these reasons I conclude that the equitable jurisdiction to award compound interest may be exercised in the case of personal claims at common law, as it is in equity. Furthermore I am satisfied that, in particular, the equitable jurisdiction may, where appropriate, be exercised in the case of a personal claim in restitution. In reaching that conclusion, I am of the opinion that the decision of Hobhouse J. in *Kleinwort Benson Ltd. v. South Tyneside Metropolitan Borough Council* [1994] 4 All E.R. 972 that the court had no such jurisdiction should not be allowed to stand.

I recognise that, in so holding, the courts would be breaking new ground, and would be extending the equitable jurisdiction to a field where it has not hitherto been exercised. But that cannot of itself be enough to prevent what I see to be a thoroughly desirable extension of the jurisdiction, consistent with its underlying basis that it exists to meet the demands of justice . . . It would be strange indeed if the courts lacked jurisdiction in such a case to ensure that justice could be fully achieved by means of an award of compound interest, where it is appropriate to make such an award, despite the fact that the jurisdiction to award such interest is itself said to rest upon the demands of justice. I am glad not to be forced to hold that English law is so inadequate as to be incapable of achieving such a result. In my opinion the jurisdiction should now be made available, as justice requires, in cases of restitution, to ensure that full justice can be done. The seed is there, but the growth has hitherto been confined within a small area. That growth should now be permitted to spread naturally elsewhere within this newly recognised branch of the law. No genetic engineering is required, only that the warm sun of judicial creativity should exercise its benign influence rather than remain hidden behind the dark clouds of legal history . . .

Lord Browne-Wilkinson

Since drafting this speech I have seen, in draft, the speeches of my noble and learned friends, Lord Goff of Chieveley and Lord Woolf. Both consider that compound interest should be awarded in this case on the grounds that equity can act in aid of the common law and should exercise its jurisdiction to order compound interest in aid of the common law right to recover moneys paid under an *ultra vires* contract.

I fully appreciate the strength of the moral claim of the bank in this case to receive full restitution, including compound interest. But I am unable to accept that it would be right in the circumstances of this case for your Lordships to develop the law in the manner proposed. I take this view for two reasons.

First, Parliament has twice since 1934 considered what interest should be awarded on claims at common law. Both the Act of 1934, section 3(1), and its successor, section 35A of the Act of 1981, make it clear that the Act does not authorise the award of compound interest. However both Acts equally make it clear that they do not impinge on the award of interest in equity. At the time those Acts were passed, and indeed at all times down to the present day, equity has only awarded compound interest in the limited circumstances which I have mentioned. In my judgment, your Lordships would be usurping the function of Parliament if, by expanding the equitable rules for the award of compound interest, this House were now to hold that the court exercising its equitable jurisdiction in aid of the common law can award compound interest which the statutes have expressly not authorised the court to award in exercise of its common law jurisdiction.

Secondly, the arguments relied upon by my noble and learned friends were not advanced by the bank at the hearing. The local authority would have a legitimate ground to feel aggrieved if the case were decided against them on a point which they had had no opportunity to address. Moreover, in my view it would be imprudent to introduce such an important change in the law without this House first having heard full argument upon it. Although I express no concluded view on the points raised, the proposed development of the law bristles with unresolved questions. For example, given that the right to interest is not a right which existed at common law but is solely the creation of statute, would equity in fact be acting in aid of the common law or would it be acting in aid of the legislature? Does the principle that equity acts in aid of the common law apply where there is no concurrent right of action in equity? If not, in the absence of any trust or fiduciary relationship what is the equitable cause of action in this case? What were the policy reasons which led Parliament to provide expressly that only the award of simple interest was authorised? In what circumstances should compound interest be awarded under the proposed expansion of the equitable rules? In the absence of argument on these points it would in my view be imprudent to change the law. Rather, the whole question of the award of compound interest should be looked at again by Parliament so that it can make such changes, if any, as are appropriate.

What we see from these two judgments is that Lord Goff considers that where the common law does not offer an adequate remedy, equity has a continuing obligation to fill that breach. Lord Browne-Wilkinson however takes the view that, although it is morally justifiable for the money to be repaid to the bank with compound interest added, the courts cannot make such an award because statute indicates quite clearly that this is not permissible. Accordingly, Lord Browne-Wilkinson argues that the courts cannot usurp Parliament in this respect, and cannot award a remedy merely because the circumstances of the instant case require it. Lords Browne-Wilkinson, Slynn of Hadley and Lloyd of Berwick allowed the appeal, and therefore it is Lord Browne-Wilkinson's evaluation of equity's role that is upheld as the better law. Nevertheless, the strength of the dissent by Lords Woolf and Goff of Chieveley means that their comments should not be entirely discarded.

ACTIVITY

Group discussion

What do you consider the role of equity to be? Should it exist in order to do justice in individual cases as the circumstances require? What problems might arise from such an approach? Can you think of situations where similar fact cases might be decided differently? Do you consider this to be acceptable? Should equity follow strict principles? What problems might arise from such an approach? Can you think of situations where injustice may arise from similar fact cases being decided in the same way? Sometimes it is too easy to give your own instinctive opinion to such questions. Accordingly, you may find it helpful to allocate one point of view to two 'teams' within the group, and appoint one or more members of the group to be the judge. This will mean that rather then giving your opinion, you will need to convince the judge that the approach adopted by your team is correct, and to expose the weaknesses in the opposing argument. The judge will then have to evaluate each of the arguments presented, and explain why he or she finds them convincing or not convincing, and then give judgment according to which is the stronger answer. You may also wish to find additional sources and materials to support your argument.

In addition to equity's reallocation of property entitlements through the mechanism of the trust, another example of equity's conscience-based intervention is to recognise a broader range

of remedies than damages. Remedies such as the injunction and specific performance recognise the precise nature of a relationship between two specific individuals, and require a wrongdoer to act in accordance with the expectations of that relationship. Consider, for example, the example of conversion from the law of torts. Conversion is the wrongful deprivation of property belonging to another. Accordingly, when Rob steals Vic's car and sells it to Patsy, she may be liable under the tort of conversion because although she has bought the car in good faith from Rob, Rob did not have title to the car to be able to sell it. In this instance, Vic is able to sue Patsy under the tort of conversion, and if Vic is successful, he is able to claim damages from Patsy. The common law remedy of damages is therefore a remedy that may be claimed against anyone into whose hands the goods have fallen.

On the other hand, where Vic and Rob enter into a contract for the sale and purchase of a specific and unique item, the seller Rob will be aware that Vic is contracting with him for that unique item that cannot be acquired by contracting with anyone else. Accordingly, the remedy of specific performance, that is, requiring the contract to be performed according to its terms, may be awarded against Rob instead of damages because specific performance will remedy the dispute between Vic and Rob more effectively.

Today, equity affects all branches of the law, both public and private. The injunction is an equitable remedy, and therefore in administrative law, criminal law and the law of torts, the principles of equity will need to be used. The principles of equity are also central to the law of contract and commercial law, and the resolution of many contractual and commercial problems depends on recourse to equitable remedies and principles. Equity also underpins family relationships and ownership of family property, where the likelihood that expectations of entitlement will arise and the likelihood that consideration for a promise will not be financial, and where it is entirely probable that agreements and arrangements will be concluded without formal records or documents being created are far greater. Equity is therefore an important and useful subject in the study of the law.

Chapter summary

In this chapter an outline was provided of:

- The purpose of equity
- Its relationship with the law
- How equity works.

This chapter will be useful for discussions and assignments touching upon the role and purpose of equity and equity's relationship with the law.

Further reading

Duggan, A.J. (1997) 'Is equity efficient?' 113 *Law Quarterly Review* 601.

Mason, A. (1994) 'The place of equity and equitable remedies in the contemporary common law world' 110 *Law Quarterly Review* 238.

Mason, A. (1997) 'Equity's role in the twentieth century' 8 *King's College Law Journal* 1.

Millett, P. (1995) 'Equity – the road ahead' 9 *Trust Law International* 35

Worthington, S. (2006) *Equity*. 2nd ed. Oxford: Oxford University Press.

2

The evolution of equity

Chapter outline

This chapter will cover:

- The origins of equity
- The formalisation of equity
- The fusion of equity and the common law
- Equitable operations deliberately created
- Incomplete obligations that are equitable in character
- Equity's remedial role
- Equity's relationship with the law
- The context of equity
- The scope of equity to innovate.

Introduction

Understanding how – and indeed why – equity works is perhaps easier when its historical antecedents are explained. The legal historian F.W. Maitland describes equity as '*a gloss on the common law*'.[1] In effect, as was touched upon in Chapter 1, equity developed as a corrective to the common law where a strict application of the common law rules would deny a person an entitlement which the courts considered reasonable for him (rarely her in those days) to expect. As Potter explains in his *Introduction to the History of Equity and its Courts*[2] this presupposes that the common law existed prior to the evolution of equity, and that equity and the common law are facets of a larger entity. Equity therefore exists as an adjunct to the rules of common law, although as will be seen, equity has developed in such a way that equitable obligations may now be created deliberately, and many are even enshrined in statute.

The Provisions of Oxford

Although earlier origins may be identified with some historical analyses going back as far as the ancient Greeks[3] and others identifying origins in principles that existed prior to the Norman Conquest of England,[4] a useful starting point is the Provisions of Oxford 1258. The Normans had conquered England in 1066 and set about establishing a legal system that was common to the entire kingdom, i.e. the common law. By 1258, the foundations of the common law had been established. However, in 1258, the Provisions of Oxford prohibited new forms of legal action from being developed. Therefore claimants had to fit the wrongs they had suffered into the existing forms of legal action. A modern analogy might be to say that if a person is wronged, it is necessary, in order to litigate, to identify that the wrong suffered is for example a breach of contract, or a trespass or a criminal offence or negligence. The difficulty with this was that it left many people without a remedy for wrongs that had befallen them. For example, where a debt had been repaid but the bond that contained evidence of the agreement between the debtor and the creditor had not been cancelled, the common law would not cancel the bond, and would instead require the debt to be repaid again.

Nevertheless, it was possible to petition the king to do justice in individual cases (as justice was felt to be the prerogative of the monarch) – the beginnings of what is recognised today as equity. Over time this function was devolved to the Chancellor, who could decide on what was just in situations where the common law courts did not offer an adequate solution. One feature of this process was that Chancellors decided cases according to their own individual sense of what was right and wrong. Accordingly, what occurred was that similar cases had very different outcomes depending on whether the Chancellor favoured the arguments put forward by the claimant, or those advanced by the defendant. By the time of the Tudor and Stuart monarchs (1485–1660), the Chancellor's role as an individual had evolved into presiding over the Chancery Court, whose function was to hear the anomalous cases that did not fit into the common law's system of writs.

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[1] Holdsworth W.S. (1903) *History of English Law* vol 1. London: Methuen & Co Ltd.
[2] Potter, H. (1931) *An Introduction to the History of Equity and its Courts.* London: Sweet and Maxwell, p.1.
[3] Douzinas, C. (2000) *The end of Human Rights.* Oxford: Hart.
[4] Maitland, F.W. (1936) *Equity – A Course of Lectures.* 2nd ed. Cambridge: Cambridge University Press.

Conflict of common law and equity

A particular difficulty arose where there was conflict between common law and equity. Which was to take precedence? On the one hand, the Court of Chancery did not alter legal entitlements. Therefore if a person was the legal owner of property at law, equity did not intervene in that, although the Chancellor could decree that the owner owned the property for the benefit of another person (an approach that evolved into the concept of the trust). It would appear therefore that the common law should take precedence over equity. This was problematic however in situations where a common law court had given judgment in favour of the claimant, but it was successfully argued before the Court of Chancery that this had been obtained by oppressive or unconscionable conduct. Accordingly, the Court of Chancery would issue an injunction preventing the victorious claimant from enforcing his judgment against the defendant. In *The Earl of Oxford's Case* (1815) 1 Ch Rep 1 therefore, the issue to be decided was which court's judgment was to take precedence. In essence, should the Court of Chancery be permitted effectively to overturn the common law court's judgment? It was concluded that in such circumstances, equity should take precedence over the common law.

EXTRACT

The Earl of Oxford's Case (1815) 1 Ch Rep 1

The Law of God speaks for the Plaintiff. And Equity and good Conscience speak wholly for him. Nor does the Law of the Land speak against him. But that and Equity ought to join Hand in Hand, in moderating and restraining all Extremities and Hardships. By the Law of God, He that builds a House ought to dwell in it; and he that plants a Vineyard ought to gather the Grapes thereof; and it was a Curse upon the Wicked, that they should build Houses and not dwell in them, and plant Vineyards and not gather the Grapes thereof. And yet here in this Case, such is the Conscience of the Doctor, the Defendant, That he would have the Houses, Gardens and Orchards, which he neither built nor planted: But the Chancellors have always corrected such corrupt Consciences, and caused them to render quid pro quo; for the Common Law it self will admit no Contract to be good without quid pro quo, or Land to pass without a-valuable Consideration, and therefore Equity must see that a proportionable Satisfaction be made in this Case . . . And (his Lordship) the Plaintiff in this Case only desires to be satisfied of the true Value of the new Building and Planting since the Conveyance, and convenient Allowance for the Purchase. And Equity speaks as the Law of God speaks. But you would silence Equity.

1st. Because you have a Judgment at Law.

2dly. Because that Judgment is upon a Statute-Law.

To which I answer,

First, As a Right in Law cannot die, no more can Equity in Chancery die, and therefore nullus recedat a Cancellaria sine remedio, a. Therefore the Chancery is always open, and although the Term be adjourned the Chancery is not; for Conscience and Equity is always ready to render to every one their Due, and The Chancery is only removable at the Will of the King and Chancellor; and by The Chancellor must give Account to none but only to the King and Parliament. The Cause why there is a Chancery is, for that Mens Actions are so divers and infinite, That it is impossible to make any general Law which may aptly meet with every

particular Act, and not fail in some Circumstances. The Office of the Chancellor is to correct Mens Consciences for Frauds, Breach of Trusts, Wrongs and Oppressions, of what Nature soever they be, and to soften and mollify the Extremity of the Law, which is called Summum Jus. And for the Judgment, &c., Law and Equity are distinct, both in their Courts, their Judges, and the Rules of Justice; and yet they both aim at one and the same End, which is, to do Right; as Justice and Mercy differ in their Effects and Operations, yet both join in the Manifestation of God's Glory. But in this Case, upon the Matter there is no Judgment, but only a Discontinuance of the Suit, which gives no Possession; and altho' to prosecute Law and. Equity together be a Veration; yet voluntarily to attempt the Law in a doubtful Case, and after to resort to Equity, is neither strange nor unreasonable. But take it as a Judgment to all Intents; then I answer, That in this Case there is no Opposition to the Judgment; neither will the Truth or Justice of the Judgment be examined in this Court, nor any Circumstance depending thereupon; but the same is justified and approv'd; and therefore a Judgment is no Let to examine it in Equity, so as all the Truth of the Judgment, &c., be (not) examin'd . . . it appeareth, That when a Judgment is obtained by Oppression, Wrong and a hard Conscience, the Chancellor will frustrate and set it aside, not for any error or Defect in the Judgment, but for the hard Conscience of the Party; and that in such Cases the Judges also play the Chancellors; and that these are not within the Statute 4 H. 4, cap. 23. Which is, That after a Judgment given in the Court of our Sovereign Lord the King, the Parties and their Heirs shall be in Peace, until the Judgment be undone by. Attaint or Error. But secondly, It is objected, That this is a Judgment upon a Statute-Law. To which I answer, It has ever been the Endeavour of all Parliaments to meet with the corrupt Consciences of Men as much as might be, and to supply the Defects of the Law therein, and if this Cause were exhibited to the Parliament it would soon be ordered and determined by Equity; and the Lord Chancellor is, by his Place under his Majesty, to supply that Power until it may be had, in all Matters of Meum and Tuum, between Party and Party; and the Lord Chancellor doth not except to the Statute or the Law (Judgment), upon the Statute, but taketh himself bound to obey that Statute according to 8 Ed. 4, and the Judgment there upon may be just, and the College in this Case may have a good Title in Law, and the Judgment yet standeth in Force . . . Will you then have Equity suppressed in all Cases, where in a Judgment at Law, or upon Statute, is had The Use of the Chancery has been in all Ages to examine Equity in all Cases, saving against the King's Prerogative; and Doctor and Student, then you must have a Special Statute to except the Chancellor. For general Statutes do extend to the particular Usages of all the great Courts at Westminster, especially of the Chancery, and especially for Matters of Equity.

The systemisation of equity

A number of matters contributed to the move away from the ad hoc approach of the mediaeval Chancellors. Firstly, the post of Chancellor came to be regarded more as a judicial role than an ecclesiastical role. The consequence was that whereas the early chancellors were churchmen, this was in decline by the 16th century, and by the 17th century, they were uniformly men who had received legal training. The last non-legally trained Chancellor was Lord Shaftesbury, who was Chancellor until 1682. Accordingly, legally trained Chancellors brought with them the techniques they had learnt in the common law courts – techniques such as recording and following precedents and creating rules that could be applied generally to similar fact situations.

EXTRACT

Winder, W.H.D. (1941) 'Precedent in Equity' *Law Quarterly Review* 245

Before the opening of the eighteenth century precedent was rapidly superseding conscience as the foundation of practical equity. Trevor M.R. declared that a case before him [*Walter* v *Sanders* (1703) 1 Eq Ca Abr 58] was not to be distinguished from *Sir Edward Turner's* 'and be must therefore decree it (though against his conscience) that here might be an uniformity of judgments'. This notion that judicial consistency must be maintained, even at the expense of abstract justice, appears throughout the history of equity. 'The course of the decisions' became, perhaps, the most popular words in which the idea found shape. The phrase is clearly derived from 'course' in such a phrase as 'the course of the Exchequer', *cursus scarrarii*. Thus the records of the Chancery show Bacon. 'knowing the ancient practice and course of the Court of Chancery to be that decrees had been made' with a certain effect, revering a ruling of Lord Ellesmere who had decided the other way [*Barkley* v *Marckwick* (1617) Ritchie 14].

The tendency to rely rather on precedents than on general principles or maxims is strengthened in the eighteenth century. Lord Macclesfield L.C. on one occasion, having taken time to consider his judgment so as to be attended with precedents in the interval, announced that 'since there were no precedents to guide him, be thought the constant maxim of this Court sufficient for this purpose, *viz*. that he who would have equity, or comes here for equity, must do equity' [*Demary* v *Metcalf* (1715) Gilb 104]. His successor, Lord King, adopted the same method in reaching a decision: 'Not having heard any precedent cited in this case, I am therefore to be guided by the reason of the thing, and to prevent a delay of justice [*Morrice* v *Hankey* (1732) 3 P Wms 146].' Lord Cowper L.C. is reported as saying that 'there were no precedents . . . and therefore the Court was at liberty to judge upon the reason of the thing [*Jacobson* v *Williams* (1717) 1 P Wms 382]'. We constantly read in the reports that precedents are ordered to be searched for; sometimes the search is conducted by the Registrar. The search might bring to light unnoticed printed reports or, and this is not uncommon, cases only to be found recorded in the Registrar's Books. The Chancellors were not to be deterred by the scarcity of printed reports from an adoption of the case-law system. Cases existing only in manuscript have played a more important part in legal development in equity then at common law. Precedent had because too strong a characteristic of English law by the seventeenth century for its influence on equity to be dependent merely on the enterprise of law reporters. The supply of Chancery reports lagged for behind the demand. A reference to the Registrar's Books was of more assistance than was, at common law, a consultation of the formal record, for the latter did not hint at the reasons for the judgment recorded. The Registrar's Books, on the other hand, often mentioned briefly the main principle of the decree, after the facts and steps in the suit had been rehearsed. . . .

Precedents accumulated but slowly so that there long continued to be gaps in equity which could be filled only by a novel ruling. A power to decide a matter untouched by authority is distinct from a power to disregard authority already in point. Equity judges continued to exercise the first power freely after the second had become weakened by the demands of judicial consistency. Lord King L.C. in *Exp. Hopkins* [Anon (1728) Moesly 68] found it sufficient that he did 'not see any precedent to the contrary', but in an earlier case he had shown himself more cautions: 'As it had never been done in Chancery he would not make a precedent.' In *Challis* v *Casborn* [(1715) Gilb 96] Lord Cowper told counsel that 'unless they could show some precedents he could not assist them', but Lord Northington had complete confidence in his own judgment and no doubts about his power to act on it: 'I have not the least doubt on this case; and if there is no precedent of such a determination as I shall make. I have no scruples to make one, and shall glory in doing it . . . I lay down this rule . . .' [*Morris* v *M'Cullock* (1763) Amb 432] Nor did he deprive himself of the credit of being the first to treat religions influence as subject to the

doctrine of undue influence by the thought that the cause was 'the first of the kind that ever came before this Court, and, I may add, before any Court of judicature in this kingdom' [*Norton* v *Relly* (1764) 2 Eden 286]. Arden M.R. felt 'warranted to make a precedent' where a legatee had benefited by a peculiar kind of fraud although the case was 'rather novel in its circumstances, and that scarcely has afforded any decision in the law of England' [*Kennell* v *Abbott* (1797) 4 Ves 804].

Equity has been more ready than the common law to give an affirmative answer in a case *primae impressionism.* However the two systems may compare with regard to the power to overrule or vary precedents, equity has been more willing to supplement them than has the common law. The width of equitable principles has made this easier. For example, Shadwell V.C. said that he would be exceedingly forgetful of his duty as a judge in a Court of equity if he were to say that undue influence were not to be presumed in the relationship of physician and patient, although the point was a novel one. With regard to other relationships involving influence he said: 'I should not require to have quoted to me an exact precedent but I should be guided by the principle on which the Court acts in cases between solicitor and client' [*Dent* v *Bennett* (1835) 7 Sim 539]. But when the same principle was applied for the first time to persons engaged to be married, Langdale M.R. was less certain; it was, for him, 'a case of first impression and one of great difficulty' [*Page* v *Horne* (1848) 11 Beav 227]. though he gave relief, but, he confessed. 'not without considerable doubt'. The unquestioning resolution of Lord Northington, the measured purpose of Shadwell V.-C., and the besitant conclusion of Langdale M.R., in extending the same principle, mark stages in the refusal of equity to allow the silence of precedent to forbid a remedy.

In more modern times Jessel M.R. in the Court of Appeal stated that 'the Court is not afraid of making a precedent when justice will require it' [*MacHenry* v *Lewis* 47 LT 549]. His statement, naturally, cannot be taken as unqualified. He himself held that 'the fact that there is no precedent for such an interference is also a reason for this Court not interfering' in the manner asked of it; he thought the precedent 'would have been discovered a long time ago' if it existed [*Peruvian Guano Co.* v *Bockwoldt* 23 Ch D 225]. It is always difficult to say what is a 'new precedent' and this difficult is greater in equity than at law because of the wider terms in which its doctrines are often laid down. Jessel M.R. could say that 'this case only shows that new cases require, not the application of new law, but the application of old principles of law in a new way; nothing more'. But at a later date he stated: 'The case before me appears, so far as I know, . . . to raise an entirely new point: therefore, according to my mode of dealing with a novel question, I must decide it upon principle; that is, a principle to be extracted from former decisions, from the general rules of the Court, and from the nature of the law' [*Attorney General* v *Wandsworth Board of Works* 6 Ch D 539] [*Freme* v *Clement* 18 Ch D 499]. In *Corporation of London* v *Riggs* [13 Ch D 798] he was forced to admit that 'whatever I may call my decision, it will, in effect. In making law, which I never have any desire to do; but I cannot find that the point is covered by any decided case'. He found satisfaction in the thought that the case would 'in all probability be carried to a higher Court, and it will be for that Court to make the law, or, as we say, declare the law'. The distinction between a new application of an old principle and a new rule is difficult to apply in practice and does not seem to have assisted Jessel M.R. in this case. In the familiar judgment in *Re Hallett* [13 Ch D 696] he pointed out that equity is not supposed to have existed from time immemorial and that many of the rules of equity were invented by Chancellors whom it is possible to name. The creative power of equity judges had not completely ceased by Sir George Jessel's day, as his own derisions show, but perhaps the distinction on which he found he could not in practice rely, has masked this power.

If equity is less insistent on authority if the case is of first impression, it is more insistent if the decision will affect titles, or even settled practice in dealings with property. Cases of this type more frequently arise in Chancery than in other Courts. The caution of a common law judge, later to be Lord Chancellor, that 'the altering settled rules concerning property is the most dangerous way of removing landmarks' [*Goodright* v *Wright* (1717) 1 P Wms 397], has always

been remembered. The following year be renewed his warning: 'Where things are settled and rendered certain, it will not be so material how, as long as they are so, and that all people know how to act' [*Butler* v *Duncomb* (1718) 1 P Wms 448]. 'It is dangerous to alter old-established forms', said Lord Talbot L.C [*Hunter* v *Maccray* (1736) Cases t T 196], a fear which had inspired his judgment in *Att.-Gen.* v *Scott* [(1735) Cases t T 138]: 'For me therefore to do a thing merely upon the authority of an obscene case (*viz. Fletcher* v *Robinson*), which does not seem to have been determined upon that point neither, and might perhaps shake the settlements of five hundred families, is what I cannot answer to my conscience.' He had also formerly said that it was much better to stick to known general rules than to follow any particular precedent as 'such a proceeding would confound all property'. The ordinary rules of case-law must always read subject ot the qualification made in such case as these. Usually this qualification requires stricter obedience to precedent than in other cases, but it does not always work in the same way. It may lead to the disregard of a decision the effect of which is to cast doubt on titles or to unsettle regular practice. It may also lead to a single decision being followed although unsupported by a course of decisions. Thus in *Att.-Gen.* v *Mayor of Bristol* [(1820) 2 Jac & W 294] Lord Eldon declared that the principle of not disturbing settled rules of construction was of so much important that 'if there has been not merely a variety of cases, but even only one ancient case, and there has been practice and experience in favour of it, it ought to be adhered to'. . . .

There is no doubt, however, that the opinion Cotton L.J. held was the minority one and is the minority one at the present day. Since the Judicature Act no distinction seems to have been drawn between appeals on matters of equity and appeals on matters of law, and there is abundant expression of opinion that the Court of Appeal is bound by its own single decision. If it was right to say that it was strictly bound by a decision of the Court of Exchequer Chamber, it was a short step to say that it was self-bound in matters of common law. As it was not always strictly bound, according to the weight of opinion, by a decision of the Court of Appeal in Chancery, the step is a longer one when matters formerly dealt with in that Court are in issue. The common law example may have made this step an easier one to take. But the ever-increasing respect paid by equity to the single precedent, as distinct from the course of the decisions, may have led to this development in any event, though it is not going too far to say that the passing of the Judicature Act accelerated it. But for that reform, certain exceptions to the strict rule of case-law, particularly the exception of the recent decision, might have become clearly defined and candidly accepte d. Equity judges have contributed more than Common law judges to modern case-law learning, and it is probably the memory of these contributions which still occasionally leads a member of the Court of Appeal to deny that that Court is universally bound by its own decision. If it is not so bound, the position might well be clarified in the light of the experience gained in the equity cases.

Another important factor is thought to be the development of legal education. Students of law would learn their craft by shadowing and observing practising lawyers. The spread of literacy caused by the development of printing meant that by the 16th century, students began to take notes of what they observed in courts, and of course, these notes were passed around among their peers. This led to judgments being recorded, and a written record of judgments meant that it was easier to be aware of how cases had been decided and thereafter to follow them in later cases. Therefore, by the late 17th century, Potter comments that:

> the reports of cases rapidly improved so that it became possible not merely to say what had been decided, but also the grounds for decision.[5]

[5] Potter, H. (1931) *An Introduction to the History of Equity and its Courts.* London: Sweet and Maxwell, p.1.

By the 19th century, the Chancellor, whose role had evolved into presiding over the Chancery court, was responsible for systematising the administration of equity into a set of rules that were routinely applied in similar fact cases. As Lord Eldon explains in *Gee v Pritchard* (1818) 2 Swan 402 at 414:

> The doctrines . . . ought to be well settled, and made as uniform, almost as those of the common law, laying down fixed principles, but taking care that they are able to be applied according to the circumstances of each case. I cannot agree that the doctrines of this court are to be changed by every succeeding judge.

Cases that came before the Court of Chancery were no longer decided according to an individual Chancellor's moral code. Instead, precedents were followed, and developed into a system of rules that are routinely applied in similar cases. This was the origins of the situation encountered today where awarding equitable remedies such as the injunction or specific performance are not unusual outcomes – indeed they are routinely applied for in both the civil and the criminal courts.

Yet, as shall be demonstrated in later chapters, equity nevertheless retains an element of discretion, in that an equitable remedy will not be granted if the claimant has acted in a manner that is unfair or in some way 'sharp' as regards the defendant in the conduct of the case. Therefore, while the claimant who is seeking damages for breach of contract will be entitled to an award of damages for the breach, the claimant who is applying for a search order in order to conduct a search of the defendant's premises for the evidence that is necessary to proving his or her case is not likely to be permitted to use the material he or she has obtained if full disclosure of the relevant facts had not been made to the court when the application was made.[6]

The fusion of common law and equity

Despite the overlap between equity and the common law, equity was administered from separate courts from the common law, with the result that for example the allegation of a breach of contract would have to be proved in the common law courts, and then the action would have to be recommenced in the Chancery Court if the claimant required the breach to be remedied by an equitable remedy, such as an injunction, rather than damages. This was evidently a cumbersome process – the most engaging illustration of which may be Dickens' description of the Court of Chancery in the opening chapter of his novel *Bleak House*.

EXTRACT

Charles Dickens, *Bleak House*

The raw afternoon is rawest, and the dense fog is densest, and the muddy streets are muddiest near that leaden-headed old obstruction, appropriate ornament for the threshold of a leaden-headed old corporation, Temple Bar. And hard by Temple Bar, in Lincoln's Inn Hall, at the very heart of the fog, sits the Lord High Chancellor in his High Court of Chancery.

[6] *Guess? Inc v Lee Seck Mon* [1987] FSR 125.

> Never can there come fog too thick, never can there come mud and mire too deep, to assort with the groping and floundering condition which this High Court of Chancery, most pestilent of hoary sinners, holds this day in the sight of heaven and earth.
>
> On such an afternoon, if ever, the Lord High Chancellor ought to be sitting here – as here he is – with a foggy glory round his head, softly fenced in with crimson cloth and curtains, addressed by a large advocate with great whiskers, a little voice, and an interminable brief, and outwardly directing his contemplation to the lantern in the roof, where he can see nothing but fog. On such an afternoon some score of members of the High Court of Chancery bar ought to be – as here they are – mistily engaged in one of the ten thousand stages of an endless cause, tripping one another up on slippery precedents, groping knee-deep in technicalities, running their goat-hair and horse-hair warded heads against walls of words and making a pretence of equity with serious faces, as players might. On such an afternoon the various solicitors in the cause, some two or three of whom have inherited it from their fathers, who made a fortune by it, ought to be – as are they not? – ranged in a line, in a long matted well (but you might look in vain for truth at the bottom of it) between the registrar's red table and the silk gowns, with bills, cross-bills, answers, rejoinders, injunctions, affidavits, issues, references to masters, masters' reports, mountains of costly nonsense, piled before them . . . This is the Court of Chancery, which has its decaying houses and its blighted lands in every shire, which has its worn-out lunatic in every madhouse and its dead in every churchyard, which has its ruined suitor with his slipshod heels and threadbare dress borrowing and begging through the round of every man's acquaintance, which gives to monied might the means abundantly of wearying out the right, which so exhausts finances, patience, courage, hope, so overthrows the brain and breaks the heart, that there is not an honourable man among its practitioners who would not give – who does not often give – the warning, 'Suffer any wrong that can be done you rather than come here!'
>
> Who happen to be in the Lord Chancellor's court this murky afternoon besides the Lord Chancellor, the counsel in the cause, two or three counsel who are never in any cause, and the well of solicitors before mentioned? There is the registrar below the judge, in wig and gown; and there are two or three maces, or petty-bags, or privy-purses, or whatever they may be, in legal court suits. These are all yawning, for no crumb of amusement ever falls from JARNDYCE AND JARNDYCE (the cause in hand), which was squeezed dry years upon years ago. The short-hand writers, the reporters of the court, and the reporters of the newspapers invariably decamp with the rest of the regulars when Jarndyce and Jarndyce comes on . . . This scarecrow of a suit has, in course of time, become so complicated that no man alive knows what it means. The parties to it understand it least, but it has been observed that no two Chancery lawyers can talk about it for five minutes without coming to a total disagreement as to all the premises. Innumerable children have been born into the cause; innumerable young people have married into it; innumerable old people have died out of it. Scores of persons have deliriously found themselves made parties in Jarndyce and Jarndyce without knowing how or why; whole families have inherited legendary hatreds with the suit.

Although this work of fiction may dramatise the reality of the Court of Chancery, it nevertheless gives some flavour of the complexity of the 19th century legal system, and why the fact that it was administered from two separate courts with different rules was unsatisfactory.

This was resolved by a series of statutes called the Judicature Acts in 1873–5, which sought to fuse the administration of the common law and equity. This means that today,

all courts have, in principle, the jurisdiction to administer aspects of common law and aspects of equity, and this means that the distinction between law and equity is less clear than in the past. Accordingly, academics and judges dispute the extent to which equity and the common law may be said to have fused as a result of the Judicature Acts.

EXTRACT

A. Mason (1994) 'The Place of Equity in the Contemporary Common Law World' *Law Quarterly Review* 238

VISCOUNT Simonds, it is said, cavilled at the description of equity as an appendix to the common law. His objection was that the description did not do justice to the important corpus of substantive law which the Court of Chancery brought into existence. Had his Lordship survived to witness the developments in equitable doctrine that have taken place since he voiced the objection almost 50 years ago, he would have regarded the description as an utterly misleading statement of equity's place in the scheme of things today, accurate though it may be as an historical explanation of equity before the Judicature Acts . . . What are the reasons for the onward march of equity after the physicians had pronounced it incapable of childbirth? They are, I think, many and varied, some of them not being of general application. Two can readily be identified. First, there were the Judicature Act 1873 (U.K.) and its counterparts in other jurisdictions ('the Judicature Acts'). By providing for the administration of the two systems of law by the one system of courts and by prescribing the paramountcy of equity, the Judicature Acts freed equity from its position on the coat-tails of the common law and positioned it for advances beyond its old frontiers. Secondly, the ecclesiastical natural law foundations of equity, its concern with standards of conscience, fairness, equality and its protection of relationships of trust and confidence, as well as its discretionary approach to the grant of relief, stand in marked contrast to the more rigid formulae applied by the common law and equip it better to meet the needs of the type of liberal democratic society which has evolved in the twentieth century. It is remarkable that the common law has remained for so long impervious to the beguiling charms of equity. More than 100 years elapsed after the introduction of the original Judicature Act before lawyers became receptive to the notion, still regarded as heretical by some Australian commentators, that equity and common law are capable of constituting together a single body of law rather than two separate bodies of law administered together. The belated recognition of this truth by the House of Lords in *United Scientific Holdings Ltd. v. Burnley Borough Council* [[1978] AC 904], particularly Lord Diplock's extreme statement that the waters of the two streams 'have surely mingled now,' has excited exasperation. There is perhaps more merit in Lord Simon of Glaisdale's prediction:

> 'It may take time before the waters of two confluent streams are thoroughly intermixed; but a period has to come when the process is complete.'

Legal reasoning by reference to metaphor is often uninformative and sometimes productive of confusion. Lord Diplock's comment in *United Scientific* is vulnerable to this criticism. It is not at all clear to me what is meant by the mingling of the waters of the two streams and how that mingling, assuming it to have taken place, actually assists us in deciding particular cases. The comment cannot mean that relief by way of damages, awarded according to common law principles, is available in every case where there is a breach or violation of a purely equitable duty or obligation. Nor can it mean that the equitable remedies of specific performance and injunction are more freely available simply because the two bodies of law have, or are thought to have, mingled.

What was fused by the Judicature Acts?

There is one school of thought that adheres to the argument that all that was fused was the administration of common law and equity. In Ashburner's *Principles of Equity*,[7] Browne states:

> But the two streams of jurisdiction though they run in the same channel, run side by side and do not mingle their waters. The distinction between legal and equitable claims – between legal and equitable defences – has not been broken down in any respect by recent legislation.

The essence of this argument is that common law and equity have different origins, and that a common law approach to the resolution of a dispute is completely different from an equitable approach. Accordingly, Browne's view is that common law and equity continue to develop along entirely separate trajectories. Therefore common law concepts such as the law of contract continue to develop according to the common law idea of legal formality, and equitable concepts such as the trust develop according to the more conscience based focus of equity. It means that concepts such as tracing, ownership and mistake have common law and equitable equivalents.

On the other hand, the opposing argument is that there has been more substantive fusion. One exponent of this point of view is Lord Diplock, who states, in *United Scientific Holdings Ltd v Burnley Borough Council* [1978] AC 904 at p910:

> My Lords, if by 'rules of equity' is meant that body of substantive and adjectival law that, prior to 1875, was administered by the Court of Chancery but not by courts of common law, to speak of the rules of equity as being part of the law of England in 1977 is about as meaningful as to speak similarly of the Statutes of Uses or of Quia Emptores. Historically all three have in their time played an important part in the development of the corpus juris into what it is today; but to perpetuate a dichotomy between rules of equity and rules of common law which it was a major purpose of the Supreme Court of Judicature Act 1873 to do away with, is, in my view, conducive to erroneous conclusions as to the ways in which the law of England has developed in the last hundred years.
>
> Your Lordships have been referred to the vivid phrase traceable to the first edition of Ashburner, Principles of Equity where, in speaking in 1902 of the effect of the Supreme Court of Judicature Act he says (p. 23) 'the two streams of jurisdiction' (sc. law and equity) – though they run in the same channel, run side by side and do not mingle their waters.' My Lords, by 1977 this metaphor has in my view become both mischievous and deceptive. The innate conservatism of English lawyers may have made them slow to recognise that by the Supreme Court of Judicature Act 1873 the two systems of substantive and adjectival law formerly administered by courts of law and Courts of Chancery (as well as those administered by courts of admiralty, probate and matrimonial causes), were fused. As at the confluence of the Rhône and Saône, it may be possible for a short distance to discern the source from which each part of the combined stream came, but there comes a point at which this ceases to be possible. If Professor Ashburner's fluvial metaphor is to be retained at all, the waters of the confluent streams of law and equity have surely mingled now.

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[7] Browne, D. (1933) *Ashburner's Principles of Equity.* 2nd ed. London: Butterworth & Co, p.18.

Accordingly, the fusionists would consider that common law principles and equitable principles are intermingled, making equitable remedies for breaches of common law relationships possible, as well as developing separate doctrines such as the trust and the restrictive covenant which have no common law equivalent. What this means is that common law and equity are both component parts of a broader legal system, and that it does not matter what the origins of a concept are.

More recent critics are seen to retreat however from this perspective. In *MCC Proceeds v Lehman Bros International (Europe)* [1998] 4 All ER 675, Mummery LJ explains at p.691:

> In brief, the position is that an equitable owner had no title at common law to sue in conversion, unless he could also show that he had actual possession or an immediate right to possession of the goods claimed; this substantive rule of law was not altered by the Supreme Court of Judicature Acts, which were intended to achieve procedural improvements in the administration of law and equity in all courts, not to transform equitable interests into legal titles or to sweep away altogether the rules of the common law, such as the rule that a plaintiff in an action for conversion must have possession or a right to immediate possession of the goods. The short answer to MCC Proceeds' claim is to be found rooted deep in English legal history: conversion is a common law action and the common law did not recognise the equitable title of the beneficiary under a trust. It recognised only the title of the trustee, as the person normally entitled to immediate possession of the trust property. MCC Proceeds' claim for conversion cannot be maintained, as its predecessor in title, Macmillan, had only an equitable title to the share certificates and the shares.

Accordingly, Pettit[8] adopts a view that lies somewhere between the two extremes, stating:

> Although it is clear that the decision in a case may well depend on an amalgam of rules from both common law and equity, as in *Walsh* v *Lonsdale* (1882) 21 Ch D 9, and although on a broader canvas one may regard the law of real property for instance, as an amalgam of statute, common law and equity, it is accordingly submitted that to talk of the fusion of law and equity is misleading. The facts, inter alia, that the trust has been unaffected, and there is still duality of legal and equitable ownership that in the law of property legal rights and equitable rights, even though for some purposes equivalent as in *Walsh* v *Lonsdale*, may have different effects, for instance as regards third parties, that purely equitable rights can still only be effected by equitable remedies and that the writ ne exeat regno is only available in relation to equitable debt are inconsistent with the idea conveyed by the phrase 'fusion of law and equity'.

Whatever view you consider to be the most convincing, the current situation is that the rules that have their origins in equity are now a part of the legal system of England and Wales. Therefore, equity may be involved in some capacity in many legal relationships and in the resolution of many legal disputes. For example, Alice buys a house that is being sold by Bob and Carole. Bob and Carole, as co-owners, will be in the equitable relationship of the trust in relation to their obligations towards each other as regards the proceeds of sale paid to them by Alice. If Bob and Carole breach the contract with Alice, the equitable remedy of injunction or specific performance (performance of the contract according to its terms) may be more appropriate remedies for Alice. In this scenario, although the transaction operates principally under the common law principles for the

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[8] Pettit, P.H. (2009) *Equity and the Law of Trusts.* 11th ed. Oxford: Oxford University Press, pp.11–12.

formation and operation of a contract, and under the statutory principles relating to conveyancing, there are many instances where rules that have their origin in equity (even though they now have a statutory footing) are involved. Accordingly, whatever one's view of law and equity's substantive fusion within the legal process, it is clear that there is a strong interrelationship between law and equity – although the extent of this continues to be a matter of considerable disagreement.

EXTRACT

Burrows, A. (2002) 'We do this at common law but that in equity' 22(1) *Oxford Journal of Legal Studies* 1

All students of English civil law are aware of, and indeed become accustomed to, the distinction between common law and equity. But the distinction is puzzling . . . I remember thinking, 'What is this mysterious creature equity? How can one have two inconsistent doctrines operating side by side?' . . . I began to think that the explanation for all this was in a crucial lecture or tutorial in the contract course that I had missed or that it was buried in the pages in the texts that I had somehow overlooked. However, it later became clear that my puzzlement was shared by others. When in my own lectures on remedies for breach of contract we turn from contract damages – a common law remedy – to specific performance and injunctions – equitable remedies – I sometimes ask the students, 'What is meant by the labels equitable and common law?' Almost invariably the answer will come back that equitable remedies are concerned to achieve fairness and justice between the parties. To which my standard response is, 'Does that mean that all those rules and principles on damages that we have so far been examining are designed to achieve unfairness and injustice between the parties?' The flustered student may try again, digging himself or herself into a deeper hole, by saying that equitable remedies are discretionary whereas common law remedies are not. However, that does not seem correct either; at the very least, it is highly misleading. Study of the law on damages and specific performance reveals that both rest on a system of rules and principles. It surely cannot seriously be suggested that the law is less certain – that a judge has more discretion – in deciding whether specific performance should be ordered than in deciding, in relation to damages, whether a loss is too remote or whether an intervening cause has broken the chain of causation or whether the claimant has failed in its duty to mitigate its loss. All these decisions involve the application of weak judicial discretion.

By the time I had finished studying law at Oxford I was satisfied that I knew what was meant by common law and equity. This, I had learnt, was historical labelling, going back to the division in the courts, before the Supreme Court of Judicature Acts 1873–5, between the common law courts and the Court of Chancery. To describe a rule or principle as common law was to say that it had its historical roots in the law administered in the common law courts prior to 1873. To describe a rule or principle as equitable was to say that it had its historical roots in the law administered in the Court of Chancery prior to 1873. The effect of the Supreme Court of Judicature Acts 1873–5 was to merge the common law courts and the Court of Chancery into one Supreme Court administering both common law and equity.

Then I took up my first lecturing job at the University of Manchester. There was a course there called 'Equity' and I was required to give seminars. One of the questions on the faculty seminar sheet was the following: 'Are equity and common law fused?' This was not a question we had ever considered in the Oxford trusts course. Certainly, as a new tutor, I was unsure about the answer. Indeed I was not even sure I understood the question. It gave me some confidence to

discover, when I went off to the John Rylands law library to try to find the answer, that many writers also seemed confused.

However, there was one book that stood out. Not that the authors made the question any easier for me to understand but rather because of the vehemence with which they expressed the view that equity and common law are certainly not fused. The book was *Equity, Doctrines and Remedies*, now in its third edition, written by Meagher, Gummow and Lehane. This text condemned the belief that common law and equity are merged as 'the fusion fallacy'. An impression of the vehemence of the authors' views can be gained by citing just a couple of passages from their book.

Those who commit the fusion fallacy announce or assume the creation by the Judicature system of a new body of law containing elements of law and equity but in character quite different from its components. The fallacy is committed explicitly, covertly, and on occasion with apparent inadvertence. But the state of mind of the culprit cannot lessen the evil of the offence.

And then a few paragraphs further on:

[The fusion fallacy] involves the conclusion that the new system was not devised to administer law and equity concurrently but to 'fuse' them into a new body of principles comprising rules neither of law nor of equity but of some new jurisprudence conceived by accident, born by misadventure and nourished by sour but high-minded wetnurses.

Lest it be thought that colourful turns of phrase are confined to those who are anti-fusion, let me balance matters up somewhat by referring to Kit Barker's argument in favour of rationalising the role of the bona fide purchase defence to restitution by fusing common law and equity. With some apology to Lord Atkin, Barker writes that rationality is obstructed 'by the unruly poltergeist which we know as the law/equity divide. These days, even the irreligious are tempted to conclude that only an exorcism of this troublesome ghost will allow us to set our house in order'.

It is, clear, therefore, that the fusion of law and equity is a topic that provokes strong reactions. But the question remains of what, exactly, is meant by fusion . . .

According to the anti-fusion school of thought, the Supreme Court of Judicature Acts 1873–5 fused the administration of the courts but did not fuse the substantive law. Common law and equity sit alongside one another. Moreover, they can happily sit alongside one another. Clashes or conflicts or inconsistencies between them are very rare. Where they exist, and, in so far as they are not resolved by the more specific provisions of the 1873–5 Acts, they are resolved by the general provision in section 11 of the 1873 Act which lays down that 'equity shall prevail'. This is not to say that common law or equity is frozen in the position it was in before 1873. Rather common law and equity can independently develop incrementally . . .

In contrast, the fusion school of thought argues that the fusion of the administration of the courts brought about by the 1873–5 Acts, while not dictating the fusion of the substantive law, rendered this, for the first time, a realistic possibility. While there are areas where common law and equity can happily sit alongside one another, there are many examples of inconsistencies between them. It is important to remove the inconsistencies thereby producing a coherent or harmonised law.

ACTIVITY

The fusion of common law and equity is a common topic either for the purposes of an essay or an examination question. On an online legal database (Lexis/Nexis or Westlaw) look for materials using the keywords **fusion-law-equity**. Think of other key words that might deliver results relating to the fusion debate. Write an essay plan listing the grounds upon which it may be argued that there has been substantive fusion of common law and equity, the grounds upon which the fusion argument may be disputed, and the arguments put forward by those such as Pettit who advocate a hybrid approach. Which of these arguments do you consider to be the stronger? Why do you consider this to be the case?

Contemporary equity

Despite the fusion of the administration of common law and equity by the Judicature Acts 1873–5, equity remains relevant in a number of ways today, and there are many ways in which equity continues to operate in a manner that is distinct from the formalities of the law. Accordingly, the next section of this chapter outlines some of the modern operations of equity. However, as shall be seen, equity and the trust are such broad and flexible concepts that nearly all areas of law may invoke equity in some form.

Equitable operations deliberately created

Although, equity developed as a remedial approach, some equitable relationships these days are deliberately and consciously created. For example if one gives money to a charity or writes a will one is deliberately entering into a relationship known as a trust (of which more in Part 2). The trust forms such a substantial part of equity and trust law that it is not proposed to provide more than a brief outline of the trust here (Parts 2, 3 and 4 are concerned solely with the law of trusts). Essentially however, a trust arises when one person becomes the legal owner of property for the benefit of another. Therefore wills, charitable donations, pensions and the operation of clubs and societies are all examples of situations where the trust, intentionally created, is utilised.

Co-ownership of land uses the trust concept, in that the two or more people named as co-owners will own the land on trust for themselves and the other co-owners. This form of trust, even though it is equitable in character, is defined and regulated by statute. Accordingly, s.34 and s.36 of the Law of Property Act 1925[9] provide that co-ownership of land will operate by virtue of a trust.

[9] (1925 15 & 16 Geo 5 c.15).

EXTRACT

Law of Property Act 1925, s.34 and s.36

34 Effect of future dispositions to tenants in common

(1) An undivided share in land shall not be capable of being created except as provided by the Settled Land Act 1925 or as hereinafter mentioned.

(2) Where, after the commencement of this Act, land is expressed to be conveyed to any persons in undivided shares and those persons are of full age, the conveyance shall (notwithstanding anything to the contrary in this Act) operate as if the land had been expressed to be conveyed to the grantees, or, if there are more than four grantees, to the four first named in the conveyance, as joint tenants [in trust for the persons interested in the land]:

Provided that, where the conveyance is made by way of mortgage the land shall vest in the grantees or such four of them as aforesaid for a term of years absolute (as provided by this Act) as joint tenants subject to cesser on redemption in like manner as if the mortgage money had belonged to them on a joint account, but without prejudice to the beneficial interests in the mortgage money and interest.

(3) A devise bequest or testamentary appointment, coming into operation after the commencement of this Act, of land to two or more persons in undivided shares shall operate as a devise bequest or appointment of the land to the personal representatives of the testator, and (but without prejudice to the rights and powers of the personal representatives for purposes of administration) [in trust for the persons interested in the land].

[(3A) In subsections (2) and (3) of this section references to the persons interested in the land include persons interested as trustees or personal representatives (as well as persons beneficially interested).]

(4) . . .

36 Joint tenancies

(1) Where a legal estate (not being settled land) is beneficially limited to or held in trust for any persons as joint tenants, the same shall be held [in trust], in like manner as if the persons beneficially entitled were tenants in common, but not so as to sever their joint tenancy in equity.

(2) No severance of a joint tenancy of a legal estate, so as to create a tenancy in common in land, shall be permissible, whether by operation of law or otherwise, but this subsection does not affect the right of a joint tenant to release his interest to the other joint tenants, or the right to sever a joint tenancy in an equitable interest whether or not the legal estate is vested in the joint tenants:

Provided that, where a legal estate (not being settled land) is vested in joint tenants beneficially, and any tenant desires to sever the joint tenancy in equity, he shall give to the other joint tenants a notice in writing of such desire or do such other acts or things as would, in the case of personal estate, have been effectual to sever the tenancy in equity, and thereupon [the land shall be held in trust on terms] which would have been requisite for giving effect to the beneficial interests if there had been an actual severance.

[Nothing in this Act affects the right of a survivor of joint tenants, who is solely and beneficially interested, to deal with his legal estate as if it were not held [in trust].]

(3) Without prejudice to the right of a joint tenant to release his interest to the other joint tenants no severance of a mortgage term or trust estate, so as to create a tenancy in common, shall be permissible.

In other words, even though legal ownership of land will identify co-owners as proprietors of the land on the Land Register, this will conceal the fact that the co-owners will act as trustees of the land and the proceeds of the sale of the land, and recognise their respective individual entitlement to the proceeds of sale when the land is sold. This is particularly salient in the case of a tenancy in common. Consider the following situation. Romeo and Juliet contribute to the acquisition cost of buying a house in the following proportions. Romeo contributes 60 per cent of the cost, and Juliet contributes 40 per cent. In law, they will own the house as joint tenants, with the result that if Romeo dies, Juliet becomes the sole owner and is able to sell the house. However, in equity, Romeo and Juliet may choose whether to own the house as joint tenants or as tenants in common. If they are joint tenants, then on Romeo's death, Juliet becomes the sole owner, and now owns the house for her own benefit. If Romeo and Juliet are tenants in common however, on Romeo's death his 60 per cent share of the house belongs to those who will inherit under his will or intestacy. Juliet is the sole owner of the house in law, but she owns the house for the benefit of herself (in relation to her 40 per cent share) and the beneficiaries under Romeo's will or intestacy (in relation to Romeo's 60 per cent share).

Some types of trust arise out of necessity when people enter into certain types of relationship. Co-ownership is one such example. Co-ownership of land in England and Wales cannot exist without there being a form of trust in existence. Neither can a sale and purchase transaction or a mortgage, insolvency or intestacy (dying without leaving a valid will). These types of trusts are imposed by statute, and are described as 'statutory trusts'.

A person may also deliberately create other forms of equitable obligation. For example, a restrictive covenant over land is a form of equitable relationship that is created deliberately. A restrictive covenant is essentially a contractual restriction imposed by the seller of part of a plot of land, limiting the ways in which the land may be used by the buyer – and subsequent owners of the buyer's land. Section 1(2) of the Law of Property Act 1925 does not include restrictive covenants in the list of interests affecting land that may subsist at law. However, if those who buy the land from the original buyer have notice of the covenant in the form of a charge on the Land Register (where the land is registered) or a Class D(ii) Land Charge (where the land remains unregistered), then the buyer will be required to abide by the terms of the covenant even though he or she is not a party to it. In effect, the covenant is protected because it would be unequitable for the buyer to deny its existence where he or she has bought the land having notice of the covenant.

Incomplete obligations that are equitable in character

The second operation of equity is in its recognition of obligations as equitable when they are incomplete. This is manifested particularly strongly in the context of land. Most transactions involving land are required to be made in the form of a deed and recorded on the Land Register. A deed is defined in s.1(2) of the Law of Property (Miscellaneous Provisions) Act 1989 as not being a deed unless:

(a) it makes it clear on its face that it is intended to be a deed by the person making it or, as the case may be, by the parties to it (whether by describing itself as a deed or expressing itself to be executed or signed as a deed or otherwise); and

(b) it is validly executed as a deed.

Being validly executed as a deed means that it is signed by the person making it in the presence of a witness who attests the signature. In reality however, this does not always occur. Although there are some instances of this being attributable to professional negligence on the part of a solicitor, more commonly it is because real people do not govern their lives in accordance with the law's expectations. In law therefore, no valid

relationship subsists. However, equity may intervene in order to give effect to a contractual relationship, even though that relationship has not been formalised by a deed.

EXAMPLE

Max and Minnie are students. In April they sign a lease for a flat in which they will live during their second year at university. They intend to move into the flat the following October, at the start of the new academic year. Schedule 3 to the Land Registration Act 2002 requires that this lease is registered on the Land Register. Max and Minnie are not aware of this. Equity however acknowledges the existence of this lease between Max and Minnie and their landlord because of the contract between them. Accordingly, equity treats the lease as being valid, by perfecting the imperfect obligation created by the unregistered contractual relationship. They are able therefore to sue the landlord if he breaches the terms of the lease. However Max and Minnie's lease is not a full legal obligation and therefore if Max and Minnie's landlord sells the flat before Max and Minnie move in, the new owner of the flat would have no obligation to Max and Minnie. The rationale behind this is that equity recognises that the landlord owes a promise to Max and Minnie, but does not extend the obligation to people who have no reason to be aware of Max and Minnie's lease.

The idea is that equity is used to give effect to a contractual obligation because otherwise the law of contract would be undermined. However, it cannot recognise the obligation as a matter of law because the formalities required by the law have not been fulfilled. The nature of these incomplete obligations is that they are personal in character. In other words, like the contract, or the agreement from which the obligation originates, the law only enforces the obligation against those who are directly party to it and those in relation to whom it would be inequitable to deny the existence of the obligation.

Equity similarly corrects mortgages, easements and conveyances that are either created by contract and then entered on the Land Register, or more rarely, those that are either created by deed but not registered or those that are neither created by deed nor registered (although, in the latter two cases they may only be enforced against those parties who created the obligation and those who have not given valuable consideration – Land Registration Act 2002, s.30).

Equity as a remedial approach

The third way in which equity is used in modern situations is as a remedy. Here an equitable relationship is constructed by the courts in order to enable the court to remedy an unjust deprivation of an entitlement owed by one person to another. For example, if Romeo moves into Juliet's house, they may apply to amend the Land Register, so that Romeo and Juliet are both registered as the legal owners of that which was formerly Juliet's house. However, if they do not do this, and merely treat the house as 'theirs' and come to an arrangement whereby both of them contribute to the mortgage repayments, the court may construe Juliet's ownership of the home as being for the benefit of Romeo and Juliet as a couple, and divide the proceeds of the sale of the house according to how it construes the parties' intentions. This is called a constructive trust, and will be discussed further in Chapter 14.

Further examples of a trust being construed in order to remedy a person's unjust deprivation of that which he had a legitimate expectation to believe he was entitled to receive, may be seen with the recognition of a trust as a solution to a problem. For example, if Dai creates a trust from which no one will benefit, the law will not permit the trustee to keep the trust property for him- or herself, and the trust property reverts back to Dai, or if Dai is dead, the property will revert back to Dai's estate.

Apart from the trust, equity is also used extensively in the awarding of equitable remedies, and equitable remedies such as the injunction, specific performance and rescission are commonplace remedies used across all areas of the law where damages would be inappropriate in the sense that damages do not adequately address and resolve the claimant's grievance against the defendant. Accordingly, equity has developed remedies such as requiring a contract to be performed strictly in accordance with its terms (known as specific performance) rather than awarding damages. This is particularly useful when the item contracted for is unique, such as land. The injunction is used to compel or to restrain particular conduct, and may again be more useful than remedies where the wrong committed by the defendant is ongoing. These remedies will be discussed further in Chapter 6 but equity's remedies represent a further way in which equity is used as a means of resolving a dispute rather than being a purposely created obligation.

Equity's relationship with the law

Since the Judicature Acts therefore, equity's relationship with statute law and common law has become easier to understand in practice because it is a particular method of approaching legal problems. On the other hand, it has become more difficult to define in that its relationship with the law is difficult to classify because sometimes equity operates separately from the law (as in the situation of the restrictive covenant), sometimes it provides an equitable equivalent of a legal right, and sometimes it operates to provide a remedy to a legal problem.

In essence, equity and the law are interrelated, so that the modern legal system in England and Wales consists of an amalgamation of law and equity. Accordingly, equitable principles are contained in statute, such as for example in the law relating to charities (governed by the Charities Act 2011),[10] and the recognition of trusts relating to land (governed by the Law of Property Act 1925[11] and the Trusts of Land and Appointment of Trustees Act 1996).[12] Furthermore, equity is not separate from the operation of the court system – the same rules and procedures apply in relation to claims that have their origins in law and claims that have their origins in equity. Equitable remedies may be seen as being within the range of remedies offered by the courts and therefore, in an action for breach of contract for example, the court may choose whether an award of damages at common law, or specific performance or rescission in equity, is the most appropriate remedy. In this respect, because they are no longer operated from different courts, identifying what is law and what is equity is sometimes less clear than was historically the case.

On the other hand, there are a number of ways in which law and equity maintain a sense of separateness. For example, legal and equitable entitlements may arise simultaneously in relation to property. For example, land may have a legal owner and an equitable owner who may be different persons. Also, in relation to land, there are a number of interests that have only equitable status, and are only recognised provided that the buyer has notice (usually in the Land Register) of their existence. Furthermore, equitable remedies operate differently from legal remedies, in that whereas a legal remedy is available as a matter of right where there has been a breach of an obligation, an equitable remedy is discretionary, and may be refused where the claimant has acted unfairly towards the defendant. Legal and equitable obligations are often more easily identified in practice, but difficult to define in theory.

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[10] (2011 c.25).
[11] (1925 15 & 15 Geo 5 c.15).
[12] (1996 c.47).

Legal obligations	Equitable obligations
Contract for sale and purchase of chocolate bar	Contract for sale and purchase of land
Right of way created by deed and entered on the Land Register	Right of way created by contract but entered on the Land Register
A gives £100 to B and tells B to keep it for himself	A gives £100 to B and tells B to keep it until C is 18, and then give it to C

In each of these situations, the legal obligation is characterised by there being no further formalities required. In relation to the equitable obligations, an obligation has been created by virtue of the contract, but the person in whom the responsibility is vested owes further obligation, or has made some form of gain from the situation. If so, then there is likely to be an equitable obligation in existence.

The context of equity

Because equity is such a central part of the operation of law, it is used in all spheres of the law. Perhaps it is accurate to say that its origins have focused on the significance of equity and trusts in the context of family and philanthropy, and therefore the earliest usages of equity were aimed at safeguarding family property, and for the purposes of permitting charitable objects to benefit from property. However, the modern concept of equity and the trust is used in a vast range of contexts, such as:

- pensions
- membership of clubs, societies and other associations
- a company director's use of company funds
- individual bankruptcy
- companies in administration
- wills
- intestacy
- co-ownership of the family home
- providing for family members
- giving donations to charities
- erecting memorials
- maintenance of a pet
- saying prayers
- goods ordered from mail order companies
- unit trusts
- investment trusts
- protecting assets from creditors
- facilitating commercial transactions
- avoidance or minimisation of tax
- mortgages (commercial and domestic)
- co-ownership

- restrictive covenants
- land usages created by contract
- land usages that are not recorded on the Land Register
- specific performance of contracts
- estoppel
- mistake
- tracing assets that have been stolen, converted or trespassed upon
- preventing unacceptable activity
- finding evidence in cases where it is alleged that counterfeit goods are being produced.

Modern equity is therefore a concept that is extremely broad in its spheres of engagement and it is probable that many – if not most – areas of the law in England and Wales would not operate as they do if equity did not exist.

EXTRACT

Mason, A. (1994) 'The Place of Equity and Equitable Remedies in the Contemporary Common Law World' *Law Quarterly Review* 238

Equitable doctrines and relief have extended beyond old boundaries into new territory where no Lord Chancellor's foot has previously left its imprint. In the field of public law, equitable relief in the form of the declaration and the injunction have played a critical part in shaping modern administrative law which, from its earliest days, has mirrored the way in which equity has regulated the exercise of fiduciary powers. Equitable doctrine and relief have penetrated the citadels of business and commerce, long thought, at least by common lawyers, to be immune from the intrusion of such alien principles. Equity, by its intervention in commerce, has subjected the participants in commercial transactions, where appropriate, to the higher standards of conduct for which it is noted and has exposed the participants to the advantages and detriments of relief *in rem*.

A similar effect has been achieved by resurrecting and expanding the traditional concept of unconscionable conduct as a basis for relief and recognising that the constructive trust is both an institution and a remedy. The concept of unconscionable conduct, along with the recognition of unjust enrichment which is partly a derivative of unconscionable conduct, has been the source of the recent rejuvenation of equity. Moreover, in the reshaping of branches of the law which straddle both common law and equity which has resulted in greater unity of principle, we have discovered that equity and the common law share much in common. The notion of unconscionability underlies some common law doctrines as well as equity. Estoppel and restitution are examples which come to mind. Here the interaction between common law and equity has resulted in dynamic development of legal principle, resulting in greater symmetry. Equity and common law now import from each other, just as they can and do import from other systems of law and learning.

In some fields of law, equitable concepts and doctrines have been given an expanded operation by statute. Remedial statutes designed to protect a vulnerable class of persons, *e.g.* borrowers and consumers, often provide for relief against onerous transactions which have an element about them of what is harsh and unconscionable. It very often happens that statutory recognition and extension of the equitable ground for relief sparks off further development of the basic equitable concept or doctrine.

ACTIVITY

Consider a situation where you have owned or given something for the benefit of another person. Have you ever been the treasurer of a club or society? Have you ever raised money for a charitable cause or given money to a charity? Have you ever collected money from friends or siblings to buy a relative or a friend a present? Do you own a house or a flat? Do you share the ownership of something with someone (a house or an equity and trusts textbook)? Consider why you do not own the item for your own benefit. Why is the other person entitled to it? Is it as a result of a financial contribution? Is it on the basis of an agreement or a promise you have made? Understanding why it may be useful to be able to own something for the benefit of another person helps to understand why the law upholds this type of relationship, and provides remedies when the relationship does not live up to the parties' expectations.

Equity's ability to innovate

Earlier, it was demonstrated that although equity's origins were to decide cases on an individual basis, over time, this had crystallised into a situation where precedents were routinely followed and equitable principles were systematically applied. Nevertheless, this does not mean that equity is unable to innovate. One of the advantages of a common law legal system is that the courts may reinterpret the law according to the requirements of the time, and may apply existing concepts to new situations, as well as, of course, distinguishing and overruling earlier precedents. Thus, neither law nor equity is stuck in time and both are seen to apply their existing principles to new situations.

Accordingly, over the course of the last half-century, equity has been applied in a number of new contexts that had not previously required intervention from the law. For example, by the 1970s, there had been an increase in the number of owner-occupied homes, as well as an increase in the number of people cohabiting. The combination of these two factors meant that people had homes that they wished to retain in the event of their relationship breaking down, and the relationships that did break down were not always able to be dealt with by matrimonial law. So it was equity that intervened, by applying the principle of the trust to the situation, and thus permitting the courts to construe that the legal owner owned their home on trust for themselves and their partner, based on the courts' interpretation of what the parties' discussions and conduct indicated to be their intention.

Another example of equity's ability to adapt existing concepts to new situations is encountered with the development of the freezing injunction and the search order in the 1970s. The High Court may grant an injunction (essentially a court order that either compels or restricts particular behaviour in any circumstance where it is considered '*just and convenient to do so*'). This law is currently contained within s.37(1) of the Senior Courts Act 1981.[13] Accordingly, in the mid-1970s, the courts considered it to be just and convenient to grant two specific new types of injunction. The first of these is a freezing injunction, the purpose of which is to freeze assets belonging to the defendant pending trial in order to ensure that judgment in the claimant's favour is not defeated by the defendants having disposed of or dissipated their assets, or placed them outside the

[13] (1981 c.54).

jurisdiction. The second type of injunction is a search order, which compels the defendant to allow the claimant to enter onto land belonging to the defendant to search for evidence that is material to the claimant's claim. The latter type of injunction is most commonly used in actions where the claimant claims that the defendant has been making counterfeit versions of copyrighted or trademarked goods – the 'pirate' DVD or the fake Rolex watch for example. Here, equity is seen to take an existing concept – that of the injunction – and to use it to resolve problems that may have existed for a long time but which had either not previously been argued effectively or were not considered in terms of being capable of being remedied by the courts.

However, these are situations where the courts have applied an existing concept to a new solution. It is important to emphasise that the courts may not make new law, as Lord Nicholls explains in the case of *In Re Spectrum Plus Ltd (In Liquidation)* [2005] 2 AC 680 at p.697:

> The next point to note is that, broadly stated, the constitutional separation of power between the legislature and the judiciary in this country is that the legislature makes the law, the **courts** administer the law. Parliament makes new law, by enacting statutes having prospective and varying degrees of retrospective effect: see *Wilson v First County Trust Ltd (No 2)* [2004] 1 AC 816, 831–832, para 19. When disputes arise, whether between citizens or between a citizen and the Government, they are to be resolved in accordance with the law, and that is a matter for the judicial arm of the state. In this regard it is for the judiciary to decide what is the law, not the legislature or the executive.

Therefore, over the course of the 20th century, there has been an increasing reluctance to displace the function of Parliament. Accordingly, the courts, even when administering the principles of equity will not depart from the existing law, and neither will they devise new remedies simply because the circumstances of an individual case require it, as Bagnall J explains in *Cowcher v Cowcher* [1972] 1 All ER 943 at p.948:

> Rights of property are not to be determined according to what is reasonable and fair or just in all the circumstances; in particular those rights do not alter on the break-up of a marriage. This proposition was fundamental to the decisions in both cases but was also expressly asserted (*Pettitt v Pettitt* per Lord Reid at p.394, Lord Morris at p.395, Lord Hodson at 402, and Lord Diplock at p.416).
>
> In any individual case the application of these propositions may produce a result which appears unfair. So be it; in my view that is not an injustice. I am convinced that in determining rights, particularly property rights, the only justice that can be attained by mortals, who are fallible and are not omniscient, is justice according to law; the justice which flows from the application of sure and settled principles to proved or admitted facts. So in the field of equity the length of the Chancellor's foot has been measured or is capable of measurement. This does not mean that equity is past child-bearing; simply that its progeny must be legitimate-by precedent out of principle. It is well that this should be so; otherwise no lawyer could safely advise on his client's title and every quarrel would lead to a law suit.

Therefore, as with the rest of the law, equity is not static. It does alter and evolve over time. But it alters within the framework of the legal system's mechanisms of following valid precedents, distinguishing (or very rarely) overruling unsuitable precedents, and not creating new obligations and remedies in a manner that interferes with the legislature's authority to make the law.

Modern equity therefore is both relevant and interesting. It has a wide range of applications, and may be used creatively and innovatively when advancing legal argument. Therefore, despite its long historical antecedents, and extensive usage in the context of Victorian family property law, equity is a modern, flexible and dynamic area of the law.

Chapter summary

This chapter may be useful for assignments and assessments on:

- The historical evolution of equity
- Equity's formalisation and systemisation
- The Judicature Acts 1873–5
- The question of whether common law and equity are fused
- The modern role of equity
- Equity's capacity to innovate
- Equity's relationship with the law.

Further reading

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3

Equity's involvement in other areas of law

Chapter outline

This chapter will cover equity's involvement in:

- The law of contract
- Land law
- Torts and criminal law
- Commercial law
- Company law
- Intellectual property law.

Introduction

Even if you are not currently studying equity and the law of trusts, the concept of equity may still be relevant to you. The objectives of this chapter are twofold therefore. Firstly, it demonstrates that equity is not a subject that is constrained to one university-level module – it is a subject that pervades much of how the law, particularly civil law, operates. Accordingly, it is relevant for students studying equity and trusts as a means of demonstrating the subject's broader significance. However, the chapter aims to outline the ways in which equity may be relevant to other subjects, specifically the law of contract, land law, company law and commercial law. It must be emphasised though that this book does not aim to provide an in-depth discussion of equity's relevance to these subjects, and merely serves as an outline of the ways in which equity's principles may be invoked outside the confines of an equity and trusts module.

Equity in contract law

In general, the law of contract is governed by the common law. However, there are a number of examples of equity's intervention in the law of contract. Lord Denning in particular sought to use equity very extensively in developing solutions to contractual disputes, and although the courts have retreated significantly in recent years from some of the equitable approaches he established, his judgments nevertheless demonstrate that the law of contracts is not entirely divorced from equity's involvement, and therefore estoppel, undue influence and mistake as well as equitable remedies in contract are all governed by equity.

Estoppel

In essence, estoppel serves to prevent a contracting party from reneging on a promise not to enforce his or her strict legal rights in situations where the promisee has relied to his or her detriment on the promisor's assurance. There are numerous forms of estoppel, as Lord Denning explains in *McIlkenny v Chief Constable of the West Midlands* [1980] QB 283:

> For the word 'estoppel' only means stopped . . . It was brought over by the Normans. They used the old French 'estoupail.' That meant a bung or cork by which you stopped something from coming out. It was in common use in our courts when they carried on all their proceedings in Norman-French. Littleton writes in the law-French of his day (15th century) using the words 'pur ceo que le baron est estoppe a dire,' meaning simply that the husband is stopped from saying something.
>
> From that simple origin there has been built up over the centuries in our law a big house with many rooms. It is the house called Estoppel. In Coke's time it was a small house with only three rooms, namely, estoppel by matter of record, by matter in writing, and by matter in pais. But by our time we have so many rooms that we are apt to get confused between them. Estoppel per rem judicatam, issue estoppel, estoppel by deed, estoppel by representation, estoppel by conduct, estoppel by acquiescence, estoppel by election or waiver, estoppel by negligence, promissory estoppel, proprietary estoppel, and goodness knows what else. These several rooms have this much in common: They are all under one roof. Someone is stopped from saying something or other, or doing something or other, or contesting something or other. But each room

> is used differently from the others. If you go into one room, you will find a notice saying, 'Estoppel is only a rule of evidence.' If you go into another room you will find a different notice, 'Estoppel can give rise to a cause of action.' Each room has its own separate notices. It is a mistake to suppose that what you find in one room, you will also find in the others.

Equity has extended the concept of estoppel, and therefore estoppel in equity means that where a person has promised not to enforce their legal rights, and a person has relied on that promise to their detriment, the promisor cannot then change his or her mind and enforce the original agreement. The common law concept of estoppel by representation requires the defendant to provide some form of consideration for the promise. However, in equity the mere fact of there being a promise prevents the claimant from enforcing his or her strict legal rights. This is originally developed in the case of *Hughes v Metropolitan Railway* (1877) 2 App Cas 439, but it is not until the case of *Central London Property Trust Ltd v High Trees House* [1947] KB 130 that the scope of the doctrine is clarified.

EXTRACT

Hughes v Metropolitan Railway Company (1877) 2 App Cas 439

Case facts

The appellants leased a plot of land to the respondents. One of the conditions of the lease was that the appellants could give notice to the respondents to repair the land, and the respondents would have to do this within six months of the notice. In October 1874, the appellants gave the respondents notice to repair. However, soon afterwards, the appellants and the respondents entered into negotiations for the appellants to sell the freehold title to the land to the respondents. By 31 December 1874, the parties had failed to reach any agreement in relation to the sale and purchase transaction, and therefore the respondents undertook the repair work, completing it by 30 June 1875. The appellants sued for forfeiture of the lease on the basis that the notice given in October 1874 required the work to have been completed by April (six months from when the notice was given).

Judgment

Lord O'Hagan

Both parties contemplated as the issue of it a sale of the premises, and of necessity the question of repairs was put out of consideration. No doubt they might have agreed that the negotiation should be, without prejudice to the notice, but they did nothing of the kind. It seems to me quite clear at that time that the forfeiture was not intended to take place during the negotiation, and I incline to agree that the period which had elapsed before the beginning of it, after the notice was given cannot be taken into account, and pieced on to that which elapsed after it had ended, to make up the six months, and complete the default. But it is not necessary to pronounce on this point with a view to our decision. The negotiation continued until December 31, and did not then conclude. The appellant expressly dealt with it as still subsisting, and having refused the offer already made to him, invited another. To his invitation he got no reply, and he proceeded to act upon his notice. I concur with Mellish, LJ, that the proper course would have been to inform the respondents within a reasonable time that, failing to make a new proposal, they should understand the negotiation to have been concluded and the parties subjected to their legal rights. This would have been a reasonable and equitable course, but it was not taken, and the appellant must bear the consequences. I think that the judgment should be affirmed, and the appeal dismissed with costs.

Lord Selborne

As to the effect of the correspondence down to December 31 and for some not definite time afterwards, there is an agreement of both courts that the first two and a half months of the notice, or thereabouts, were waived, and I must say that, looking at the terms of the correspondence, I can see no reasonable room for doubt about it, because the first letter of November 28 1974, says as clearly as possible these two things . . . That is the effect of it, and the accession to that in the subsequent correspondence by the plaintiff is as plain as if he had said in terms: 'I do not require you forthwith to commence the repairs; I am willing to enter into the treaty that you propose; it is not improbable that an arrangement may be made; and, therefore, I agree that the commencement of the repairs may be deferred as you suggest.'

Outcome

Accordingly, the appeal was dismissed. The defendant could not be said to have acted in breach of the lease by not completing the repairs by April 1874.

EXTRACT

Central London Property Trust Ltd v High Trees House Ltd [1947] KB 130

Case facts

In 1937, the claimants leased a block of flats to the defendants. By 1940, because of the outbreak of World War II, only a small number of the flats in the block had been leased, and it became apparent that the defendants were unable to pay the rent. The claimants therefore wrote to the defendants explaining that they were willing to accept rent at a reduced rate. By 1945, all the flats in the block had been leased. However, the defendants continued to pay the rent at the lower rate until September 1945 when the claimants demanded that the rent payments be restored to the higher rate. Furthermore, in order to ascertain whether they could claim the arrears for the lower rate of rent paid between 1940 and 1945, the claimants also claimed that the defendants should pay the higher rate of rent for the final two quarters of 1945.

Denning J

If I were to consider this matter without regard to recent developments in the law, there is no doubt that had the plaintiffs claimed it, they would have been entitled to recover ground rent at the rate of 2,500l a year from the beginning of the term, since the lease under which it was payable was a lease under seal which, according to the old common law, could not be varied by an agreement by parol (whether in writing or not), but only by deed. Equity, however stepped in, and said that if there has been a variation of a deed by a simple contract (which in the case of a lease required to be in writing would have to be evidenced by writing), the courts may give effect to it . . . That equitable doctrine, however, could hardly apply in the present case because the variation here might be said to have been made without consideration. With regard to estoppel, the representation made in relation to reducing the rent, was not a representation of an existing fact. It was a representation, in effect, as to the future, namely, that payment of the rent would not be enforced at the full rate but only at the reduced rate. Such a representation would not give rise to an estoppel, because, as was said in *Jorden v. Money* [[1843–60] All ER Rep 350], a representation as to the future must be embodied as a contract or be nothing.

The courts have not gone so far as to give a cause of action in damages for the breach of such a promise, but they have refused to allow the party making it to act inconsistently with it. It is in that sense, and that sense only, that such a promise gives rise to an estoppel. The decisions are

a natural result of the fusion of law and equity: for the cases of *Hughes v. Metropolitan Ry. Co.* [(1877) 2 App Cas 439], *Birmingham and District Land Co.* v. *London & North Western Ry. Co.* [(1888) 40 Ch D 268] and *Salisbury (Marquess) v. Gilmore* [1942] 2 KB 38, afford a sufficient basis for saying that a party would not be allowed in equity to go back on such a promise. In my opinion, the time has now come for the validity of such a promise to be recognized. The logical consequence, no doubt is that a promise to accept a smaller sum in discharge of a larger sum, if acted upon, is binding notwithstanding the absence of consideration: and if the fusion of law and equity leads to this result, so much the better. I am satisfied that a promise such as that to which I have referred is binding and the only question remaining for my consideration is the scope of the promise in the present case.

Outcome

Denning J concluded that the promise related to the economic conditions prevailing when the promise was made. Accordingly, the reduced rent was all that was payable until 1945 when all the flats were leased, and the appellant could not demand the arrears. Once all the flats had been leased, then the promise came to an end and the obligation to pay the full rent was restored. Therefore, the respondent would have to pay the full rent from the beginning of 1945 onwards.

Equitable estoppel, or promissory estoppel as it came to be known will only arise where there should be a clear and unequivocal representation that strict rights will not be enforced – there should be no other possible way of construing the representation made by the promisor to the promisee. Therefore in *Baird Textiles Holdings v Marks and Spencer PLC* [2002] All ER (Comm) 737, the claim for estoppel failed because there was a lack of certainty regarding what the parties intended. Sir Andrew Morritt VC explains:

> I agree with the conclusion of the judge. The alleged obligation on M & S to acquire garments from Baird is insufficiently certain to found any contractual obligation because there are no objective criteria by which the court could assess what would be reasonable either as to quantity or price. This is not a case in which, the parties having evidently sought to make a contract, the court seeks to uphold its validity by construing the terms to produce certainty. Rather it is a case in which the lack of certainty confirms the absence of any clear evidence of an intention to create legal relations . . . In my view English law, as presently understood, does not enable the creation or recognition by estoppel of an enforceable right of the type and in the circumstances relied on in this case. First it would be necessary for such an obligation to be sufficiently certain to enable the court to give effect to it . . . Second, in my view, the decisions in the three Court of Appeal decisions on which M & S rely do establish that such an enforceable obligation cannot be established by estoppel in the circumstances relied on in this case. This conclusion does not involve the categorisation of estoppels but is a simple application of the principles established by those cases to the obligation relied on in this. I do not consider that any of the dicta in the line of cases relied on by Baird could entitle this court to decline to apply those principles.
>
> Estoppel cannot be used as a cause of action, merely as a defence. Therefore estoppel cannot be relied upon to compel a defendant to enforce a promise, merely as a defence when a claimant alleges that the defendant is acting in breach of a contract in circumstances where the claimant has previously given an assurance that conduct of the type undertaken by the defendant would not breach the contract.
>
> Not only must there be a promise, there must also be detrimental reliance on the promise . . . it that there must be an element that the defendant would not have acted as he had if the claimant had not made the promise.

The characteristics of promissory estoppel therefore are that:

- it may only be used to defend a breach of contract. As Sir Andrew Morritt VC explains, promissory estoppel cannot be used by the claimant as a cause of action. Therefore it cannot be used in order to force the defendant to comply with a promise that has been made, but rather, as a defence when it is alleged that a promise has been broken;
- a promise must have been made by the claimant;
- that has been relied up on by the defendant;
- to his or her detriment.

The final three elements require that there is a clear connection between the claimant's promise and the defendant's reliance. If the defendant's conduct is not attributable to the claimant's promise, or if the defendant acts from a motive other than a reliance on the claimant's promise, then estoppel cannot be relied upon. The nature of the promise in the *High Trees* case was one where the claimant specifically promised not to enforce the contract on its original terms, and the cases where promissory estoppel has been claimed successfully tend to focus on this type of situation – the claimant accepts something that is in some way inferior to that which was bargained for, and then seeks to renege on that promise. In *Ajayi v Briscoe* [1964] 3 All ER 556 for example, there was no evidence that the defendant had relied on the claimant's statement. The case concerned a defendant who had bought a fleet of lorries on hire purchase from the claimant. The defendants had not made the payments by instalments as required by the contract, and argued estoppel when the claimant sued for breach of contract. Although the circumstances of this litigation are relevant to the outcome of the case, in that the defendant did not raise the issue of estoppel at first instance, only on appeal, it was nevertheless discovered that there was no evidence of the defendant having altered his position as a result of the lorries he was buying by instalments being out of service. Accordingly, the defence of estoppel failed.

That which is less clear is the need for the change of position to be detrimental in some way to the defendant. In many cases where the defence of promissory estoppel has succeeded there has been an element of detriment – for example in *Robertson v Minister of Pensions* [1949] 1 KB 227 it was argued that the detriment to the defendant arose from his not obtaining an independent medical opinion because of the reliance on the claimant's promise. In other cases however, it has been specifically stated that detriment is not necessarily required. For example, in *W.J. Alan & Co Ltd v El Nasr Export and Import Co* [1972] 2 QB 189, detriment was not felt to be an essential element, although it is likely that proving detriment on the part of the defendant would strengthen the argument that it would be inequitable for the claimant to rely strictly on his or her rights.

Mistake

Under the law of contract, the common law identifies mistake as a factor that renders the contract void.[1] Therefore if money is paid as a result of a mistake, or if property is not transferred as a result of a mistake, then the common law rules regarding mistake will apply. Furthermore, common law mistake will also apply where there has been misrepresentation on the part of the defendant, and also where it is argued that the nature of the mistake was such that no contract could have been formed.

Equity however has identified a broader range of circumstances as giving rise to mistake, which will render the contract voidable (i.e. valid until rescinded). Therefore, in

[1] *Bell v Lever Brothers Ltd* [1932] AC 161.

cases involving the mistaken representation of the parties' common agreement for example, equity will allow for the rectification of documents that do not accurately reflect the parties' intentions.[2] Equity will also permit mistake to subsist as a defence in applications for specific performance or to recover assets transferred by mistake. Where proprietary estoppel arises, equity will also permit the contract to be voided for mistake. A contract will be voidable for mistake in equity either where there is fraud on the part of one of the contracting parties, or where the contract is in breach of an equitable obligation, as in the case of *Cooper v Phibbs* (1867) LR 2 HL 149.

EXTRACT

Cooper v Phibbs (1867) LR 2 HL 149

A man named Edward Joshua Cooper created a trust out of a plot of land he had inherited from his uncle. The terms of the trust provided that the land would be held for his sons, and his brother's sons. When he died however, he had no sons, and therefore, under the terms of the trust, the land passed to his nephew – also called Edward Cooper. The nephew however did not know that the land was held on trust for him, and therefore presumed that, when Edward Joshua Cooper, his uncle, died, the land had been inherited by his uncle's daughters. Edward Cooper therefore leased the land from his cousins, and only later did he realise that the land he had been leasing actually belonged to him. He therefore brought a claim against his cousins requiring the lease to be delivered up (i.e. cancelled). Edward Joshua Cooper's daughters argued that the fishery had belonged to their father, and that they were therefore entitled to lease it to their cousin, Edward. Although the lease was valid in law, it was void in equity, and could therefore be set aside.

Lord Cranworth

The consequence was, that the present Appellant, when, after the death of his uncle, he entered into the agreement to take a lease of this property, entered into an agreement to take a lease of what was, in truth, his own property – for, in truth, this fishery was bound by the covenant, and belonged to him . . . therefore, he says, I entered into the agreement under a common mistake, and I am entitled to be relieved from the consequence of it . . . It appears to me, therefore, that it is impossible to say that he is not entitled to the relief which he asks, namely, to have the agreement delivered up and the rent repaid.

Lord Westbury

There can be no doubt for a moment, therefore, with regard to the settled principles of equity, that what was given to him in the character of owner in trust for the other persons, and what was acquired by him by virtue of those powers, became also subject to that trust. The result, therefore, is, that all that he acquired by virtue of the parliamentary powers would become subject to the trusts of the settlement of 1827, subject only to the repayment to him by the parties entitled under those trusts of the moneys properly expended by him in acquiring additional rights of fishery, and improving the whole . . . The result, therefore, is, that at the time of the agreement for the lease which it is the object of this Petition to set aside, the parties dealt with one another under a mutual mistake as to their respective rights. The Petitioner did not suppose that he was, what in truth he was, tenant for life of the fishery. The other parties acted upon the impression given to them by their father, that he (their father) was the owner of the

[2] *Joscelyne v Nissen* [1970] 2 QB 86.

fishery, and that the fishery had descended to them . . . but if parties contract under a mutual mistake and misapprehension as to their relative and respective rights, the result is, that that agreement is liable to be set aside as having proceeded upon a common mistake. Now, that was the case with these parties – the Respondents believed themselves to be entitled to the property, the Petitioner believed that he was a stranger to it, the mistake is discovered, and the agreement cannot stand.

But then, when the Appellant comes here to set aside the agreement, an obligation lies upon him so to constitute his suit as to enable a Court of Equity to deal with the whole of the subject-matter, and once for all to dispose of the rights and interests of the parties in the settlement. Now although the agreement was inoperative for the purpose of giving to the Petitioner a valid lease of the property, yet it might operate to this extent, that so far as the Respondents had in equity a lien upon the property, their estates and interests in respect of that lien might be affected by the agreement.

Nevertheless, there has been considerable criticism of the concept of mistake in equity a defined by Lord Denning in the case of *Solle v Butcher* [1950] 1 KB 671 in recent years because of its discretionary character.[3] The reason for this is that the courts have identified that there is no consistency between the precedents regarding when exactly a contract should be voidable in equity – something that is discussed at considerable length in the case of *Great Peace Shipping Ltd v Tsavliris Salvage (International) Ltd* [2003] QB 679.

EXTRACT

Great Peace Shipping Ltd v Tsavliris Salvage (International) Ltd [2002] EWCA Civ 1407

Case facts

A ship called the Cape Providence was severely damaged in the South Indian Ocean. The defendants offered to salvage the ship. However, they discovered that it would take them five or six days to reach the Cape Providence, by which time it would probably be too late to rescue the crew or the cargo. The owners of the Cape Providence then decided that it would be better to find a ship that was nearer to the Cape Providence and ask it to go and rescue the crew and the cargo. The nearest available ship was the Great Peace. Or so it seemed. Unfortunately, the defendants were given the wrong information regarding Great Peace's location, which turned out to be further away from the Cape Providence than had been assumed. Nevertheless, on the basis of this information, the claimants and the defendants entered into a contract whereby the Great Peace would escort the Cape Providence back to shore. However, when the defendants discovered that the Great Peace was not 35 miles away as had been assumed, but was instead 410 miles away, they did not immediately cancel the contract. Instead, they found an alternative ship which was able to rescue the crew of the Cape Providence, and then cancelled the contract with the claimants. The claimants sued for breach of contract. However, the defendants argued that the contract had been concluded by reason of a mistake, rendering it either void at common law or voidable in equity.

[3] Cartwright, J. (2002) 'Common Mistake in Law and Equity' *Law Quarterly Review* 196.

Lord Phillips

The mistake in this case

A mistake can be simply defined as an erroneous belief. Mistakes have relevance in the law of contract in a number of different circumstances. They may prevent the mutuality of agreement that is necessary for the formation of a contract. In order for two parties to conclude a contract binding in law each must agree with the other the terms of the contract . . . It may be that each party mistakenly believes that he has entered into such a contract in circumstances where an objective appraisal of the facts reveals that no agreement has been reached as to the terms of the contract . . . More commonly an objective appraisal of the negotiations between the parties may disclose that they were at cross-purposes, so that no agreement was ever reached. In such a case there will be a mutual mistake in that each party will erroneously believe that the other had agreed to his terms . . . Another type of mistake is that where the parties erroneously spell out their contract in terms which do not give effect to an antecedent agreement that they have reached. Such a mistake can result in rectification of the contract. In the present case the parties were agreed as to the express terms of the contract . . . The mistake relied upon by the defendants is as to an assumption that they claim underlay the terms expressly agreed . . . Thus what we are here concerned with is an allegation of a common mistaken assumption of fact which renders the service that will be provided if the contract is performed in accordance with its terms something different from the performance that the parties contemplated. This is the type of mistake which fell to be considered in *Bell v Lever Bros Ltd* [1932] AC 161. We shall describe it as 'common mistake', although it is often alternatively described as 'mutual mistake'.

Mr Reeder for the defendants puts his case in two alternative ways. First he submits that performance of the contract in the circumstances as they turned out to be would have been fundamentally different from the performance contemplated by the parties, so much so that the effect of the mistake was to deprive the agreement of the consideration underlying it. Under common law, so he submits, the effect of such a mistake is to render the contract void . . .

If the facts of this case do not meet that test, Mr Reeder submits that they none the less give rise to a right of rescission in equity. He submits that such a right arises whenever the parties contract under a common mistake as to a matter that can properly be described as 'fundamental' or 'material' to the agreement in question. Here he draws an analogy with the test for rescission where one party, by innocent misrepresentation, induces the other to enter into a contract-indeed that is one situation where the parties contract under a common mistake. The foundation for this submission *is Solle v Butcher* [1950] 1 KB 671.

Mistake in equity

In *Solle v Butcher* [1950] 1 KB 671 Denning LJ held that a court has an equitable power to set aside a contract that is binding in law on the ground of common mistake. Subsequently, as Lord Denning MR, in *Magee v Pennine Insurance Co Ltd* [1969] 2 QB 507, 514 said of *Bell v Lever Bros Ltd* [1932] AC 161:

> 'I do not propose today to go through the speeches in that case. They have given enough trouble to commentators already. I would say simply this: a common mistake, even on a most fundamental matter, does not make a contract void at law: but it makes it voidable in equity. I analysed the cases in *Solle v Butcher* [1950] 1 KB 671, and I would repeat what I said there, at p 693: "A contract is also liable in equity to be set aside if the parties were under a common misapprehension either as to facts or as to their relative and respective rights, provided that the misapprehension was fundamental and that the party seeking to set it aside was not himself at fault."'

Neither of the other two members of the court in *Magee v Pennine Insurance Co Ltd* cast doubt on *Bell v Lever Bros Ltd*. Each purported to follow it, although reaching different conclusions on the facts. It is axiomatic that there is no room for rescission in equity of a contract which is void. Either Lord Denning MR was purporting to usurp the common law principle in *Bell v Lever Bros Ltd* and replace it with a more flexible principle of equity, or the equitable remedy of rescission that he identified is one that operates in a situation where the mistake is not of such a nature as to avoid the contract. Decisions have, hitherto, proceeded on the basis that the latter is the true position . . . Toulson J has taken a different view. He has concluded that it is not possible to differentiate between the test of mistake identified in *Bell v Lever Bros Ltd* and that advanced by Lord Denning MR as giving rise to the equitable jurisdiction to rescind. He has examined the foundations upon which Lord Denning MR founded his decision in *Solle v Butcher* and found them defective. These are conclusions that we must review. If we agree with them the question will then arise of whether it was open to him, or is open to this court, to rule that the doctrine of common mistake leaves no room for the intervention of equity . . .

A number of cases, albeit a small number, in the course of the last 50 years have purported to follow *Solle v Butcher* [1950] 1 KB 671, yet none of them defines the test of mistake that gives rise to the equitable jurisdiction to rescind in a manner that distinguishes this from the test of a mistake that renders a contract void in law, as identified in *Bell v Lever Bros Ltd* [1932] AC 161. This is, perhaps, not surprising, for Denning LJ, the author of the test in *Solle v Butcher*, set *Bell v Lever Bros Ltd* at nought. It is possible to reconcile *Solle v Butcher* and *Magee v Pennine Insurance Co Ltd* [1969] 2 QB 507 with *Bell v Lever Bros Ltd* only by postulating that there are two categories of mistake, one that renders a contract void at law and one that renders it voidable in equity. Although later cases have proceeded on this basis, it is not possible to identify that proposition in the judgment of any of the three Lords Justices, Denning, Bucknill and Fenton Atkinson, who participated in the majority decisions in the former two cases. Nor, over 50 years, has it proved possible to define satisfactorily two different qualities of mistake, one operating in law and one in equity.

In *Solle v Butcher* Denning LJ identified the requirement of a common misapprehension that was 'fundamental', and that adjective has been used to describe the mistake in those cases which have followed *Solle v Butcher*. We do not find it possible to distinguish, by a process of definition, a mistake which is 'fundamental' from Lord Atkin's mistake as to quality which 'makes the thing [contracted for] essentially different from the thing [that] it was believed to be': [1932] AC 161, 218.

A common factor in *Solle v Butcher* and the cases which have followed it can be identified. The effect of the mistake has been to make the contract a particularly bad bargain for one of the parties. Is there a principle of equity which justifies the court in rescinding a contract where a common mistake has produced this result?

'Equity is . . . a body of rules or principles which form an appendage to the general rules of law, or a gloss upon them. In origin at least, it represents the attempt of the English legal system to meet a problem which confronts all legal systems reaching a certain stage of development. In order to ensure the smooth running of society it is necessary to formulate general rules which work well enough in the majority of cases. Sooner or later, however, cases arise in which, in some unforeseen set of facts, the general rules produce substantial unfairness.' (*Snell's Equity*, 30th ed (2000), para 1–03.)

Thus the premise of equity's intrusion into the effects of the common law is that the common law rule in question is seen in the particular case to work injustice, and for some reason the common law cannot cure itself. But it is difficult to see how that can apply here. Cases of fraud and misrepresentation, and undue influence, are all catered for under other existing and uncontentious equitable rules. We are only concerned with the question whether relief might be given for common mistake in circumstances wider than those stipulated in *Bell v Lever Bros*

Ltd [1932] AC 161. But that, surely, is a question as to where the common law should draw the line; not whether, given the common law rule, it needs to be mitigated by application of some other doctrine. The common law has drawn the line in *Bell v Lever Bros Ltd*. The effect of *Solle v Butcher* [1950] 1 KB 671 is not to supplement or mitigate the common law: it is to say that *Bell v Lever Bros Ltd* was wrongly decided.

Our conclusion is that it is impossible to reconcile *Solle v Butcher* with *Bell v Lever Bros Ltd*. The jurisdiction asserted in the former case has not developed. It has been a fertile source of academic debate, but in practice it has given rise to a handful of cases that have merely emphasised the confusion of this area of our jurisprudence. In paras 110 to 121 of his judgment, Toulson J has demonstrated the extent of that confusion. If coherence is to be restored to this area of our law, it can only be by declaring that there is no jurisdiction to grant rescission of a contract on the ground of common mistake where that contract is valid and enforceable on ordinary principles of contract law . . .

The result in this case

We revert to the question that we left unanswered at paragraph 94. It was unquestionably a common assumption of both parties when the contract was concluded that the two vessels were in sufficiently close proximity to enable the Great Peace to carry out the service that she was engaged to perform. Was the distance between the two vessels so great as to confound that assumption and to render the contractual adventure impossible of performance? If so, the defendants would have an arguable case that the contract was void under the principle in *Bell v Lever Bros Ltd* [1932] AC 161.

Toulson J addressed this issue, at para 56:

> 'Was the Great Peace so far away from the Cape Providence at the time of the contract as to defeat the contractual purpose-or in other words to turn it into something essentially different from that for which the parties bargained? This is a question of fact and degree, but in my view the answer is No. If it had been thought really necessary, the Cape Providence could have altered course so that both vessels were heading toward each other. At a closing speed of 19 knots, it would have taken them about 22 hours to meet. A telling point is the reaction of the defendants on learning the true positions of the vessels. They did not want to cancel the agreement until they knew if they could find a nearer vessel to assist. Evidently the defendants did not regard the contract as devoid of purpose, or they would have cancelled at once.' . . .

The parties entered into a binding contract for the hire of the Great Peace. That contract gave the defendants an express right to cancel the contract subject to the obligation to pay the 'cancellation fee' of five days' hire. When they engaged the Nordfarer they cancelled the Great Peace. They became liable in consequence to pay the cancellation fee. There is no injustice in this result.

Outcome

The defendants had acted in breach of a valid contract, which was neither void nor voidable, and were therefore obliged to pay the cancellation fee.

Thus it is seen that the concept of common mistake in equity appears to have disappeared completely, because if the contract is valid in law, then there should be no justification for rendering it voidable in equity, unless there is an element of fraud on the part of the defendant.[4] Accordingly, where the parties are at cross-purposes and each believes they are contracting for something different, then unless the mistake is sufficiently fundamental as to render the entire contract void, the contract will continue to subsist.

[4] Phang, A. (2003) 'Controversy in common mistake' *Conveyancer and Property Lawyer* 247.

On the other hand, where there is an element of culpability on the part of the defendant, the intervention of equity in the doctrine of mistake is justified. However, rather than being categorised as a mistake, this would appear to be more akin to a form of estoppel, whereby the parties are estopped from relying on the operative mistake.

Another example of equity's continued intervention might arise where the mistake could not be rectified at common law. An example of this could be where the subject matter of the contract is also the subject matter of a trust. Consider for example the situation that arose in the case of *Colyer v Clay* (1843) 7 Beav 188. Let us say that Jane enters into a contract with Edward whereby Jane agreed to buy Edward's equitable interest in a house that Tru and Rusty own for the benefit of Edward and Bertha. Jane does not wish to buy the house itself, merely Edward's share of it. Edward and Jane enter into a contract for Edward's share of the house. However, unbeknown to both Edward and Jane, Bertha has died recently, and her share has passed to Edward. If the contract involved property where Edward was its legal owner, there would be no difficulty with finding the contract void at common law. However, because the property is owned by Edward in equity, then the equitable doctrine of mistake must also be relied upon.

EXTRACT

Yeo, T.M. (2005) 'Great Peace: A distant disturbance?' *Law Quarterly Review* 393

GREAT Peace Shipping Ltd v Tsavliris Salvage (International) Ltd [2003] EWCA Civ 1407; [2003] Q.B. 679 (Great Peace) (noted by Reynolds (2003) 119 L.Q.R. 177 and Midwinter (2003) 119 L.Q.R. 180) is notable for purporting to overrule *Solle v Butcher* [1950] 1 K.B. 671, CA and denying the existence of an equitable jurisdiction to set aside contracts made under a fundamental common mistake . . . In principle, where the contract is not void at law, equitable jurisdiction could be invoked when it would be unconscionable for a person to take advantage of legal rights; the problem is in defining the circumstances that amount to unconscionability in specific types of situations. Unconscionable behaviour in the procuring of the formation of agreements has been an ancient and fertile area for equitable intervention, including cases where one party has taken advantage of the mistake of another. The Court of Appeal in *Solle v Butcher* purported to extend the equitable jurisdiction such that, in the absence of blameworthy behaviour of either party at the time of contracting, the court could still rescind the contract on the application of one of the parties on the basis of a common fundamental mistake; it could be unconscionable for a party to insist on strict contractual rights because of the mistake.

The question whether the equitable jurisdiction to set contracts aside for unilateral mistakes has survived Great Peace has not been decided in the English courts, although its continued existence has been assumed: *Huyton SA v Distribuidora Internacional de Productos Agricolas SA de CV* [2003] 2 Lloyd's Rep. 780 and *Harrison v Halliwell Landau* [2004] EWHC 1316.

This is, it is submitted, a right move. While there are legitimate fears that a general power to set aside contracts for common mistake in *Solle v Butcher* involves judicial adjustments of contractually-allocated risks, they may be met by a clearer delineation of what risks lie within or outside contractual allocation . . . and clearer demarcation of the circumstances that amount to unconscionable insistence of legal rights in a contract based on a common fundamental mistake, e.g. where there has been unjust enrichment or serious failure of consideration for which the developing law of restitution has not been able to provide a remedy. Indeed, Great Peace did not close this route off completely; there is residual equitable jurisdiction where there has been (equitable) 'fraud or surprise upon an ignorant party'.

Undue influence

Although the common law recognises duress as a factor that vitiates consent to a contract, equity recognises that undue influence may be equally damaging to the notion of consent. However, the concept of undue influence has tended to rely more specifically on the notion of 'constructive fraud'.[5] It is not necessary to prove fraud in the criminal sense – fraud here means an absence of conscionable conduct, i.e. inducing a promise and then not keeping one's own side of the agreement, or obtaining some advantage in a manner that is regarded as unfair. Therefore a trustee who buys assets from the trust is acting fraudulently even though he or she is acting honestly and with no intention to cause loss. In the law of contract, the doctrine of undue influence has been defined as meaning that one party to the contract uses his or her power over the other to induce him or her to enter into the contract.

Two types of undue influence exist. Firstly, there is actual undue influence, whereby the claimant must prove that the defendant used undue influence in order to persuade the claimant to enter into the contract between the claimant and the defendant. For example, in *In Re Craig* [1971] Ch 95 the claimants sought to set aside a series of gifts made by the deceased before his death on the basis that the donee had exerted undue influence upon him.

The second type of undue influence is presumed undue influence. Presumed undue influence will be relevant where the claimant is induced into entering into a contract, but it is not the defendant who has induced the claimant to enter into the transaction. Instead, the transaction is such that the defendant should have presumed that undue influence was likely, and should therefore have taken steps to ensure that the claimant's consent was freely given. Undue influence will be presumed where the nature of the transaction is such that it does not appear to benefit the claimant, and it is then a matter for the defendant to prove that the transaction was freely entered into. Cases where undue influence has been relied upon are often cases where, for example, Petruchio and Katharina obtain a mortgage of their co-owned home from a bank or a building society. However, when the mortgagee seeks to enter into possession and sell the mortgaged land in order to recover its loan, Katharina argues that it would not have entered into the transaction but for Petruchio's undue influence over her. In *Royal Bank of Scotland v Etridge*,[6] Lord Nicholls explains that undue influence will be presumed where the mortgage is non-commercial in character, and where it does not appear to confer a direct benefit on the claimant. The mortgagee is then put on notice that undue influence is a possibility, and must therefore take steps to ensure that the contract was freely entered into. Where the presumption of undue influence cannot be rebutted by the defendant, the contract will be set aside as being inequitable.

EXTRACT

Royal Bank of Scotland v Etridge (No 2) [2001] UKHL 44

Case facts

This case concerned a number of appeals on a similar issue, namely that a mortgage was obtained in relation to a co-owned home in order to provide a loan for a company with which

[5] *Nocton v Lord Ashburton* [1914] AC 932.
[6] [2001] UKHL 44.

one of the co-owners (but not the other) was involved. The loan was not repaid, and the mortgagees sought to enter into possession in order to sell the land. The co-owner then argued that the transaction was procured as a result of her spouse's undue influence.

Lord Nicholls

Undue influence is one of the grounds of relief developed by the courts of equity as a court of conscience. The objective is to ensure that the influence of one person over another is not abused. In everyday life people constantly seek to influence the decisions of others. They seek to persuade those with whom they are dealing to enter into transactions, whether great or small. The law has set limits to the means properly employable for this purpose. To this end the common law developed a principle of duress. Originally this was narrow in its scope, restricted to the more blatant forms of physical coercion, such as personal violence. Here, as elsewhere in the law, equity supplemented the common law. Equity extended the reach of the law to other unacceptable forms of persuasion. The law will investigate the manner in which the intention to enter into the transaction was secured: 'how the intention was produced', in the oft repeated words of Lord Eldon LC, from as long ago as 1807 (*Huguenin v Baseley* 14 Ves 273, 300). If the intention was produced by an unacceptable means, the law will not permit the transaction to stand. The means used is regarded as an exercise of improper or 'undue' influence, and hence unacceptable, whenever the consent thus procured ought not fairly to be treated as the expression of a person's free will. It is impossible to be more precise or definitive. The circumstances in which one person acquires influence over another, and the manner in which influence may be exercised, vary too widely to permit of any more specific criterion.

Equity identified broadly two forms of unacceptable conduct. The first comprises overt acts of improper pressure or coercion such as unlawful threats . . . The second form arises out of a relationship between two persons where one has acquired over another a measure of influence, or ascendancy, of which the ascendant person then takes unfair advantage . . . In cases of this latter nature the influence one person has over another provides scope for misuse without any specific overt acts of persuasion. The relationship between two individuals may be such that, without more, one of them is disposed to agree a course of action proposed by the other. Typically this occurs when one person places trust in another to look after his affairs and interests, and the latter betrays this trust by preferring his own interests. He abuses the influence he has acquired . . . The law has long recognised the need to prevent abuse of influence in these 'relationship' cases despite the absence of evidence of overt acts of persuasive conduct. The types of relationship, such as parent and child, in which this principle falls to be applied cannot be listed exhaustively . . . The principle is not confined to cases of abuse of trust and confidence. It also includes, for instance, cases where a vulnerable person has been exploited. Indeed, there is no single touchstone for determining whether the principle is applicable . . . Whether a transaction was brought about by the exercise of undue influence is a question of fact. Here, as elsewhere, the general principle is that he who asserts a wrong has been committed must prove it. The burden of proving an allegation of undue influence rests upon the person who claims to have been wronged. This is the general rule . . . Proof that the complainant placed trust and confidence in the other party in relation to the management of the complainant's financial affairs, coupled with a transaction which calls for explanation, will normally be sufficient, failing satisfactory evidence to the contrary, to discharge the burden of proof. On proof of these two matters the stage is set for the court to infer that, in the absence of a satisfactory explanation, the transaction can only have been procured by undue influence . . . Generations of equity lawyers have conventionally described this situation as one in which a presumption of undue influence arises . . .

The evidential presumption discussed above is to be distinguished sharply from a different form of presumption which arises in some cases. The law has adopted a sternly protective attitude

towards certain types of relationship in which one party acquires influence over another who is vulnerable and dependent and where, moreover, substantial gifts by the influenced or vulnerable person are not normally to be expected. Examples of relationships within this special class are parent and child, guardian and ward, trustee and beneficiary, solicitor and client, and medical adviser and patient. In these cases the law presumes, irrebuttably, that one party had influence over the other. The complainant need not prove he actually reposed trust and confidence in the other party. It is sufficient for him to prove the existence of the type of relationship . . . It is now well established that husband and wife is not one of the relationships to which this latter principle applies . . . Although there is no presumption, the court will nevertheless note, as a matter of fact, the opportunities for abuse which flow from a wife's confidence in her husband . . . there are two prerequisites to the evidential shift in the burden of proof from the complainant to the other party. First, that the complainant reposed trust and confidence in the other party, or the other party acquired ascendancy over the complainant. Second, that the transaction is not readily explicable by the relationship of the parties . . . The need for this second prerequisite has recently been questioned: see Nourse LJ in *Barclays Bank plc v Coleman* [2001] QB, 20, 30–32 . . . My Lords, this is not an invitation I would accept. The second prerequisite, as expressed by Lindley LJ, is good sense. It is a necessary limitation upon the width of the first prerequisite. It would be absurd for the law to presume that every gift by a child to a parent, or every transaction between a client and his solicitor or between a patient and his doctor, was brought about by undue influence unless the contrary is affirmatively proved . . . So something more is needed before the law reverses the burden of proof, something which calls for an explanation. When that something more is present, the greater the disadvantage to the vulnerable person, the more cogent must be the explanation before the presumption will be regarded as rebutted . . .

The problem considered in *O'Brien's* case and raised by the present appeals is of comparatively recent origin. It arises out of the substantial growth in home ownership over the last 30 or 40 years and, as part of that development, the great increase in the number of homes owned jointly by husbands and wives . . . They must surely be free, if they so wish, to use this asset as a means of raising money, whether for the purpose of the husband's business or for any other purpose . . . If the freedom of home-owners to make economic use of their homes is not to be frustrated, a bank must be able to have confidence that a wife's signature of the necessary guarantee and charge will be as binding upon her as is the signature of anyone else on documents which he or she may sign. Otherwise banks will not be willing to lend money on the security of a jointly owned house or flat . . . In the ordinary course a bank which takes a guarantee security from the wife of its customer will be altogether ignorant of any undue influence the customer may have exercised in order to secure the wife's concurrence. In *O'Brien* Lord Browne-Wilkinson prayed in aid the doctrine of constructive notice. In circumstances he identified, a creditor is put on inquiry. When that is so, the creditor 'will have constructive notice of the wife's rights' unless the creditor takes reasonable steps to satisfy himself that the wife's agreement to stand surety has been properly obtained: see [1994] 1 AC 180, 196 . . .

In *O'Brien* the House considered the circumstances in which a bank, or other creditor, is 'put on inquiry' . . . The House set a low level for the threshold which must be crossed before a bank is put on inquiry . . . a bank is put on inquiry whenever a wife offers to stand surety for her husband's debts . . . As to the type of transactions where a bank is put on inquiry, the case where a wife becomes surety for her husband's debts is, in this context, a straightforward case. The bank is put on inquiry. On the other side of the line is the case where money is being advanced, or has been advanced, to husband and wife jointly. In such a case the bank is not put on inquiry, unless the bank is aware the loan is being made for the husband's purposes, as distinct from their joint purposes . . .

Lord Clyde

I question the wisdom of the practice which has grown up, particularly since *Bank of Credit and Commerce International SA v Aboody* [1990] 1 QB 923 of attempting to make classifications of cases of undue influence. That concept is in any event not easy to define . . . Thus on the face of it a division into cases of 'actual' and 'presumed' undue influence appears illogical . . . English law has identified certain relationships where the conclusion can prima facie be drawn so easily as to establish a presumption of undue influence. But this is simply a matter of evidence and proof. In other cases the grantor of the deed will require to fortify the case by evidence, for example, of the pressure which was unfairly applied by the stronger party to the relationship, or the abuse of a trusting and confidential relationship resulting in for the one party a disadvantage and for the other a collateral benefit beyond what might be expected from the relationship of the parties. At the end of the day, after trial, there will either be proof of undue influence or that proof will fail and it will be found that there was no undue influence. In the former case, whatever the relationship of the parties and however the influence was exerted, there will be found to have been an actual case of undue influence. In the latter there will be none.

Lord Hobhouse of Woodborough

The division between presumed and actual undue influence derives from the judgments in *Allcard v Skinner*. Actual undue influence presents no relevant problem. It is an equitable wrong committed by the dominant party against the other which makes it unconscionable for the dominant party to enforce his legal rights against the other . . . He who alleges actual undue influence must prove it.

Presumed undue influence is different in that it necessarily involves some legally recognised relationship between the two parties. As a result of that relationship one party is treated as owing a special duty to deal fairly with the other. It is not necessary for present purposes to define the limits of the relationships which give rise to this duty. Typically they are fiduciary or closely analogous relationships. A solicitor owes a legal duty to deal fairly with his client and he must, if challenged, be prepared to show that he has done so . . . Such legal relationships can be described as relationships where one party is legally presumed to repose trust and confidence in the other-the other side of the coin to the duty not to abuse that confidence. But there is no presumption properly so called that the confidence has been abused. It is a matter of evidence . . . It is a fallacy to argue from the terminology normally used, 'presumed undue influence', to the position, not of presuming that one party reposed trust and confidence in the other, but of presuming that an abuse of that relationship has occurred; factual inference, yes, once the issue has been properly raised, but not a presumption.

The Court of Appeal in *Aboody* [1990] 1 QB 923 and Lord Browne-Wilkinson classified cases where there was a legal relationship between the parties which the law presumed to be one of trust and confidence as 'presumed undue influence: class 2(A)'. They then made the logical extrapolation that there should be a class 2(B) to cover those cases where it was proved by evidence that one party had in fact reposed trust and confidence in the other. It was then said that the same consequences flowed from this factual relationship as from the legal class 2(A) relationship.

In agreement with what I understand to be the view of your Lordships, I consider that the so-called class 2(B) presumption should not be adopted. It is not a useful forensic tool. The wife or other person alleging that the relevant agreement or charge is not enforceable must prove her case. She can do this by proving that she was the victim of an equitable wrong. This wrong may be an overt wrong, such as oppression; or it may be the failure to perform an equitable duty, such as a failure by one in whom trust and confidence is reposed not to abuse that trust

by failing to deal fairly with her and have proper regard to her interests. Although the general burden of proof is, and remains, upon her, she can discharge that burden of proof by establishing a sufficient prima facie case to justify a decision in her favour on the balance of probabilities, the court drawing appropriate inferences from the primary facts proved. Evidentially the opposite party will then be faced with the necessity to adduce evidence sufficient to displace that conclusion. Provided it is remembered that the burden is an evidential one, the comparison with the operation of the doctrine *res ipsa loquitur* is useful.

However described, this is an essential step in the reasoning of Lord Browne-Wilkinson. The wife becomes involved at the request of her husband. It is he who, in these types of case, is the source of the undue influence and commits the equitable wrong against her. But the party with whom the wife contracts and to whom the wife accepts obligations is the lender. It is the lender who is seeking to enforce those obligations. Therefore there has to be some additional factor before the lender's conscience is affected and he is to be restrained from enforcing his legal rights. The solution adopted by Lord Browne-Wilkinson was to formulate a principle of constructive notice. He did so in terms which were not as restrictive as the established principles of constructive knowledge. However, there is a structural difficulty in his approach. Notice of the risk of undue influence is not an all or nothing question. Situations will differ across a spectrum from a very small risk to a serious risk verging on a probability. There has to be a proportionality between the degree of risk and the requisite response to it. Lord Browne-Wilkinson expressed it in terms of a 'substantial risk' (p 196). But, then, in describing the requisite response he stated (p 197) that he had been considering 'the ordinary case where the creditor knows only that the wife is to stand surety for her husband's debts'. This is, as my noble and learned friend Lord Nicholls has said, a low threshold. There are arguments which would favour a higher threshold. It would enable a more positive approach to be taken to the response. It would avoid calling for a response when the level of risk did not really justify it. But the advantage of this low threshold is that it assists banks to put in place procedures which do not require an exercise of judgment by their officials and I accept Lord Nicholls's affirmation of the low threshold . . .

Needless to say the question whether the bank has been put on inquiry has to be answered upon the basis of the facts available to the bank. Does the bank know that the wife is standing surety for her husband's debts? This should be an easy question for the bank to answer. The bank should know who the principal debtor is and what is the purpose of the facility. Likewise the bank should know of any factors which are likely to aggravate the risk of undue influence. Paradoxically the best place at which to start to assess the risk of undue influence is to consider the true nature of the transaction and examine the financial position of the principal debtor and the proposal which he is making to the bank. These are the facts which the bank has most readily to hand and, if it finds that it lacks relevant information, it is in a position to get it and has the expertise to assess it. A loan application backed by a viable business plan or to acquire a worthwhile asset is very different from a loan to postpone the collapse of an already failing business or to refinance with additional security loans which have fallen into arrear. The former would not aggravate the risk; the latter most certainly would do so. The bank is as well placed as anyone to assess the underlying rationality of the debtor's proposal. It will be the bank that will have formed the view that it is not satisfied with the debtor's covenant and the security he can provide and it will be the bank that has called for additional security. The bank will also probably be aware what has been the previous involvement, if any, of the wife in the husband's business affairs.

The position therefore is that in relation to any guarantee by a wife of her husband's debts (or those of his company) the bank is put on inquiry and accordingly will have to respond unless it is to run the risk of finding that the guarantee and other security provided by the wife are unenforceable. If it becomes aware of any aggravation of the risk of undue influence, its

response must take that into account. More will be required to satisfy it that the wife's agreement has been properly obtained . . .

Lord Scott of Foscote

Undue influence cases have, traditionally, been regarded as falling into two classes, cases where undue influence must be affirmatively proved (Class 1) and cases where undue influence will be presumed (Class 2) . . . the Class 2 presumption is an evidential rebuttable presumption. It shifts the onus from the party who is alleging undue influence to the party who is denying it. Second, the weight of the presumption will vary from case to case and will depend both on the particular nature of the relationship and on the particular nature of the impugned transaction. Third, the type and weight of evidence needed to rebut the presumption will obviously depend upon the weight of the presumption itself. In *Allcard v Skinner* (1887) 36 Ch D 145 the presumption was a very heavy one. Correspondingly strong evidence would have been needed to rebut it . . .

The onus will, of course, lie on the person alleging the undue influence to prove in the first instance sufficient facts to give rise to the presumption. The relationship relied on in support of the presumption will have to be proved . . . Where, however a Class 2 presumption of undue influence is said to arise, the nature of the impugned transaction will always be material, no matter what the relationship between the parties. Some transactions will be obviously innocuous and innocent . . . it is, in my opinion, the combination of relationship and the nature of the transaction that gives rise to the presumption and, if the transaction is challenged, shifts the onus to the transferee.

In *Bank of Credit and Commerce International SA v Aboody* [1990] 1 QB 923 Slade LJ split the Class 2 cases into two subdivisions . . . it seems to me to lose sight of the evidential and rebuttable character of the Class 2 presumption. The presumption arises where the combination of the relationship and the nature of the transaction justify, in the absence of any other evidence, a conclusion that the transaction was procured by the undue influence of the dominant party. Such a conclusion, reached on a balance of probabilities, is based upon inferences to be drawn from that combination. There are some relationships, generally of a fiduciary character, where, as a matter of policy, the law requires the dominant party to justify the righteousness of the transaction. These relationships do not include the husband wife relationship. In the surety wife cases, the complainant does have to prove undue influence: the presumption, if it arises on the facts of a particular case, is a tool to assist him or her in doing so. It shifts, for the moment, the onus of proof to the other side . . .

For my part, I doubt the utility of the Class 2B classification. Class 2A is useful in identifying particular relationships where the presumption arises. The presumption in Class 2B cases, however, is doing no more than recognising that evidence of the relationship between the dominant and subservient parties, coupled with whatever other evidence is for the time being available, may be sufficient to justify a finding of undue influence on the balance of probabilities. The onus shifts to the defendant. Unless the defendant introduces evidence to counteract the inference of undue influence that the complainant's evidence justifies, the complainant will succeed. In my opinion, the presumption of undue influence in Class 2B cases has the same function in undue influence cases as res ipsa loquitur has in negligence cases. It recognises an evidential state of affairs in which the onus has shifted.

In the surety wife cases it should, in my opinion, be recognised that undue influence, though a possible explanation for the wife's agreement to become surety, is a relatively unlikely one. *O'Brien* itself was a misrepresentation case. Undue influence had been alleged but the undoubted pressure which the husband had brought to bear to persuade his reluctant wife to sign was not regarded by the judge or the Court of Appeal as constituting undue influence.

The wife's will had not been overborne by her husband. Nor was *O'Brien* a case in which, in my opinion, there would have been at any stage in the case a presumption of undue influence.

My Lords I think, given the regrettable length of this opinion, I should try and summarise my views about the principles that apply and the practice that should be followed in surety wife cases.

1. The issue as between the surety wife and the lender bank is whether the bank may rely on the apparent consent of the wife to the suretyship transaction.
2. If the bank knows that the surety wife's consent to the transaction has been procured by undue influence or misrepresentation, or if it has shut its eyes to the likelihood that that was so, it may not rely on her apparent consent.
3. If the wife's consent has in fact been procured by undue influence or misrepresentation, the bank may not rely on her apparent consent unless it has good reason to believe that she understands the nature and effect of the transaction.
4. Unless the case has some special feature, the bank's knowledge that a solicitor is acting for the wife and has advised her about the nature and effect of the transaction will provide a good reason for the purposes of (3) above.

Outcome

This being a multiple appeal case, some of the applications succeeded and others failed. However, the House of Lords set out the means by which the mortgagee could protect itself from the possibility of the mortgagor alleging undue influence.

Remedies

The specifics of equitable remedies are dealt with elsewhere (see Chapter 5), so here it will suffice simply to explain that the range of remedies developed by equity are used to remedy disputes in the law of contract where the common law remedy of damages would not suffice. Specific performance for example requires a contract to be performed in accordance with its terms, and is often granted where the subject matter of the contract is unique, as in the case of a contract for the purchase of a plot of land.

A second equitable remedy used in the law of contract is subrogation. Subrogation applies when a third party pays a debt owed by a debtor to a creditor. The third party is then able to claim any assets that the debtor gave as security for the loan.

The equitable remedy of rectification is used where a written document fails to reflect that which the parties had intended to agree. The court may order for the written form of the agreement to be rectified.

The remedy of rescission allows a party to a contract to have the contract set aside and for him to be returned to his pre-contractual position. Rescission in equity is where the contract has been created, but is later set aside because of mistake, misrepresentation or undue influence.

Equity in land law

Equity's involvement in land law is extremely extensive. Indeed it is extremely difficult to discuss land law without the involvement of equity, and therefore the trust of land, equitable interests, the sale and purchase of land, and the law of mortgages all involve equity in some capacity.

Trusts of land

A number of common usages of land will give rise to a trust. Any co-ownership of land gives rise to a trust, as is provided by s.34 and s.36 of the Law of Property Act 1925. Therefore if more than one person (such as a married or cohabiting couple) wishes to co-own land, then a trust must be created. Any land that is conveyed to a person who is below the age of 18 gives rise to a trust, as does any situation where land is conveyed to more than four co-owners. Furthermore, because land is a valuable asset, a trust of land is also created deliberately, whereby land is owned by trustees for the benefit of a third party.

Trusts of land will also arise where land is owned by one person, but where there has been a common intention that that person owns the land for the benefit of him- or herself and another person, who has relied on the common intention to their detriment.

Personal interest acquiring proprietary status

Section 1(2) of the Law of Property Act 1925 defines five types of interests in land as being legal interests. These are:

(a) An easement, right, or privilege in or over land for an interest equivalent to an estate in fee simple absolute in possession or a term of years absolute;

(b) A rentcharge in possession issuing out of or charged on land being either perpetual or for a term of years absolute;

(c) A charge by way of legal mortgage;

(d) . . . and any other similar charge on land which is not created by an instrument;

(e) Rights of entry exercisable over or in respect of a legal term of years absolute, or annexed, for any purpose, to a legal rentcharge.

Nevertheless, other types of interests affecting land may exist. These are largely equitable, in other words enforceable as a matter of contract between the person who creates them and the person who derives the benefit from them. Examples include a contract for the sale and purchase of land, a restrictive covenant or a mortgage or lease created by contract. However, such interests will also acquire proprietary status in equity through the process of notification being given on the Land Register, or through the process of registering Land Charges and the doctrine of notice where the land remains unregistered. Accordingly, equitable interests such as estate contracts (i.e. an agreement for the future sale and purchase of land) and covenants affect the buyer of land on a proprietary basis because the buyer will have notice of their existence.

Sale and purchase transactions

A sale and purchase transaction for land, known as a conveyance, also uses equity. A conveyance of land occurs in three stages. The first stage is the pre-contractual stage, where neither the buyer nor the seller owes the other any obligation either in law or in equity. The second stage is after the parties have signed and exchanged contracts. If either party were to withdraw from the transaction at this stage, one might easily recognise that there has been a breach of contract, actionable in law. However, as the property has not been transferred at this stage, it is not possible for the court to put the parties in the position in which they would be if the contract had been performed according to the parties' agreement.

Therefore, the law's approach is to invoke the concept of the trust, and conceptualise the relationship between the seller and the buyer at the post-contract stage as being one of trust, whereby the seller is the legal owner of the property for the benefit of the buyer until the sale is complete. This idea is clearer when one considers the situation once the transaction has been completed. Completion of a contract for the sale and purchase of land occurs when the seller moves out of the property, and the buyer moves in, having paid the purchase money to the seller. One would not dispute the fact that, at this stage, the buyer is the rightful owner of the property – he or she has paid the purchase money to the seller and has moved into the house. Nevertheless, the Land Register has not yet been amended to take account of the change of ownership, and still records the seller as the owner. As ownership of land is proved by the Land Register, the seller remains the owner in law, but for the benefit of the buyer, until the Land Register is amended to reflect what has happened in practice.

There are a number of other examples of incomplete obligations being regarded as equitable. These are primarily encountered in the context of land law where that which ought to have been done by a deed has merely been done either by a contract, or by some less formal agreement that has been relied upon. Accordingly, a contract for a lease will take effect as an equitable lease if the parties are acting as though a lease existed, with the tenant paying rent, and the landlord receiving it. The idea is that equity is used to give effect to a contractual obligation because otherwise the law of contract would be undermined. However, it cannot recognise the obligation as a matter of law because the formalities required by the law have not been fulfilled. This is the modern operation of equity being used to ensure that a strict adherence to the operation of the law does not lead to an absurdity.

However, the nature of these incomplete obligations is that they are personal in character. In other words, like the contract, or the agreement from which the obligation originates, the law only enforces the obligation against those who are directly a party to it. Therefore, if one returns to the situation of the conveyancing transaction, parties other than the seller and the buyer would have no need to recognise that the buyer is the rightful owner. They could rely on the Land Register for evidence of who the owner is, and could deal with the owner accordingly. It is only against the seller that the law will enforce the buyer's entitlement (although the person who is not a purchaser for value would similarly be furnished with an obligaton to uphold the arrangement).

Mortgages

In addition to equity's involvement with the law of mortgages in the context of undue influence, discussed above in the context of contract law, other aspects of the law of mortgages will involve equity as well. For example, if a mortgagee enters into possession in accordance with s.101 of the Law of Property Act 1925 in order to sell the mortgaged land because the borrower has defaulted on the loan repayments, the mortgagee will owe the mortgagor an equitable duty of good faith. This appears to be less extensive than the duty of care in negligence, and does not require the mortgage lender to act in a way that is free from self-interest – after all, if the mortgagee wishes to sell the land in order to recover the value of its loan, then its primary motivation is, necessarily, its own self-interest. However, the relationship of the mortgagee exercising the power of sale is analogous to the trust because the mortgagee must not sell the mortgaged land to itself.[7] Furthermore, the mortgagee must avoid a conflict of interest by ensuring that the land is sold for a fair price.[8] The proceeds of sale also have the flavour of trusts, in that the mortgagee becomes the owner of them for the benefit of both itself and the mortgagor.

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[7] *Farrar v Farrars Ltd* (1888) LR 40 Ch D 395.

[8] *Tse Kwong Lam v Wong Chit Sen* [1983] 3 All ER 54.

Equitable remedies

The equitable remedies of specific performance and injunction are also used extensively in relation to land – specific performance being the preferred remedy where there has been a breach of contract in relation to the sale and purchase of land, and the injunction being used to remedy a breach of covenant.

Equity in criminal law and the law of torts

Perhaps equity's greatest involvement in the law of torts is in the use of the injunction, which may be used in criminal law to prevent tortious behaviour such as harassment under s.1 or s.1A of the Protection from Harassment Act 1997[9] and in the law of torts to prevent nuisance. The injunction will also be used in order to prevent publication of material that is libellous. Recently, the media has expressed considerable interest in the 'super-injunction' whereby celebrities and politicians sought to obtain injunctions against newspapers and individuals preventing them from publishing information that was detrimental to them. The injunction is a court order that compels or restricts particular conduct, therefore where it is alleged that libellous material will be published, an injunction may be sought to prevent publication where the court considers that it is 'just and convenient to do so' (Senior Courts Act 1981, s.37).

Equity in commercial law

Increasingly, equity is becoming extremely relevant to commercial law. Companies for whom entering administration is becoming increasingly probable may attempt to use the concept of the trust in order to safeguard customers' purchases. Also commercial transactions such as mortgages will involve the law of trusts.

Safeguarding customers' purchases

Accordingly, in *Re Kayford* [1975] 1 All ER 604 and *Barclays Bank v Quistclose Investments* [1970] AC 567, trusts were successfully established for the benefit of customers, who would receive their money back as beneficiaries under a trust, rather than as creditors of the company in administration. In both these cases, the companies had put money into separate accounts for the benefit of customers in order to safeguard against the risk of the company becoming insolvent. This type of ring-fencing is also useful in order to take assets out of corporate accounts or for tax reasons.[10]

It may also assist sub-contractors in the building trade if the principal contractor is not paid by the owner of the land. A trust may also be used in order to ensure that a company's initial investors continue as investors until the company is established, and may also be used to facilitate contracts between parties who do not know whether they are able to trust the other party. A trustee who meets with the approval of both parties may be appointed. The trustee's role here is to receive each party's consideration, and to transfer it to its proper recipient once the other party's consideration has been received, or, if it is not received, to transfer it back to the original donor.

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[9] (1997 c.40).

[10] Hayton, D., Kortmann, S. and Verhagen, H. (eds) (1999) *Principles of European Trust Law*. Kluwer: The Hague.

EXTRACT

Millett, P.J. (1998) 'Equity's place in the Law of Commerce' *Law Quarterly Review* 214

Equitable doctrines and reliefs have penetrated the citadels of business and commerce long thought, at least by common lawyers, to be 'immune from the intrusion of such principles'. Three things have combined to bring about this development. First, there is the growing complexity and professionalisation of commercial life which have accompanied the change from an industrial to a service economy and the growth of the financial services industry. Much commerce today is based on trust; on each side of a commercial arms' length transaction there are likely to be relationships of trust and confidence. As a result, the modern fiduciary is usually a professional. He expects to be paid for his services, and he expects to be liable (and to be covered by appropriate insurance) if he performs his duties negligently. The picture of the trustee or fiduciary as an old friend of the family who has gratuitously volunteered his services is long obsolete. Principles of equity designed to mitigate the severity of its rules as they bore on the well-meaning amateur are incongruous when applied to the paid professional. We ought to stop repeating the inaccurate incantation that equity does not permit a trustee to profit from his trust. Of course it does. What it forbids is his making a *secret or uncovenanted* profit from his trust. We also need to reconsider the propriety of including the standard form of trustee exemption clause which exempts the trustee from liability for loss or damage not caused by his own dishonesty . . . Secondly, there has never been a greater need to impose on those who engage in commerce the high standards of conduct which equity demands. The common law insists on honesty, diligence, and the due performance of contractual obligations. But equity insists on nobler and subtler qualities: loyalty, fidelity, integrity, respect for confidentiality, and the disinterested discharge of obligations of trust and confidence. It exacts higher standards than those of the market place, where the end justifies the means and the old virtues of loyalty, fidelity and responsibility are admired less than the idols of 'success, self-interest, wealth, winning and not getting caught'. It is unrealistic to expect that employees can be given incentives through enormous bonuses without undermining their business ethics. It is hardly necessary to say more on this subject in a year in which we have seen employees in the financial services industry, enticed by the prospect of even larger bonuses, threaten not only to leave their employer for a competitor but to take their entire teams of junior staff with them; and in which we have seen a takeover bidder make use, possibly of stolen documents, but certainly of confidential information belonging to the target company, with major City firms apparently regarding such conduct as acceptable. Thirdly, plaintiffs and their advisers have discovered the apparent advantages of alleging breach of trust or fiduciary duty, with the result that a statement of claim is considered to be seriously deficient if it does not contain inappropriate references to these concepts which are often scattered throughout the pleadings with complete abandon . . .

Breach of trust or fiduciary duty

Breach of trust or fiduciary duty is widely seen as a magic formula the use of which automatically gives a plaintiff a number of advantages. First, in a claim for restitution, the formula is still thought necessary if resort is to be had to equity's more effective tracing rules. Secondly, it enables the plaintiff to claim proprietary relief, and thereby obtain priority in the defendant's insolvency or alternatively maintain a claim to profits. Thirdly, there is a widespread belief, not yet wholly abandoned, that the common law rules of causation and remoteness of damages, which appear so unfairly to limit a plaintiff's claim at common law to compensation for what he has actually lost, can miraculously be side-stepped by intoning the magic formula.

It is of the first importance not to impose fiduciary obligations on parties to a purely commercial relationship who deal with each other at arms' length and can be expected to look after their own interests . . . Much judicial and academic learning has been devoted to attempts to define the term 'fiduciary', particularly in Australia and Canada. In England, as usual, we have tried to muddle through without attempting a definition, believing that anyone can recognise a fiduciary when he sees one. Recent experience shows this to be optimistic. We should direct our efforts, not to finding a definition of the concept 'fiduciary', but to defining the characteristics of the various fiduciary relationships . . .

The search for a single, all-embracing definition is doomed to failure. There are at least three distinct categories of fiduciary relationship which possess different characteristics and which attract different kinds of fiduciary obligation. The most important of these is the relationship of trust and confidence. Such a relationship arises whenever one party undertakes to act in the interests of another, or where he places himself in a position where he is obliged to act in the interests of another. The core obligation of a fiduciary of this kind is the obligation of loyalty. Its various manifestations were described in *Bristol & West Building Society* v. *Mothew* [[1998] Ch 1]. They are very well known and need not be explored further in this article.

The second kind of fiduciary relationship is one of influence. Its defining characteristic is vulnerability. Equity is jealous to prevent the exploitation of the vulnerable. It is unconscionable for a party to exploit the influence which he may have over another for the benefit of himself and not that other. The relationship does not depend on any undertaking by one party to act in the interests of another; it is rather a relationship of ascendancy and dependency. Undue influence is not, as is sometimes supposed, the equitable counterpart of duress. It is not a form of economic duress. It is no defence that the victim of undue influence acted freely and of his own volition . . . The equitable doctrine of undue influence looks to the lack of good conscience on the part of the person exercising the influence. It is concerned with the way in which the victim's consent was obtained rather than with the reality of his consent. If resort may be had to the terminology of judicial review, it is concerned with procedural rather than with substantive unfairness. If the complaint is of serious substantive unfairness, it may be more appropriate (and is likely to be more rewarding) to turn to the ancient jurisdiction of equity to relieve against harsh and unconscionable bargains.

The third category is the relationship of confidentiality. This arises whenever information is imparted by one person to another in confidence. The obligation to respect confidentiality has several jurisdictional bases. It may be contractual or equitable. It may arise from the circumstances in which the information was imparted, or from the obviously confidential nature of the information. It may arise even if the information was improperly or accidentally obtained: the principle that 'the information must have been imparted in circumstances importing an obligation of confidence' obviously applies only where the information is voluntarily imparted. Finders and thieves, who are not fiduciaries, are bound to respect the confidentiality of the document they have found or stolen. So is the solicitor to the party opposite, who is not in a fiduciary relationship with the party seeking to protect confidentiality. There is nothing fiduciary, or even relational, in the principle which compels the return of documents mistakenly given on discovery. In earlier cases the Court had restrained the use of confidential information obtained by a trick. Now it restrained the use of information obtained as a result of a mistake. It is unconscionable for one party to take advantage of an obvious mistake by another; but this does not put the parties into any kind of fiduciary relationship. What is in play is probably the ancient jurisdiction of a court of equity to relieve against the consequences of mistake, accident and surprise. The fact is that, absent a proper law of privacy, the doctrine of confidentiality is having to do much of its work . . .

These different relationships are not mutually exclusive. They may coexist between the same parties at the same time. The solicitor and client relationship normally exhibits the characteristics of all four. It arises from a contract of retainer, which establishes a commercial relationship between the parties and gives rise to a common law duty of skill and care. At the same time it is both a fiduciary relationship of trust and confidence and a fiduciary relationship of influence. The former subjects the solicitor to a duty of undivided loyalty to his client in his dealings with third parties; the latter subjects him to special disabilities in his dealings with his client. Finally, almost all information given by the client to his solicitor is confidential, and is entrusted to the solicitor in the course of a fiduciary relationship to be used for the benefit of the client and not his own. What this demonstrates is that parties may be simultaneously in a commercial and a fiduciary relationship. That is why not every breach of duty by a fiduciary is a breach of fiduciary duty. There is a common thread to the fiduciary obligations to which these different fiduciary relationships give rise. It is the principle that a man must not exploit the relationship for his own benefit. This is what distinguishes a fiduciary relationship from a commercial one . . .

Equity in company law

In company law, the most extensive use of equity relates to a company director's fiduciary duty to the company. A company director will deal with assets on the company's behalf. However, he or she must not benefit from this relationship. A fiduciary duty is the duty owed by trustees, agents and company directors to act in good faith, not to make a profit from the relationship, not to put him- or herself in a position where his or her personal interest will – or may – conflict with the interests of the beneficiary and not to derive any benefit from the trust relationship without this being authorised. In essence it means that a trustee or a company director or an agent must take responsibility for the obligation he or she has undertaken, and must not exercise this responsibility carelessly or through motives of personal gain and self-interest.

EXTRACT

Halsbury's Laws of England Equity Vol 16(2) (Reissue)

Paragraph 854: Persons in a confidential position

A fiduciary is someone who has undertaken to act for or on behalf of another in a particular matter in circumstances which give rise to a relationship of trust and confidence. The distinguishing obligation of a fiduciary is the obligation of loyalty. This is so in most cases of agency, since the agent has duties to perform which involve the placing of confidence in him by the principal. On the same footing are directors and promoters of companies. A receiver and a trustee in bankruptcy hold property received by them in a fiduciary capacity, but a partner does not receive the assets of the partnership on account of himself and his partners in a fiduciary capacity, although he may be a trustee of particular assets when the partnership has ceased. A banker is not usually in a fiduciary position as regards his customer, but he may assume that position; and, where there is a relationship of confidentiality between banker and customer, the court may intervene to prevent the relationship from being abused.

Not all duties owed by a fiduciary are fiduciary duties. The expression 'fiduciary duty' is properly confined to those duties which are peculiar to fiduciaries and the breach of which attracts legal

consequences differing from those consequent upon the breach of other duties. It is inappropriate to apply the expression to the obligation of a trustee or other fiduciary to use proper skill and care in the discharge of his duties. Thus a director's duty to exercise care and skill is not a fiduciary duty although it is a duty actionable in the equitable jurisdiction of the court, and a claim for an account brought by a principal against his agent is based on a contractual duty not a fiduciary duty and is accordingly barred by the statutes of limitation unless the agent is more than a mere agent but is a trustee of the money which he has received. The core liability of the fiduciary arises from the single-minded loyalty of the fiduciary to which his principal is entitled. Thus, inter alia, the fiduciary must act in good faith; he must not make a profit out of his trust; he must not place himself in a position where his duty and his interest may conflict; he may not act for his own benefit or the benefit of a third person without the informed consent of his principal. Breach of any of these duties attracts those remedies which are peculiar to the equitable jurisdiction. They are primarily restitutionary or restorative, though exceptionally equitable compensation may be awarded in lieu.

In the case of *Bristol and West Building Society v Mothew* [1996] 4 All ER 698, Millett LJ gives an extensive explanation of the meaning of a fiduciary duty, and explains its application in relation to company directors. As will be seen, the central characteristic is loyalty to the obligation.

EXTRACT

Bristol and West Building Society v Mothew [1996] 4 All ER 698

Case facts

The defendant in this case was a solicitor, who acted for both the buyers and their mortgage lender (the claimants) in a conveyancing transaction. The claimants agreed to advance a loan, on the condition that theirs would be the only mortgage issued in relation to the property. The claimants required the solicitor to inform them if the buyers proposed to obtain any other mortgages between the date of the contract and completion of the transaction. However, the buyers did owe a debt on their existing house, and the lender (which was Barclays Bank, not the claimant building society) agreed to allow a small part of that debt to continue and to be secured by a second mortgage over their new home. The defendant solicitor knew about this arrangement but inadvertently failed to inform the claimants. The buyers failed to repay the loan, and the claimants went into possession of the house in order to sell it. The sale price was less than the value of the loan, and therefore the claimants sued the solicitor for breach of contract, negligence and breach of trust.

Millett LJ

[T]his branch of the law has been bedevilled by unthinking resort to verbal formulae. It is therefore necessary to begin by defining one's terms. The expression 'fiduciary duty' is properly confined to those duties which are peculiar to fiduciaries and the breach of which attracts legal consequences differing from those consequent upon the breach of other duties. Unless the expression is so limited it is lacking in practical utility. In this sense it is obvious that not every breach of duty by a fiduciary is a breach of fiduciary duty . . .

It is similarly inappropriate to apply the expression to the obligation of a trustee or other fiduciary to use proper skill and care in the discharge of his duties. If it is confined to cases where the fiduciary nature of the duty has special legal consequences, then the fact that the

source of the duty is to be found in equity rather than the common law does not make it a fiduciary duty. The common law and equity each developed the duty of care, but they did so independently of each other and the standard of care required is not always the same. But they influenced each other, and today the substance of the resulting obligations is more significant than their particular historic origin . . . I . . . indorse the comment of Ipp J in *Permanent Building Society (in liq) v Wheeler* (1994) 14 ACSR 109 at 157 where he said:

> 'It is essential to bear in mind that the existence of a fiduciary relationship does not mean that every duty owed by a fiduciary to the beneficiary is a fiduciary duty. In particular, a trustee's duty to exercise reasonable care, though equitable, is not specifically a fiduciary duty . . .'

Ipp J explained this (at 158):

> 'The director's duty to exercise care and skill has nothing to do with any position of disadvantage or vulnerability on the part of the company. It is not a duty that stems from the requirements of trust and confidence imposed on a fiduciary. In my opinion, that duty is not a fiduciary duty, although it is a duty actionable in the equitable jurisdiction of this court . . . I consider that Hamilton owed PBS a duty, both in law and in equity, to exercise reasonable care and skill, and PBS was able to mount a claim against him for breach of the legal duty, and, in the alternative, breach of the equitable duty. For the reasons I have expressed, in my view the equitable duty is not to be equated with or termed a "fiduciary" duty.'

. . . In my judgment this is not just a question of semantics. It goes to the very heart of the concept of breach of fiduciary duty and the availability of equitable remedies . . .

This leaves those duties which are special to fiduciaries and which attract those remedies which are peculiar to the equitable jurisdiction and are primarily restitutionary or restorative rather than compensatory. A fiduciary is someone who has undertaken to act for or on behalf of another in a particular matter in circumstances which give rise to a relationship of trust and confidence. The distinguishing obligation of a fiduciary is the obligation of loyalty. The principal is entitled to the single-minded loyalty of his fiduciary. This core liability has several facets. A fiduciary must act in good faith; he must not make a profit out of his trust; he must not place himself in a position where his duty and his interest may conflict; he may not act for his own benefit or the benefit of a third person without the informed consent of his principal. This is not intended to be an exhaustive list, but it is sufficient to indicate the nature of fiduciary obligations. They are the defining characteristics of the fiduciary. As Dr Finn pointed out in his classic work *Fiduciary Obligations* (1977) p 2, he is not subject to fiduciary obligations because he is a fiduciary; it is because he is subject to them that he is a fiduciary . . . The nature of the obligation determines the nature of the breach. The various obligations of a fiduciary merely reflect different aspects of his core duties of loyalty and fidelity. Breach of fiduciary obligation, therefore, connotes disloyalty or infidelity. Mere incompetence is not enough. A servant who loyally does his incompetent best for his master is not unfaithful and is not guilty of a breach of fiduciary duty.

In the present case it is clear that, if the defendant had been acting for the society alone, his admitted negligence would not have exposed him to a charge of breach of fiduciary duty . . . So it is necessary to ask: why did the fact that the defendant was acting for the purchasers as well as for the society convert the defendant's admitted breach of his duty of skill and care into a breach of fiduciary duty? To answer this question it is necessary to identify the fiduciary obligation of which he is alleged to have been in breach.

It is at this point, in my judgment, that the society's argument runs into difficulty. A fiduciary who acts for two principals with potentially conflicting interests without the informed consent of both is in breach of the obligation of undivided loyalty; he puts himself in a position where his duty to one principal may conflict with his duty to the other: see *Clark Boyce v Mouat* [1993]

4 All ER 268, [1994] 1 AC 428 and the cases there cited. This is sometimes described as 'the double employment rule'. Breach of the rule automatically constitutes a breach of fiduciary duty. But this is not something of which the society can complain. It knew that the defendant was acting for the purchasers when it instructed him. Indeed, that was the very reason why it chose the defendant to act for it. The potential conflict was of the society's own making (see Finn p 254 and *Kelly v Cooper* [1993] AC 205, [1993] 3 LRC 476).

It was submitted on behalf of the society that this is irrelevant because the defendant misled the society. It did not know of the arrangements which the purchasers had made with their bank, and so could not be said to be 'fully informed' for the purpose of absolving the defendant from the operation of the double employment rule. The submission is misconceived. The society knew all the facts relevant to its choice of solicitor. Its decision to forward the cheque for the mortgage advance to the defendant and to instruct him to proceed was based on false information, but its earlier decision to employ the defendant despite the potentially conflicting interest of his other clients was a fully informed decision.

That, of course, is not the end of the matter. Even if a fiduciary is properly acting for two principals with potentially conflicting interests he must act in good faith in the interests of each and must not act with the intention of furthering the interests of one principal to the prejudice of those of the other (see Finn p 48). I shall call this 'the duty of good faith'. But it goes further than this. He must not allow the performance of his obligations to one principal to be influenced by his relationship with the other. He must serve each as faithfully and loyally as if he were his only principal. Conduct which is in breach of this duty need not be dishonest but it must be intentional. An unconscious omission which happens to benefit one principal at the expense of the other does not constitute a breach of fiduciary duty, though it may constitute a breach of the duty of skill and care. This is because the principle which is in play is that the fiduciary must not be inhibited by the existence of his other employment from serving the interests of his principal as faithfully and effectively as if he were the only employer. I shall call this 'the no inhibition principle'. Unless the fiduciary is inhibited or believes (whether rightly or wrongly) that he is inhibited in the performance of his duties to one principal by reason of his employment by the other, his failure to act is not attributable to the double employment.

Finally, the fiduciary must take care not to find himself in a position where there is an actual conflict of duty so that he cannot fulfil his obligations to one principal without failing in his obligations to the other: see *Moody v Cox* [1917] 2 Ch 71, [1916–17] All ER Rep 548 and *Commonwealth Bank of Australia v Smith* (1991) 102 ALR 453. If he does, he may have no alternative but to cease to act for at least one and preferably both. The fact that he cannot fulfil his obligations to one principal without being in breach of his obligations to the other will not absolve him from liability. I shall call this 'the actual conflict rule'.

In the present case the judge evidently thought that the defendant was in breach of both the duty of good faith and the actual conflict rule. In *Bristol and West Building Society v May, May & Merrimans (a firm)* [1996] 2 All ER 801 at 817–818 he said:

> '. . . there can be no doubt that the requirement of unconscionable conduct is present where a solicitor who is acting for both borrower and lender misrepresents to the lender some fact *which he knows, or must be taken to know*, will or may affect the lender's decision to proceed with the loan. In those circumstances the solicitor *is abusing his fiduciary relationship with one client, the lender, to obtain an advantage for his other client, the borrower*. It is as much "against the dictates of conscience" for a solicitor *knowingly to prefer the interests of one client over those of another client* as it is for him to prefer his own interests over those of his client.' (My emphasis.)

I respectfully agree; but no such allegation is made in the present case.

As to the actual conflict rule, the judge said (at 832):

> 'First, in *Mothew*, the "agent" was a fiduciary who had put himself in a position in which his duty to the lender was in conflict with the interests of his other client, the borrower.' (My emphasis.)

I do not accept this. By instructing him to act for them, the purchasers must be taken to have authorised the defendant to complete the report without which the mortgage advance would not have been forthcoming; and to complete it truthfully. The defendant was required by the society to report on the purchasers' title as well as to confirm the absence of any further borrowing. The two stood in exactly the same case. The defendant would not have been in breach of his duty to the purchasers if he had disclosed the facts to the society any more than if he had reported a defect in their title.

This proposition can be tested by considering what the defendant's position would have been if he had acted for the purchasers and another solicitor had been instructed to act for the society. He would have been required to deduce the purchasers' title to the satisfaction of the society's solicitor, and to confirm to him that no further borrowing or second charge was in contemplation. His duty to the purchasers would have required him to ascertain the facts from them and to report them to the society. Unless they told him the facts and instructed him to lie to the society, instructions which he would be bound to refuse, his duty to the purchasers would not inhibit him in providing full and truthful information to the solicitor acting for the society.

In my judgment, the defendant was never in breach of the actual conflict rule. It is not alleged that he acted in bad faith or that he deliberately withheld information because he wrongly believed that his duty to the purchasers required him to do so. He was not guilty of a breach of fiduciary duty . . .

Outcome

The defendant, although liable for breach of confidence and negligence was not liable for breach of trust, as there was no fiduciary duty in place.

Equity in intellectual property law

Intellectual property lawyers are also likely to make use of equity. For example, if an individual or a company suspects that another is making unauthorised copies of their goods, a search order may be used in order to require the defendant to allow a search of his or her premises to obtain the necessary evidence. The cases on search orders often involve companies who allege that their brand has been misused by those who are not authorised to use it (for example *Coca-Cola v Gilbey* [1995] 4 All ER 711, and *Guess? Inc v Lee Seck Mon* [1987] FSR 125) or by film and music companies who allege that copies of their product are being made and distributed (*Rank Film Distributors Ltd v Video Information Centre* (*a firm*) [1981] 2 All ER 76). The search order will be discussed further in Chapter 5.

Therefore, although a module on equity and trust collates the different aspects of equity's involvement in the law, many other subjects will also need to make use of equitable concepts.

Chapter summary

This chapter will be useful for assignments and assessments on:

- The role and significance of equity
- Equity's significance in other areas of law.

Further reading

Hayton, D., Pigott, H and Benjamin, J. (2002) 'The use of trusts in international financial transactions' 1 *Journal of International Banking and Financial law* 23.

Loi, K.C.F. (2010) 'Mortgagees exercising power of sale: nonfeasance, privilege, trusteeship and duty of care' *Journal of Business Law* 576.

Loi, K.C.F. (2012) 'Quistclose trusts and Romalpa clauses: substance and nemo dat in corporate insolvency' *Law Quarterly Review* 412.

McCormack, G. (1996) 'The Remedial Constructive Trust and Commercial Transactions' 17(1) *Company Lawyer* 3. 214.

Millett, P.J. (1998) 'Equity's Place in the Law of Commerce' *Law Quarterly Review*

4

The nature of equitable obligations

Chapter outline

This chapter will cover:

- The personal nature of equitable obligations
- The proprietary nature of equitable obligations
- The maxims of equity.

Introduction

One of the inconveniences of equity is that defining an obligation as equitable has the tendency to mean different things in different contexts. Sometimes an equitable obligation is personal, i.e. only affecting the parties to the purported arrangement. In other cases however, an equitable obligation has a proprietary or quasi proprietary status and the obligation can therefore affect a much wider range of persons. Accordingly, in this chapter the differing nature of equitable obligations will be explored.

Equity as a personal obligation

Primarily, the nature of an obligation in equity is that it affects the conscience of the party who has agreed to be bound by it, or whose conduct indicates that he ought to expect to be bound by it. This means that the obligation is imposed solely on the person whose words or conduct indicate either a willingness to undertake the obligation, or that responsibility has been assumed. The common law is much broader in this sense, in that it recognises that an innocent third party into whose hands the property has fallen may also be liable. For example, where the defendant has committed the tort of conversion for example, the claimant is able to sue the tortfeasor him- or herself, or the innocent person who has bought the property from the tortfeasor – the idea being that the tortfeasor never had good title to the property and cannot therefore sell it. Equity on the other hand imposes the obligation solely on the wrongdoer to make good the wrong for which he or she is responsible.

This is known as acting *in personam*. This may be likened to the concept of privity in the law of contract, whereby only the person who has agreed to the obligation may be bound by it. The idea of equity acting *in personam* encompasses the notion that only the person, who because of their agreement or their conduct should expect to be bound by an obligation, will be bound by it, and equity will not therefore affect the innocent person who acquires the property.

Accordingly, if property belonging to a trustee is sold to a third party, then the beneficiary cannot recover the property, and can only pursue the trustee in an action for breach of trust in order to require the trustee to account for the loss sustained. This is a personal right because it may only be enforced against a specific individual – the trustee.

The bona fide purchaser for value without notice

Nevertheless, equity is in some respects broader than privity of contract, in that persons other than a contracting party may be liable for the breach of an equitable obligation. In essence, an equitable obligation will affect the person who made the agreement or whose conduct indicated an expectation to be bound (as in the case of the trustee) **and** any other persons who are outside the class of persons known as the bona fide purchaser for value without notice – or 'equity's darling'. All elements of this test must be fulfilled in order to enable a person to avoid an equitable obligation – the third party must be acting bona fide **and** must be a purchaser for value **and** must purchase the legal estate **and** must act without notice. In essence, it means that equity's *in personam* characteristic is broader than the concept of contractual privity – a contract may only be enforced against a contracting party. An equitable interest may be enforced against a person who is not a bona fide purchaser for value without notice.

Bona fide

Although bona fide generally relates to the genuineness of the third party's lack of notice, it also includes acting without duplicity as regards the owner. In the case of *Midland Bank*

Trust Co Ltd v Green [1981] AC 513 for example, although the buyer was without notice, he was still found to have acted mala fides (meaning in bad faith, or contrary to the obligation to act honestly and with no attempt being made to deal with the claimant in a fair way). Counsel for the respondent explains in this case:

> To avoid the stigma of bad faith it must be shown that there was a genuine reason for what was done. But here the facts show that the only object of this transaction was to defeat Geoffrey's option and a justifiable reason would have to be shown for wanting to exclude him. There was a conspiracy to defeat his option and in that there was a lack of good faith. Bona fides is more than just lack of notice. If the transaction had been above board it would not have been carried out in the way it was. On the facts as they stand the plain inference is to be drawn that the object was to defeat Geoffrey's option in such a way that he should not hear of what had been done.

Although Lord Wilberforce was of the opinion that good faith generally relates to the presence or absence of notice, he was willing to concede the respondent's argument that good faith does not relate solely to notice:

> My Lords, the character in the law known as the bona fide (good faith) purchaser for value without notice was the creation of equity. In order to affect a purchaser for value of a legal estate with some equity or equitable interest, equity fastened upon his conscience and the composite expression was used to epitomise the circumstances in which equity would or rather would not do so. I think that it would generally be true to say that the words 'in good faith' related to the existence of notice. Equity, in other words, required not only absence of notice, but genuine and honest absence of notice . . . But, and so far I would be willing to accompany the respondents, it would be a mistake to suppose that the requirement of good faith extended only to the matter of notice, or that when notice came to be regulated by statute, the requirement of good faith became obsolete. Equity still retained its interest in and power over the purchaser's conscience. The classic judgment of James L.J. in *Pilcher v. Rawlins* (1872) L.R. 7 Ch. App. 259, 269 is clear authority that it did: good faith there is stated as a separate test which may have to be passed even though absence of notice is proved. And there are references in cases subsequent to 1882 which confirm the proposition that honesty or bona fides remained something which might be inquired into (see *Berwick & Co. v. Price* [1905] 1 Ch. 632, 639; *Taylor v. London and County Banking Co*. [1901] 2 Ch. 231, 256; *Oliver v. Hinton* [1899] 2 Ch. 264, 273).

Purchaser for value

Contrary to the more common meaning of the term 'purchaser' to mean a buyer, a purchaser is anyone who acquires an interest in the property. Accordingly a mortgagee may be a purchaser, as is someone who acquires an entitlement by way of a gift, even though such people would not be viewed as buyers. However, a purchaser for value requires that some element of valuable consideration is given. Equity requires more than the nominal consideration that is required in the law of contract. Therefore, whereas in the law of contract '*A contracting party can stipulate for what consideration he chooses. A peppercorn does not cease to be good consideration if it is established that the promisee does not like pepper and will throw away the corn*,'[1] consideration in equity must be more than nominal although need not be sufficient. Therefore money will be good consideration in equity, even though the sum paid need not reflect the full market value of the property.

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[1] Per Lord Somervell of Harrow in *Chappell & Co. Ltd v Nestle & Co Ltd*. [1960] AC 87 at 114.

Legal estate

In order to defeat the equitable owner's claim, the purchaser for value must acquire a legal interest in the property, as the principle that where equities are equal the first in time prevails applies here. Therefore, a person whose own entitlement is equitable only, will not be able to defeat a pre-existing equitable interest. An example of this in operation may be seen with the case of *Mortgage Corporation Ltd v Nationwide Credit Corporation Ltd* [1994] Ch 49.

EXTRACT

Mortgage Corporation Ltd v Nationwide Credit Corporation Ltd [1994] Ch 49

Case facts

On 10 July 1989 a charge by way of a legal mortgage was granted to the claimant company, Mortgage Corporation. On 31 July 1989 a second charge was created, this time to the defendant company, Nationwide. The claimants made no application to the Land Registry for notice of the charge to be entered on the Land Register. However, although an attempt was made by the defendants to register their charge, this was rejected because the consent of a prior mortgage lender, Mortgage Trust Ltd, was required, and this had not been obtained. Both Mortgage Corporation and Nationwide's charges could only therefore take effect in equity.

Dillon LJ

As I see it, independently of the Act, the defendants' charge is necessarily overridden by the plaintiffs' charge. If, by virtue of section 106, neither charge having been registered, both are regarded as taking effect only in equity, then the equitable rule as to the priorities that *qui prior est tempore potior est jure* applies; if they are considered independently even of section 106 of the Act, then they are both charges by way of legal mortgage, and the later, in time, the defendants' charge, can only take effect as a charge on the equity of redemption in the property subject to the plaintiffs' charge.

In this case, both Nationwide and Mortgage Corporation's mortgages were equitable by virtue of not having been recorded on the Land Register. What this means is that both companies could sue the borrower for breach of contract if the mortgage loan was not repaid, but if the borrower sold the house to a third party, the mortgage lenders would not be able to recover their loan from the third party. However, if the mortgages had been legal mortgages, i.e. recorded as a charge on the Land Register, if the borrower had sold the land, the mortgage lenders could have enforced the mortgage against the buyer. Thus we see that in order to defeat an equitable interest the purchaser must buy a legal interest in the mortgaged land.

Notice

The final element is notice, which takes three forms. Firstly, there is actual knowledge – essentially this is what the third party does know. However, the doctrine of notice also applies where the third party has constructive or imputed notice of the trust. Constructive notice is the information that the third party would have if he or she had made proper enquiries, and imputed notice is notice that has been obtained by the third party's solicitor or agent in the course of the transaction. An example of the two latter forms of notice are encountered in the case of *Kingsnorth Trust Ltd v Tizard* [1986] 2 All ER 54.

EXTRACT

Kingsnorth Trust Ltd v Tizard [1986] 2 All ER 54

Case facts

Mr and Mrs Tizard bought a house. Both of them contributed to the deposit and the mortgage repayments. Some years later however, they sold the house, and used the proceeds of sale to buy another house, which was put into Mr Tizard's sole name. The fact that Mrs Tizard had contributed to the first house meant that because the proceeds of sale were used to purchase the second house, she was entitled in equity to a share of the second house. Mr and Mrs Tizard then separated, and Mrs Tizard moved out of the matrimonial home, but evidence adduced at the trial demonstrated that she remained in occupation of the matrimonial home by virtue of the fact that she continued to spend some part of every day there with the couple's two children, and also stayed there while Mr Tizard was away. Mr Tizard then attempted to obtain a mortgage loan secured on the matrimonial home, and approached the claimant company, who granted the loan. Mr Tizard then defaulted on the repayments, and the Kingsnorth Trust sought to enter into possession in order to sell the house. Mrs Tizard argued that the Kingsnorth Trust could not enter into possession because they had constructive and imputed knowledge of her equitable interest.

Judge John Finlay QC

When Mr Marshall inspected on Sunday, 13 March there was no one at the property except Mr Tizard. Mr Tizard showed him round and then he inspected the property inside and outside on his own. He found evidence of occupation by two teenagers, a boy and a girl, from clothes, posters etc that he found in their respective rooms; he saw male clothes in the main bedroom; he had an impression that the fourth bedroom seemed to be used for storage, there were suitcases in it, but he could not in evidence recollect whether it contained a bed, dressing table, and so on; and he found no evidence at all of occupation by a female, other than the teenage daughter. Mr Tizard, in apologising for the state of the house, said to Mr Marshall that his wife had gone many months ago, that they were separated and that she was living with someone nearby.

Mr Marshall's valuation report dated 15 March 1983 was made on a printed form headed with the logo and name of Bradshaws who had provided Mr Marshall with a supply of these forms. He took one with him to do the valuation and made rough notes on it. Afterwards he produced the dated report which is completed in typescript. It gives the address of the property, and Mr Tizard's name is typed in the space for the name of the applicant. The section titled 'Occupants' contains three questions: 'Who occupies the property?', 'Are there any tenancies known to you or apparent on inspection?', 'If Yes, Please give full details, including rental.' The second question was answered 'No', so there is no answer to the third. In answer to the first question there is typed, rather surprisingly in upper case (save for names and addresses, the remainder of the typescript uses upper and lower case in a normal way), the words 'Applicant, Son and Daughter' . . . . It follows in my judgment that the knowledge of the agent, Mr Marshall, that Mr Tizard had a wife is to be taken to be the knowledge of the principal, the plaintiffs.

The plaintiffs received Mr Tizard's application in which he described himself as single; and received Mr Marshall's report in which there was mention of a son and daughter. The application mentioned two 'Children or other dependants' who were stated to be both aged 15. The application had a space in which there fell to be inserted 'Age of spouse next birthday'. It was left blank. It also contained spaces for insertion of the spouse's name, and the name and address of the spouse's employers; and in these spaces there appeared 'N/A', not applicable. The application left it in doubt whether the two 15-year-old dependants were children or others, but Mr Marshall's report made it clear that they were the son and daughter of the applicant.

Had Mr Marshall's report indicated that Mr Tizard was married, it seems to me to be clear that, bearing in mind that the application stated over Mr Tizard's signature that he was single, the plaintiffs would have been put on notice that further investigation was required. Indeed, even if I am wrong in my view that Mr Marshall should have reported what Mr Tizard said about his wife, the reference to 'Son and Daughter' in the report should have alerted the plaintiffs to the need to make further inquiries.

Primarily, the plaintiffs are to be taken to have been aware that Mr Tizard was married and had described himself as single; in these circumstances their further inquiries should have led them to Mrs Tizard.

Outcome

Accordingly, Kingsnorth Trust could not enter into possession of the house because it should have known about Mrs Tizard's share.

In relation to land however, the doctrine of notice has been largely superseded by registration. Accordingly, equitable interests over land that is registered on either the Land Register (where the land is registered) or the Land Charges Register (where the land is not registered) will acquire a proprietary status, meaning that it may be enforced against anyone who seeks to deprive the claimant of it. In essence, the Land Registers seek to give notice to everyone who may acquire an interest in the land of the claimant's equitable entitlement, and therefore no one can claim to be a bona fide purchaser for value without notice. Thus an equitable interest over land will be as enforceable as a legal interest.

Mere equities

Other types of equitable interests, known as 'mere equities', are also unlikely to be enforced against third parties. These include the right to have a transaction set aside as a consequence of fraud or undue influence, as well as the deserted spouse's entitlement to remain in the matrimonial home. They are less than an equitable interest, but may nevertheless be enforceable on a personal basis, or against a person who is not a bona fide purchaser of the legal estate for value without notice, as Lord Upjohn explained in *National Provincial Bank Ltd v Ainsworth* [1965] AC 1175:

> An equity to which a subsequent purchaser is subject must create an interest in the land. As Professor Crane has pointed out in an interesting article in *The Conveyancer and Property Lawyer*, Vol. 19 (N.S.), p. 343 at p. 346: 'Beneficial interests under trusts, equitable mortgages, vendors' liens, restrictive covenants and estate contracts are all equitable interests.' No lesser interests have been held to be sufficient. A mere 'equity' used in contradistinction to an 'equitable interest' but as a phrase denoting a right which in some circumstances may bind successors is a word of limited application and, like the learned editors of *Snell*, 25th edition, at p.18, I shall attempt no definition of that phrase. It was illustrated in the case before me of *Westminster Bank Ltd. v. Lee* [[1956] Ch 7], where I was constrained in the then state of the authorities to assume that a mere equity might bind successors, yet being at most a mere equity, even subsequent equitable encumbrancers, contrary to the usual rule, could plead purchaser for value without notice. But, my Lords, freed from the fetters which there bound me, I myself cannot see how it is possible for a 'mere equity' to bind a purchaser unless such an equity is ancillary to or dependent upon an equitable estate or interest in the land. As Mr. Megarry has pointed out in the *Law Quarterly Review*, Vol. 71, at p. 482, the reason why a mere equity can be defeated by a subsequent purchaser of an equitable estate for value without notice is that the entire equitable estate passes and it is

> not encumbered or burdened by a mere equity of which he has no notice. For example, a purchaser takes subject to the rights of a tenant in possession whatever they may be. If he sees a document under which the tenant holds, that is sufficient unless he knows, or possibly in some circumstances is put on inquiry to discover, that the tenant has in addition a mere equity, e.g., a right to rectify the document. If the purchaser knows that, he knows that the document does not correctly describe the estate or interest of the tenant in the land and he takes subject to that estate or interest, whatever it may be. But a mere 'equity' naked and alone is, in my opinion, incapable of binding successors in title even with notice; it is personal to the parties.

For example, if an interest in land has been created without observance of the correct formalities, such as creation by way of a deed or protection by way of a notice entered on the Land Register, then it is likely that it will be enforceable against the owner of the land when the interest is created, but will cease to be effective against the buyer of the land once it is sold. The interest is equitable either because the law will enforce a valid contract, or because the principles of equity will not permit a person to benefit from his or her lack of good conscience. However, equity will not enforce this sort of obligation on third parties in relation to whom the law can see no justification for enforcing what is, in essence, a personal obligation.

The current law determining when an equitable interest will be proprietary is discussed in Conte's analysis of *Sinclair Investments (UK) Ltd v Versailles Trade Finance Ltd (In Administration)* [2011] EWCA Civ 347; [2011] 3 WLR 1153 (CA (Civ Div)).

EXTRACT

Conte, C. (2012) 'No proprietary relief for breach of fiduciary duty' *Law Quarterly Review* 184

The recent decision in *Sinclair Investments (UK) Ltd v Versailles Trade Finance Ltd (In Administration)* [2011] EWCA Civ 347 was a watershed. It settled a long-running controversy regarding whether, and if so when, a principal may claim a proprietary interest in any money or asset his fiduciary has acquired in breach of fiduciary duty. The Court of Appeal enunciated the following general proposition: a principal will obtain proprietary relief if the money or asset is or has been beneficially the principal's property (the 'first limb'), or if the fiduciary acquired the same by taking advantage of an opportunity properly belonging to the principal (the 'second limb'). *Sinc. Cadogan Petroleum Plc v Tolly* [2011] EWHC 2286 (Ch) addressed the inevitable fallout from that decision. In doing so, *Cadogan* itself raised important issues of legal principle. The judgment will undoubtedly spark further debate . . .

In short, for the claimant to obtain proprietary relief at the end of the story, when the story begins he must possess a proprietary right in particular subject matter. This proprietary base is a necessary, but not sufficient, condition for a proprietary claim. In addition, the value representing that right must be traceable in law or equity to a proprietary right in the subject matter of the claim, which money or asset the defendant still holds. Although he did not use the proprietary base terminology, Newey J. held that in this context a claimant principal cannot establish the necessary proprietary base unless he rescinds his contract with the third party, who has bribed his fiduciary. Unfortunately, he only stated his conclusion, without any further explanation. Newey J. merely cited *El-Ajou v Dollar Land Holdings Plc (No.1)* [1993] 3 All E.R. 717 at 734, a case concerning equitable rescission and its relationship to equitable tracing. The judge did not spell out the underlying reasoning he adopted to reach his conclusion, or analyse Millett J.'s decision in the latter case. Despite this, Newey J.'s conclusion is justifiable. Four steps are necessary.

First, bribery is a species of fraud as regards the claimant principal. Hence, it should be treated similarly to fraud. Secondly, agreements with third parties affected by bribery of the principal's agent are voidable in equity. Thirdly, a contract procured by bribery is binding. Accordingly, title passes to the third party. However, the claimant principal obtains a 'mere equity' empowering him to set aside the contract in equity. A mere equity is not a proprietary right, but a power to obtain one. It is not an interest capable of being traced. Finally, when the claimant principal elects to exercise his power and rescind the contract, equitable title to the money or asset vests or revests in the claimant at that moment. A trust is created. However, this trust is deemed to have arisen on the date which title was contractually transferred to the third party. This retrospective effect is necessary to create the equitable proprietary interest, or fiduciary relationship, required before undertaking an equitable tracing exercise. By virtue of this retrospectivity, the claimant principal can demonstrate a proprietary base at each stage of the story. In principle, the claimant may trace. Further, if the evidence shows that the third party paid a bribe to the fiduciary which traceably represented the claimant principal's money in equity, the latter will be entitled to proprietary relief regarding that sum . . .

The following table gives an outline of the main types of obligation and against whom they may be enforced.

Type of obligation	Enforceable against
Contract	Contracting party
Trust	Enforceable against trustee and person who is not equity's darling
Licence	Enforceable against licensor/licensee (and sometimes third party because of estoppel)
Legal interest affecting land as defined in s.1(2) LPA 1925 created by deed and recorded on Land Register	Enforceable against all who seek to deprive the claimant of it
Equitable interest affecting land recorded on the Land Register/ Land Charges Register	Enforceable against all who seek to deprive the claimant of it
Equitable interest affecting land not recorded on the Land Register/Land Charges Register	Enforceable against a person who is not a purchaser for value
Contribution to purchase price of house	Enforceable against remedial/constructive trustee May be enforceable on a proprietary basis as an interest that overrides under Schedule 3 to the LRA 2002 where the land is registered, or under the doctrine of notice where the land is not registered May be overreached in accordance with s.2 LPA 1925 Depending on extent of contribution, may be a mere equity, rendering the defendant liable to account but not enforceable against others
Fraud/undue influence	Enforceable against wrongdoer and person (e.g. mortgagee) who should have taken steps to protect against possibility of fraud or undue influence on the basis of their having notice that fraud or undue influence is a possibility
Proprietorship of land evidenced by Land Register or deeds	Enforceable against all

Therefore, what is seen is that equitable interests are generally personal, i.e. enforceable against the wrongdoer only. As with privity of contract, the rationale is that only the person who, by his or her words or his or her conduct, has accepted an obligation to be bound will be bound. Liability is extended in equity to those who have no reason not to be bound (the bona fide purchaser for value without notice). In other words, those who are aware of the existence of the obligation, and those who obtain something for nothing sustain no loss in recognising the obligation, and there is no reason therefore for them not to be bound by the obligation. Equitable interests over land may acquire proprietary status akin to legal rights, by being enforceable against anyone who later acquires the land. However, in effect this is an extension of the notice principle, by virtue of a process of notice being given to the entire world.

Equity's maxims

Equity's approach to law operates essentially as a means of adapting strict principles in order to mitigate against unconscionable conduct where the claimant would otherwise be left without redress even though the wider purpose of the law would require it. Equity also operates to fill gaps left by the law in situations where the claimant's conduct is unforeseen. It is for this reason that equity is often associated with notions of justice, although, as has been shown it is justice in the sense of the law's principles not being in conflict with each other, rather than justice according to an individual's concept of what should give rise to a legitimate expectation of entitlement. Accordingly, equity is extremely flexible in its approach, with the result that the trust and the equitable remedies are used in a vast range of circumstances. In a narrow sense, equity follows its own precedents, with similar remedies and solutions being found in similar-fact cases. In a broad sense however, equity utilises principles such as the constructive or resulting trust and estoppel and equitable remedies wherever the defendant's conduct is such that it would be unconscionable for him or her to rely on their strict legal entitlement.

The following maxims give some flavour of equity's guiding principles in determining when equity will intervene. They are not strict rules in the manner of a statute or the *ratio decidendi* of a case, but they nevertheless provide a useful outline of equity's approach to resolving legal disputes.

Equity will not suffer a wrong to be without a remedy

This may be seen to be the central governing principle of equity. In essence, it relates to the fact that equity will attempt to ensure that where an expectation that is deemed to be legitimate, usually in the sense of the claimant having suffered some economically quantifiable detriment in reliance upon the expectation, equity will find a remedy. However, it is perhaps more accurate to state that it is a principle of general rather than specific application, in that there are many instances of equity acknowledging that a wrong has been perpetrated against the claimant, but that their loss is either one that it is not possible to compensate adequately, or that the loss sustained is one that is regrettable in the specific instances of a particular case, but one that cannot be remedied on a general basis, or that the loss is one which the courts feel that Parliament must legislate for rather than the courts.

Equity acts *in personam*

As was demonstrated above, the central focus of equity's involvement is to act *in personam*. In other words, the claimant's action is a personal one against the wrongdoer rather

than a proprietary claim against the assets of which the claimant has been deprived. Accordingly, in equity, the defendant will be the trustee who is in breach of a trust, or the contracting party in a contractual relationship that has been made without observance of the correct formalities, or the promisor in the case of estoppel, or the person who is acting in breach in the context of a breach of covenant.

Equity gives an account of profits not damages

Damages exist in order to compensate the loss sustained by the claimant. Account exists in order to deprive the defendant of the gain he or she has made. It would appear at first glance that there is no difference between these two things – after all if Patsy has lost £100 and Rob has gained £100, then there is no practical difference between damages and accounting for profits.[2] However, in some situations the difference may be significant. For example, in *FC Jones v Jones* [1997] Ch 159, the loss to the claimant was the value of the money that had been loaned to the defendant. However, the defendant's gain was the value of the loan, plus its increased value as a consequence of her prudent investment of the money. As Millett at first glance LJ explains (at p.168):

> If she made a profit, how could she have any claim to the profit made by the use of someone else's money?

Accordingly, an account for gain may be worth more in financial terms than damages under common law.

Equity follows the law

Equity is not separate from the law and equity will not act contrary to legal principles (see Chapter 2). Accordingly, equity will not order that a beneficiary under a trust is the legal owner of an asset, merely that the legal owner owns the asset for the benefit of the beneficiary. Nevertheless, it is argued that this maxim does not have universal application[3] and therefore there are equitable entitlements, such as the restrictive covenant in land law that have no legal equivalent.

Equality is equity

This maxim has a number of applications. Firstly, it operates to give effect to the idea that loss should be proportionately borne between the parties, and that the recognition of an entitlement in equity should not lead to disproportionate hardship. A further manifestation of the maxim arises in relation to the distribution of assets between the parties. In the absence of an express declaration to the contrary, equity presumes that an equal distribution is to be favoured.

It is for this reason that equity favours a tenancy in common. Therefore where two people have contributed unequally to the acquisition cost of land, equity presumes that their entitlement is proportionate to their contributions. This conflicts with the law's approach where a joint tenancy and equal shares is favoured.

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[2] *Bartlett v Barclays Bank Trust Co Ltd*. [1980] Ch 515 per Brightman LJ at p545: '*The so-called restitution which the defendant must now make to the plaintiffs, and to the settled shares, is in reality compensation for loss suffered by the plaintiffs and the settled shares, not readily distinguishable from damages except with the aid of a powerful legal microscope.*'

[3] *McKenzie v McKenzie* [2003] EWHC 601.

He who seeks equity must do equity

This maxim refers to the future conduct of the claimant, in that the process of the litigation should be conducted in a manner that is fair towards the defendant. This includes ensuring that the claimant does not cause any unnecessary delays to the conduct of the proceedings. In situations where an interim injunction is granted, it will also mean that the claimant will have to give an undertaking in damages[4] in order to compensate the defendant for the inconvenience of the injunction if the claimant is ultimately unsuccessful at trial.

He who comes to equity must come with clean hands

This emphasises the discretionary nature of equity's intervention. Whereas the common law damages are available as a matter of right, equitable remedies are discretionary. Accordingly, where the claimant has acted in a manner that is inequitable towards the claimant, the court will decline to award an equitable remedy such as an injunction in situations where the defendant's conduct would otherwise justify it.

Nevertheless, equity does not require that the claimant's hands are spotless – what is required is 'clean hands' *vis-á-vis* the part of the relationship that pertains to the dispute before the court. For example, if Donna transfers land to Patsy, in order to conceal Donna's interest in the land, and this has no bearing on the litigation, this is not a breach of the clean hands principle.[5] Also, equity does not look at the claimant's general conduct, merely their conduct in the context of the situation that gives rise to the litigation. Therefore in *Duchess of Argyll v Duke of Argyll* [1967] Ch 302 the fact that the claimant had given details about the defendant's behaviour and financial affairs which had been published in a newspaper was not relevant conduct in relation to her application to the court for an injunction.

Equity looks upon that as done which ought to have been done

The essence of this maxim is that equity acts as though that which has been agreed upon has been effected. Accordingly, where an agreement to create a lease exists, and the tenant enters into possession of the land that is subject to the lease, equity regards the relationship between the parties as a valid lease.[6]

Equity does not allow a statute to be an instrument of fraud

This is another situation where equity's concern with fairness and justice is more precisely delineated. It is more correct to state that its conception of justice is one whereby statute is not permitted to be used as a means of perpetrating fraud. Accordingly, although s.9 Wills Act 1837 requires wills to be in writing, the law nevertheless recognises concepts such as secret trusts (discussed further in Chapter 15) even though they are not necessarily made in writing. The reason for this is that allowing the secret trustee to keep the trust property for him- or herself would mean that reliance on the strict requirement of the statute would permit the trustee to renege on his or her agreement to act as trustee.

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[4] *American Cyanamid v Ethicon* [1975] AC 396.
[5] *Tinsley v Milligan* [1994] 1 AC 340.
[6] *Walsh v Lonsdale* (1881) 21 Ch D 9.

Where equities are equal the first in time prevails

This maxim relates to the situation where two or more parties are claiming an entitlement in equity. The maxim explains that the one that was created first will prevail. For example in *Mortgage Corporation v Nationwide Credit Corporation* [1994] Ch 49, the claimant and the defendant had both issued mortgage loans to the borrowers. However, neither company had entered the mortgage as a notice on the Land Register. Accordingly, Nationwide Credit Corporation argued that Mortgage Corporation's mortgage loan should not take priority over its loan because Nationwide had no notice of Mortgage Corporation's loan. However, because both mortgages were equitable only, because of the absence of a notice on the Land Register, the first in time prevailed over the second.

Where equities are equal the law prevails

This maxim again emphasises the notion that equity does not exist in order to contradict legal principles. In essence it means that a person who acquires a legal entitlement to land will defeat the claim of the person whose entitlement is merely equitable. In *Mortgage Corporation v Nationwide Credit Corporation* (above) the case concerned two mortgages that could only subsist in equity because they had not been protected by a notice on the Land Register. What this means is that they could be enforced against the mortgagor, and that Mortgage Corporation's mortgage would take priority over the later equitable mortgage of Nationwide. However, if a third mortgagee had also issued a mortgage loan that *was* protected by a notice on the Land Register, that third mortgage would be a legal mortgage, and would take priority over both Mortgage Corporation and Nationwide Credit Corporation's equitable mortgages.

Delay defeats equity

As has been explained, equity takes account of the claimant's conduct, as well as that of the defendant. Therefore, in the same way as equity looks at the claimant's 'clean hands' and the claimant's future conduct, equity will also be alert to the possibility that the claimant has delayed before bringing a claim. If the claimant is deemed to have delayed unduly when they could have issued proceedings, they will be deemed to have accepted the breach, and equity will not therefore assist.

Equity looks to the substance rather than the form

Equity's concern is with the substantial nature of the relationship between the parties rather than with its outward appearance. Therefore if the relationship between the parties is in substance a trust for example, then equity will treat the relationship as though it were a trust. In *Paul v Constance* [1977] 1 All ER 195 for example, the deceased's assurances that 'this money is as much yours as it is mine' and his treatment of the bank account as a joint asset meant that, in substance, he was acting as a trustee of the money for the benefit of himself and his cohabitant, even though the relationship between them was not labelled as a trust, and indeed Scarman LJ (at p.197) conceded that it was probably unlikely that Mr Constance was even aware that the relationship he had established in relation to the money was in fact a trust:

> Counsel for the defendant has taken the court through the detailed evidence and submits that one cannot find anywhere in the history of events a declaration of trust in the sense of finding the deceased man, Mr Constance, saying: 'I am now disposing of my

> interest in this fund so that you, Mrs Paul, now have a beneficial interest in it.' Of course, the words which I have just used are stilted lawyers' language, and counsel for the plaintiff was right to remind the court that we are dealing with simple people, unaware of the subtleties of equity, but understanding very well indeed their own domestic situation.

Another manifestation of this maxim is that agreements made without observance of the correct formalities will be recognised in equity. For example, in *Walsh v Lonsdale* (1881) 21 Ch D 9, an agreement to create a lease was recognised as an equitable lease, and in *Mortgage Corporation v Nationwide Credit Corporation* [1994] Ch 49 a purported legal mortgage that had not been entered as a notice on the Land Register was nevertheless enforceable on an equitable basis.

Equity will not assist a volunteer

This maxim recognises the principle that equity favours the purchaser for value without notice. In essence, equity will not intervene to assist the party who has acted without any expectation of remuneration, who later decides that he or she wishes to be compensated for his or her efforts. However, the maxim also recognises that the claim of a purchaser for value (particularly where this is of the legal estate) should take priority over any equitable entitlement. It is for this reason that where an interest in land has not been entered as a notice on the Land Register in accordance with s.32 Land Registration Act 2002, it will not bind a buyer/mortgagee of the freehold or leasehold estate, but it will affect the person who is given the land by way of a gift or the person who inherits the land from the proprietor.[7]

Effect of maxims

The purpose of these maxims is to give a flavour of how equity addresses a problem. Central aspects are that: equity will not interfere with legal principles and legal entitlements; equity looks at the conduct of both the claimant and the defendant; and that equitable obligations are enforced against the wrongdoer and the person who has gained an entitlement without undertaking any expense. However, the maxims are not applied in every case, and there are instances where they may conflict with each other. For example the maxim 'equity looks to the substance rather than the form' is undermined by the fact that a legal entitlement prevails over one that is merely equitable. Furthermore, the breadth of their application varies as well, with maxims such as 'delay defeats equity' and 'he who comes to equity must come with clean hands' having as broad or as narrow a scope as the courts consider to be appropriate. Nevertheless, the maxims do give a general idea of how equity operates as a philosophy and how it interrelates with the law.

ACTIVITY

Find examples of cases where the equitable maxims are discussed. How is the equitable maxim used and explained in the case?

[7] Land Registration Act 2002, s.29.

Chapter summary

This chapter may be useful for assignments and assessments on:

- The personal nature of equitable obligations
- The proprietary nature of equitable obligations
- The maxims of equity
- Equity's approach to remedying legal disputes
- Equity's relationship with the law.

Further reading

Conte, C. (2012) 'No proprietary relief for breach of fiduciary duty' *Law Quarterly Review* 184.

Fox, D.W. (1992) 'A flexible approach to legal and equitable maxims' 156(3) *Justice of the Peace and Local Government Law* 35.

Gardner, S. (1995) 'Two maxims of equity' 54(1) *Cambridge Law Journal* 60.

Halliwell, M. (2004) 'Equitable property, discretionary remedies and unclean hands' *Conveyancer and Property Lawyer* 439.

Herstein, O.J. (2011) 'A normative theory of the clean hands defense' *Legal Theory* 171.

Kodilinye, G. (1992) 'A Fresh approach to the *ex turpi causa* and clean hands maxims' *Denning Law Journal* 93.

Pawlowski, M. and Brown, J. (2011) 'Mere equities and third parties in leasehold law' *Landlord and Tenant Review* 100.

Pawlowski, M. and Brown, J. (2011) 'Contracts for the sale of land and personal property: the equitable interests of the purchaser' 20 *Nottingham Law Journal* 38.

Pettit, P.H. (1990) 'He who comes to equity must come with clean hands' *Conveyancer and Property Lawyer* 416.

Sparkes, P. (1995) 'The proprietary effect of undue influence' *Law Quarterly Review* 250.

5

Equitable remedies

Chapter outline

This chapter will cover the equitable remedies of:

- Specific performance
- Injunction
- The freezing injunction
- The search order
- Rescission
- Rectification
- Account
- *Ne exeat regno*.

The discretionary nature of equitable remedies

Although the trust is primarily concerned with the law of property, other aspects of equity's involvement in the law have a much broader impact. Equitable remedies are used in all areas of law, and may be used alongside or instead of common law remedies and sanctions. The essence of equitable remedies is that they purport to resolve a dispute in situations where the common law remedy of damages would be inadequate. Nevertheless whereas remedies under the common law are granted as of right, in the sense that a breach of contract, once proven, will entitle the claimant to an award of damages, equitable remedies are discretionary. Yet, an equitable remedy will routinely be awarded in similar cases,[1] so, where there is a breach of contract for the sale and purchase of a unique item such as land, specific performance will not be an unusual remedy. As Lord Chelmsford notes in relation to specific performance in the case of *Cesare Lamare v Dixon* (1873) LR 6 HL 414 at p. 423:

> Now, my Lords, the exercise of the jurisdiction of equity as to enforcing the specific performance of agreements, is not a matter of right in the party seeking relief, but of discretion in the Court – not an arbitrary or capricious discretion, but one to be governed as far as possible by fixed rules and principles.

The current author submits that this comment is equally applicable to the other equitable remedies. However, the claimant is not automatically entitled to such a remedy, which will not be granted if, for example, doing so would lead to undue hardship for the defendant, or if the claimant has come to equity with the fabled unclean hands, discussed in the previous chapter.

Equitable remedies are employed in two specific situations. Firstly they will apply where common law remedies would be inadequate. Therefore an equitable remedy may be granted in what was historically a common law action, such as proceedings for breach of contract, where damages would not remedy the wrong sustained. Secondly, an equitable remedy will be granted where there has been a breach of an equitable obligation. Therefore where there has been a breach of trust, this is a breach of an equitable obligation, and therefore the remedy will also, necessarily, be equitable.

Because equity acts *in personam* (as discussed in the previous chapter), equitable remedies seek to affect the conduct of the wrongdoer. In an action for breach of contract for example, an order of specific performance, requiring a contract to be performed in accordance with its terms, recognises that the claimant's loss has been caused by the defendant's failure to adhere to the terms of the contract. In order to remedy that wrong therefore, the court orders the defendant to act in accordance with his or her promise. Similarly, the payment of a monetary sum is justified on a different basis in equity and the common law. Under the common law, the remedy of damages serves a compensatory function – the idea is to compensate the claimant for the loss that has been sustained, and to enable him or her to engage the services of an alternative supplier. On the other hand, remedies in equity are more restitutionary in character. The objective of an order to make monetary payments to the claimant is to repay to the claimant that which he or she has been deprived of. Therefore, while common law damages calculate the award payable with reference to the loss sustained by the claimant, equity calculates the sum of money to be paid with reference to the gain made by the claimant. Naturally, as Brightman J

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[1] In *Citation PLC v Ellis Whittam Ltd* [2012] EWHC 549 (QB) for example, Tugendhat J remarks at paragraph 27: *'It is true that after a trial injunctions are commonly granted with little if any opposition or argument.'*

explains in *Bartlett v Barclays Bank Trust* Co Ltd [1980] Ch 515 at 545, in some cases this will not make any difference:

> The so-called restitution which the defendant must now make to the plaintiffs, and to the settled shares, is in reality compensation for loss suffered by the plaintiffs and the settled shares, not readily distinguishable from damages except with the aid of a powerful legal microscope.

Essentially, the claimant's loss and the defendant's gain will be identical in many cases. Nevertheless, these two approaches could have very different outcomes. For example if the defendant has misappropriated the claimant's money and has invested it in a profitable manner, then the defendant's gain will exceed the claimant's loss. Therefore if Rob is a trustee of £100 for the benefit of Vic, and Rob misappropriates the money and invests it in such a way that it increases in value to £150, then Vic's loss is £100, and an award of damages would be calculated on that basis in order to compensate Vic for the loss he has sustained. On the other hand, equity's restitutionary approach will be to consider Rob's gain as being £150, and will therefore order this sum to be repaid to Vic. This was something that was discussed in the case of *Cheese v Thomas* [1994] 1 All ER 35, although the case was concerned more specifically with the apportionment of loss than the distribution of gain.

EXTRACT

Cheese v Thomas [1994] 1 All ER 35

Case facts

The claimant and his great-nephew (the defendant) bought a house. The claimant contributed £43,000 to the cost of purchase, while the defendant contributed £40,000 raised by way of a mortgage loan. The arrangement to which the parties agreed was that the house would be bought in the sole name of the defendant, but the claimant would be permitted to live in it for the duration of his lifetime, and then, after the claimant's death, the house would belong to the defendant. The defendant failed to repay the mortgage loan, and, fearing that the house would be sold by the mortgage lender in order to repay the debt, the claimant sought to have the transaction set aside, on the basis that he had been unduly influenced. At first instance, the judge ordered that the transaction was manifestly disadvantageous to the claimant, and ordered that the house be sold. Unfortunately, by the time of the sale, the house had decreased in value. The mortgage lender recovered its loan, thus effectively putting the defendant back in the position he had been in prior to the transaction, but leaving the claimant with only £17,667. The issue for the Court of Appeal therefore was who should bear the loss.

Sir Donald Nicholls VC

I approach the matter in this way. Restitution has to be made, not damages paid. Damages look at the plaintiff's loss, whereas restitution is concerned with the recovery back from the defendant of what he received under the transaction. If the transaction is set aside, the plaintiff also must return what he received. Each party must hand back what he obtained under the contract. There has to be a giving back and a taking back on both sides, as Bowen LJ observed in *Newbigging v Adam* (1886) 34 Ch D 582 at 595, [1886–90] All ER Rep 975 at 984. If, for this purpose, the transaction in this case is analysed simply as a payment of £43,000 by Mr Cheese

to Mr Thomas in return for the right to live in Mr Thomas's house, there is a strong case for ordering repayment of £43,000, the benefit received by Mr Thomas, regardless of the subsequent fall in the value of the house. In the ordinary way, if a plaintiff is able to return to the defendant the property received from him under the impugned transaction, it matters not that the property has meanwhile fallen in value. This is not surprising. A defendant cannot be heard to protest that such an outcome is unfair when he is receiving back the very thing he persuaded the plaintiff, by undue influence or misrepresentation, to buy from him . . . If a joint business venture is involved, such as an agreement between a pop star and a manager, and the agreement is set aside and an account directed of the profits received by the defendant under the agreement, the court in its discretion may permit the defendant to retain some profits, if it would be inequitable for the plaintiff to take the profits without paying for the expertise and work which produced them. In *O'Sullivan v Management Agency and Music Ltd* [1985] 3 All ER 351 at 372, [1985] QB 428 at 467, Fox LJ observed it was clearly necessary that the court should have power to make an allowance to a fiduciary. He continued ([1985] 3 All ER 351 at 372–373, [1985] QB 428 at 468):

> 'Substantial injustice may result without it. A hard and fast rule that the beneficiary can demand the whole profit without an allowance for the work without which it could not have been created is unduly severe. Nor do I think that the principle is only applicable in cases where the personal conduct of the fiduciary cannot be criticised. I think that the justice of the individual case must be considered on the facts of that case. Accordingly, where there has been dishonesty or surreptitious dealing or other improper conduct then, as indicated by Lord Denning MR, it might be appropriate to refuse relief; but that will depend on the circumstances.'

What is true of profits must also be true of losses. In the ordinary way, when a sum of money is paid to a defendant under a transaction which is set aside, the defendant will be required to repay the whole sum. There may be exceptional cases where that would be unjust. This may the more readily be so where the personal conduct of the defendant was not open to criticism. Here, having heard the parties give evidence, the judge acquitted Mr Thomas of acting in a morally reprehensible way towards Mr Cheese. He described Mr Thomas as an innocent fiduciary. Here also, and I return to this feature because on any view it was an integral element of the transaction, each party applied money in buying the house. In all the circumstances, to require Mr Thomas to shoulder the whole of the loss flowing from the problems which have beset the residential property market for the last year or two would be harsh. That is not an outcome a court of conscience should countenance.

Outcome

The outcome of the case was that the claimant and the defendant were required to divide the proceeds of sale proportionately to the extent of their contribution.

Therefore, equity's remedial approach looks at the extent of the parties' culpability. In *Cheese v Thomas* for example, the court recognised that the claimant should not have to bear the full loss of the transaction, and that the burden of the loss should be equitably distributed between the parties, even though in this case, the defendant's loss had been obliterated by the repayment of the mortgage loan. This case demonstrates that the principles of equity attempt to consider what the most equitable outcome is. Therefore, where a person has made a gain to which they were not entitled, then equity will require them to repay that gain. On the other hand, where a loss is sustained, then equity will calculate how best to apportion that loss.

Specific equitable remedies

Injunctions

An award of an injunction may be awarded by the High Court, the Court of Appeal and the Supreme Court.[2] The county court may also grant injunctions, but this is limited to matters that are within the county court's jurisdiction, provided that the application for an injunction is ancillary to the main issue.[3] Accordingly, it is primarily in the High Court that injunctions are applied for and granted.

An injunction is a court order that compels the defendant either to refrain from particular conduct, or conversely, requires the defendant actively to engage in specific conduct. A prohibitory injunction (sometimes known as a restrictive injunction) may be granted in order to prevent a particular breach[4] from continuing, such as an act of trespass on another's land.

On the other hand, a mandatory injunction may be granted in order to require the defendant to take positive action in order to undo a wrong that has been committed.[5] For example, if a building has been erected in breach of a covenant or in breach of planning regulation, then a mandatory injunction may be obtained[6] in order to compel the defendant to demolish the building in order to remedy the breach.

A third category of injunction, that may be either prohibitory or mandatory in character is a *quia timet* (meaning because he fears) injunction, which is granted in order to prevent a threatened breach. The latter type of injunction may be most familiar to readers in situations where a newspaper or broadcaster is prevented from publishing information about an individual or group.[7] No breach has occurred at the time the injunction is granted, but publication of the information would amount to a breach of an obligation such as confidentiality. In *East London Rly Co v River Thames Conservators* (1904) 6 JP 302 a *quia timet* injunction was obtained in order to prevent the defendant from dredging the Thames in a way that could damage the tunnel that had been built by the claimants.

When will an injunction be granted?

According to s.37 of the Senior Courts Act 1981 (previously known as the Supreme Court Act 1981 but renamed when the House of Lords became known as the Supreme Court) an injunction may be granted whenever the court considers it to be 'just and convenient' to do so. This section consolidates earlier principles developed by the courts, which explain that it will be just and convenient to award an injunction when a failure to do so would deprive a person of their legitimate rights or cause injury, as Jessel MR explains in *Aslatt v Corporation of Southampton* (1880) 16 Ch D 143:

> Of course the words 'just or convenient' did not mean that the Court was to grant an injunction simply because the Court thought it convenient: it meant that the Court should grant an injunction for the protection of rights or for the prevention of injury according to legal principles; but the moment you find there is a legal principle, that a man is about to suffer a serious injury, and that there is no pretence for inflicting that injury upon him, it appears to me that the Court ought to interfere.

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[2] Senior Courts Act 1981, s. 49.
[3] County Courts Act 1984, s. 24.
[4] *Raithatha v Williamson* [2012] 3 All ER 1028.
[5] *Isenberg v East India House Estate Co Ltd* (1863) 3 De G J & Sm 263.
[6] *Ecom Agroindustrial Corp Ltd v Mosharaf Composite Textile Mill Ltd* [2013] EWHC 1276 Comm.
[7] *CTB v News Group Newspapers* [2011] EWHC 1326 (QB).

The fact that an injunction may be granted when it is just and convenient to do so allows for a great deal of flexibility, and offers considerable scope for the courts to expand the scope of injunctions and apply them to new situations.[8]

Interim and perpetual injunctions

A further dimension to the injunction is that an injunction may be granted either on an interim or a perpetual basis. A perpetual injunction is not necessarily one of infinite duration; it is an injunction that aims to resolve the dispute between the parties.[9] Therefore a mandatory injunction compelling the demolition of a building is an example of a perpetual injunction. Although the injunction only endures until its requirements are fulfilled, it is perpetual in that there is no need for further intervention by the courts.

On the other hand, an interim injunction (referred to in the earlier cases as an interlocutory injunction, though interim injunction is currently the preferred term) is one that is applied for and granted before the final judgment in the case, and in some cases before the case has even commenced. Its objective is to ensure that the situation that gives rise to the dispute does not deteriorate before the matter comes to trial.[10] For example, in the case of *Re B* [2011] All ER (D) 159, two young children were in the care of foster parents who had decided they wished to adopt them. However, s.44(3) of the Adoption and Children Act 2002[11] requires those who wish to adopt a child that has not been placed with them by an adoption agency to give notice to the local authority of their intention to do so at least three months before the date of the application for the adoption order. The foster parents had not fulfilled this requirement, and therefore the court granted an interim injunction that would prevent the local authority from removing the children from the care of the foster parents until the foster parents had complied with the requirement to give notice. No adjudication had yet been made as to whether the foster parents would be permitted to adopt the children, and therefore it was possible that the local authority would eventually wish to remove the children from the care of the foster parents and place them with other adopters. However, if the children were removed before the foster parents had given notice, then the option to allow the foster parents to adopt the children would be closed to the local authority. Therefore the interim injunction served to prevent the removal of the children for a period of time, allowing the foster parents to give the required notice, and thereafter a judgment could be made regarding whether the children should be adopted by the foster parents or whether the local authority should be able to remove them and place them in the care of alternative adopters.

An interim injunction is thus granted where a failure to do so would effectively close off one of the options later to be adjudicated upon. Interim injunctions are therefore commonly used in cases involving medical intervention. For example, if a medical team decides to withdraw treatment and the patient's relatives object, then it is likely that the dispute may eventually require judicial adjudication. However an interim injunction may be applied for in order to require treatment to continue on an interim basis, because otherwise treatment would be withdrawn and the patient would be likely to have died before the matter could be adjudicated properly when all the evidence and arguments have been collected. In the case of *Plimpton v Spiller*,[12] James LJ explains this rationale:

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[8] See for example the judgment of Lord Nicholls in *Mercedes Benz v Leiduck* [1996] AC 284 at p305.
[9] *Directors of Imperial Gas Light and Coke Co v Broadbent* (1859) 7 HL Cas 600.
[10] *Plimpton v Spiller* (1876) 4 Ch D 286.
[11] (2002 c.38).
[12] (1876) 4 Ch D 286.

> When I come to consider what was really done by the Master of the Rolls it is this: Though the case assumed the form of a motion to commit for contempt, the fact of the contempt was not then made out to the satisfaction of the Court; and what the Master of the Rolls really meant to do was, to reserve the final decision of the question whether a contempt had been committed until the further hearing, when the case would be fully heard in some shape or other upon the cross-examination of the witnesses, and the fuller discussion of the principles, and when further evidence might be brought in; and therefore he said: 'I do not now determine the question. I reserve it. I do not now decide, aye or no, whether any contempt has been committed. I think that if there has been an infringement there has, beyond all question, been a contempt. For although the Defendant might say, "I did not intend to commit a contempt," yet if he was actually infringing, though he thought he was not, he was still guilty of contempt, and must be punished for it in some way or other.' The Master of the Rolls appears to me to have in fact adjourned the decision of that question for a further and final hearing, exactly in the same way as upon an interlocutory motion for an injunction the question of infringement is reserved.
>
> Moreover, it does not seem to have been really questioned before the Master of the Rolls that, if he took that view of the case, he might deal with the motion as a motion for an injunction, which he in fact did.
>
> Well, then, I think we have got to deal with it in exactly the same way as if it were a motion for an injunction against a new Defendant, the validity of the patent having been already established. And then, of course, the Court, not forming an opinion very strongly either one way or the other whether there is an infringement or not, but considering it as a fairly open question to be determined at the hearing, and not to be prejudiced by any observation in the first instance, reserves the question of infringement as one which will have to be tried at the hearing, and which it will then have to consider. There will always be, no doubt, the greatest possible difficulty in determining what is the best mode of keeping things in statu quo – for that is really what the Court has to do – to keep things in statu quo – until the final decision of the question; and then, of course, the Court says, 'We will not stop a going trade. We will not adopt a course which will result in a very great difficulty in giving compensation on the one side or on the other.' We have to deal with it as a practical question in the best way we can. I think, on the whole, that the Master of the Rolls has made the right order, viz., by granting the injunction and putting the Plaintiff upon an undertaking to abide by such order (if any) as to damages as the Court may think fit to make if he should ultimately turn out to be in the wrong; and that it would not be right in this case merely to put the Defendant upon the terms of keeping an account, which I conceive might be a very clumsy and inefficient mode of recompensing the Plaintiff if he should turn out ultimately to be in the right.

However, because an interim injunction is granted before the matter is ready to proceed to a full hearing, it is likely that the parties, particularly the defendant, will not yet have had an opportunity to collect all the relevant evidence. Accordingly, in order to mitigate the effect of an unwarranted injunction, the applicant must undertake to pay damages to the respondent if it later transpires that the injunction was unmerited.[13] An interim

[13] See for example the judgment of Jessel MR in *Smith v Day* (1882) 21 Ch D 421 for an explanation of the rationale behind the requirement of an undertaking to pay damages.

compelled by way of a mandatory injunction to demolish the building, if Bob then sells the land to Vic before the building has been demolished, Vic is under no obligation to comply with the requirements of the injunction.

EXTRACT

Attorney General v Birmingham Tame and Rea Drainage Board (1881) 17 Ch D 685

Case facts

The claimants in this case obtained an injunction to prevent the council of the borough of Birmingham from allowing sewage from the city of Birmingham to flow into the river Tame. Nineteen years later, the council of the borough of Birmingham was amalgamated with other districts to form the Birmingham, Tame, and Rea Main Sewerage District, which was the responsibility of the defendants in the present action. Sewage continued to flow from Birmingham into the river Tame, and the claimant argued that the defendant had an obligation to comply with the injunction ordered against the borough council.

Jessel MR

The first observation to be made is that this is an injunction to restrain the continuance of a tort. It is an injunction merely against the council, their workmen, and agents, and cannot be said to run with the land. If they have sold the property to somebody else, there is no injunction against the new owner, and nobody ever heard in such a case of the new owner or purchaser of land being liable to the former decree. If he continues the nuisance or commits a fresh nuisance, yon can bring an action against him, and that is all; he has nothing to do with the former proceedings, and I cannot see any ground whatever for supposing that he can be bound by that decree: nor, I believe, was such a thing ever heard of before.

Lush LJ

I am of opinion that the statement of claim is defective in two essential particulars, either of which would be fatal.

In the first place, it does not shew any facts which would amount to a breach of the injunction, even supposing the Defendants were liable. The injunction was an injunction 'to restrain the Council of the borough of Birmingham from permitting the main sewers to be constructed by them from discharging the sewage or allowing it to drain or pass into the River Tame so as to create or continue the nuisance complained of by the bill;' that is, so as to be a pollution of the river rendering it injurious to the health of the inhabitants of the houses adjoining its course, or such pollution as renders it offensive and unfit for use. Now the statement is simply that the new body have maintained the outfall works under the former powers, and have constructed further works in connection with the outfall and intercepting works, and, since the time of taking it over from the borough of Birmingham, the sewage has drained or passed into the river Tame. That may be perfectly true and no nuisance whatever created. There is not a word about its being suffered to pass in in such a condition as to be injurious to the health or so as to create a nuisance, and it is quite consistent with all that, that it might have been purified in such a way as not to be offensive at all, either to persons using the water or any person on the bank. If that stood alone, therefore, it would be an essential defect in the statement of claim.

Then the second ground is, that it shews no privity whatever between the Defendants and the Council, against whom the injunction was awarded. Under the Act 11 & 12 Vict. c. 63, which was the Act in force at the time, the Town Council was the sanitary body; and under the Public

injunction will be framed as narrowly as possible[14] – the objective is only to prevent further injury until the matter can be determined at trial.[15]

In some situations, it may be necessary to apply for an injunction without notice being issued to the respondent. Freezing injunctions and search orders, discussed below, are examples of without notice injunctions and, as will be shown, are injunctions where giving notice of the application to the respondent would defeat the purpose of the injunction.

EXTRACT

Beese v Woodhouse [1970] 1 All ER 769

Case facts

The claimants in this case were the governing body of a school which was situated near an airfield. The airfield was being used as a race track and as an area for testing motorcycles. These activities were extremely noisy and disrupted teaching and other activities that were taking place at the school. The school therefore sought to prevent the part of the track nearest the school from being used by the defendants, although of course, this rendered the entirety of the track unusable for the defendants' purposes. On 27 January 1970, an interim injunction was awarded to prevent the track from being used until the hearing date on 30 January. However, one of the four defendants had made arrangements to use the track on the 29th and 30th of January and therefore applied to have the injunction lifted on the basis that it would cause them irreparable damage if the proposed activities, namely the safety testing of cars and motorcycles, did not go ahead as planned. Notice of an application for an injunction must be served at least three days before the hearing. The timescale of this case however meant that the required notice could not be given. Accordingly, the issue to be considered was whether the defendants could have the injunction lifted without notice being given to the claimants, who would not therefore be able to make representations if they wished to object to the application.

Davies LJ

There may be many cases which, to take an example, cannot be heard by the court through no fault of the plaintiff and through no fault of the defendant; but, if on a prima facie view of the case the judge comes to the conclusion that irreparable damage may be done to the plaintiff by not preventing the continuance of the alleged nuisance or whatever other wrongdoing it may be by the defendant, plainly, in my view, the judge has jurisdiction to grant an ex-parte injunction in such circumstances. I have never heard the suggestion before that it cannot be done . . .

Outcome

In this instance the Court of Appeal concluded that the injunction was only required to last for a further two days before the matter was to be decided at trial, and that there were insufficient grounds for lifting it in this case, especially as the defendants had attempted to prevent the injunction being granted on 27 January, and that this application had been refused.

Injunctions operate *in personam*

As with the operation of equity more generally, injunctions operate *in personam*. Accordingly, only the person who is the subject of the order has a duty to comply with its obligations. Therefore if Bob builds a house in breach of a restrictive covenant, and is

[14] *Skinners' Co v Irish Society* (1836) 1 My & Cr 162.
[15] *Blakemore v Glamorganshire Canal Navigation* (1832) 1 My & K 154.

Health Act, 1875, the Act now in force under which the present Defendants were elected, by an earlier section of the Act, Birmingham, as one of the municipal boroughs, was itself constituted an independent urban district, and the Town Council the urban authority to execute the additional powers and duties created by that Act. If Birmingham had remained independent, it might have been that the Town Council would have been liable for a breach of the injunction; but then, under the 8th part of the Act, the Local Government Board have the power to dissolve any urban district and merge that in a larger area, and, in the exercise of that power, the Local Government Board made an order by which they marked out a very large area and included Birmingham in it, so that Birmingham ceased to be an independent urban district, and became only a constituent part of the larger district, and the Town Council ceased to have the authority which they had within the borough of Birmingham. The Defendants are the representative body elected out of the whole district.

Now the only section in the Act which has been appealed to, to shew that they take the obligations which belong to the Town Council, is the 275th section, but the meaning of that is obvious when one comes to look at the scheme of the Act. The 275th section says, in effect, that where an order has been made such as this order, namely, where what was an independent district has been merged into a larger area, all the liabilities, obligations, and property under the Act attaching to or vested in that former district, which if it had remained independent would have belonged to them, shall, as soon as the order is made, pass to (that is, all the obligations and liabilities constituted by the Act shall, as soon as the order is made, pass to) and vest in the larger body. That is all it says. As has been already observed by the Master of the Rolls, the obligation sought to be enforced here is not one created by the Act, and has nothing whatever to do with the Act, and that is all the 275th section means – that when what was an independent urban district is merged into a larger one, the power which they were to exercise, the duties and liabilities which they must have been under if they had remained, should pass over to the larger body.

Upon either of those grounds I am of opinion that the statement of claim is bad, and that the demurrer ought to have been allowed with costs.

When a court will grant an injunction

A court will not grant an injunction where damages would be an adequate remedy. For example, in the case of *Hodgson v Duce* (1856) 4 WR 576, the defendant had committed trespass. Ordinarily, damages would have been an adequate remedy. However, because the defendant was a pauper, an injunction was obtained, as a pauper would not be capable of paying any damages ordered. Accordingly, the injury caused to the claimant must be continuous in the sense that the claimant would have to bring repeated actions before the court in respect of the injury complained of.[16] It must also be irreparable, in the sense that an award of damages would not rectify the problem.[17] In the context of a breach of contract for example, an award of damages usually enables the claimant to obtain the contracted goods or services from an alternative supplier. The injury is neither continuous nor is it irreparable. On the other hand, the presence of sewage in a canal however is continuous in that it is caused by a continuous or repeated activity on the part of the defendant. Also the award of damages would not rectify this problem in that it would not prevent the presence of sewage in the river.

Somewhat paradoxically however, damages may be granted in lieu of an injunction. Therefore in the case of *Jaggard v Sawyer* [1995] 2 All ER 189, damages were awarded

[16] *Soltau v De Held* (1851) 2 Sim NS 133.
[17] See *American Cyanamid Co v Ethicon Ltd* [1975] AC 396 at 406 per Lord Diplock.

in lieu of an injunction because: firstly, the injury to the claimant was small (the additional traffic on the road would merely be for the purposes of accessing one additional house); secondly, the injury was capable of being quantified in financial terms (namely the expense that would be incurred by the defendant in acquiring a right of way and removing the restrictive covenant, divided between the 10 owners of the private road) and adequately compensated; and thirdly, because the claimant had delayed significantly before taking action, with the result that the house that was the subject of the application had already been built, and that an injunction, if granted, would render it worthless by virtue of being landlocked.

EXTRACT

Jaggard v Sawyer [1995] 2 All ER 189

Case facts

The defendants in this case bought a house in a cul-de-sac. The house was subject to a restrictive covenant that prevented the grounds from being used for anything other than a garden. All the other houses in the cul-de-sac were subject to an identical covenant, and the owner of each house could enforce the covenant against their neighbours. After buying their house, the defendants bought the land behind their property, and a house was built on it. After significant building work had been undertaken on the house, the claimants, one of the owners of the other houses in the cul-de-sac, commenced legal proceedings arguing, firstly, that, although the house itself had not been built in breach of covenant, the access route to it, through the defendant's garden did breach the covenant. Furthermore, because the cul-de-sac was a private road and not a public highway, it was argued that access to the new house through the cul-de-sac constituted a trespass. The defendants were found liable for the trespass and the breach of covenant, but the court declined to issue a mandatory injunction requiring the house to be demolished.

Millett LJ

Most of the cases in which the injunction has been refused are cases where the plaintiff has sought a mandatory injunction to pull down a building which infringes his right to light or which has been built in breach of a restrictive covenant. In such cases the court is faced with a *fait accompli*. The jurisdiction to grant a mandatory injunction in those circumstances cannot be doubted, but to grant it would subject the defendant to a loss out of all proportion to that which would be suffered by the plaintiff if it were refused, and would indeed deliver him to the plaintiff bound hand and foot to be subjected to any extortionate demands the plaintiff might make. In the present case, as in the closely similar case of *Bracewell v Appleby* [1975] 1 All ER 993, [1975] Ch 408, the plaintiff sought a prohibitory injunction to restrain the use of a road giving access to the defendants' house. The result of granting the injunction would be much the same: the house would not have to be pulled down, but it would be rendered landlocked and incapable of beneficial enjoyment. In the cases of oversailing cranes and other trespasses to the plaintiff's air space, on the other hand, the court has not been faced with a similar *fait accompli*. The grant of an injunction would merely restore the parties to the same position, with each of them enjoying the same bargaining strength, that they had enjoyed before the trespass began. *Goodson v Richardson* (1874) LR 9 Ch App 221 was a case of this character. The defendant, being desirous of laying pipes for the supply of water to some houses which he had built, applied to the local highways board for permission to lay the pipes in the soil under the highway. Permission was granted, but he was expressly told that this was subject to the rights of the adjoining owners. He made no approach to the adjoining owners, of whom the plaintiff

was one, but began to lay pipes in the soil of their land, whereupon the plaintiff brought prompt action for an injunction. The court granted an injunction, regarding the case as a deliberate and unlawful invasion by one man of another man's land for the purpose of a continuing trespass, to the gain and profit of the trespasser, without the consent of the owner of the land. The injunction required the pipes to be removed, but this involved relatively little cost and could hardly be considered oppressive. The defendant had acted with his eyes open, and the injunction merely restored him, after a little expenditure on his part, to the position he was in at the start.

In considering whether the grant of an injunction would be oppressive to the defendant, all the circumstances of the case have to be considered. At one extreme, the defendant may have acted openly and in good faith and in ignorance of the plaintiff's rights, and thereby inadvertently placed himself in a position where the grant of an injunction would either force him to yield to the plaintiff's extortionate demands or expose him to substantial loss. At the other extreme, the defendant may have acted with his eyes open and in full knowledge that he was invading the plaintiff's rights, and hurried on his work in the hope that by presenting the court with a *fait accompli* he could compel the plaintiff to accept monetary compensation. Most cases, like the present, fall somewhere in between.

In the present case, the defendants acted openly and in good faith and in the not unreasonable belief that they were entitled to make use of Ashleigh Avenue for access to the house that they were building. At the same time, they had been warned by the plaintiff and her solicitors that Ashleigh Avenue was a private road, that they were not entitled to use it for access to the new house and that it would be a breach of covenant for them to use the garden of No 5 to gain access to No 5A. They went ahead, not with their eyes open, but at their own risk. On the other hand, the plaintiff did not seek interlocutory relief at a time when she would almost certainly have obtained it. She should not be criticised for that, but it follows that she also took a risk, viz that by the time her case came for trial the court would be presented with a *fait accompli*. The case was a difficult one, but in an exemplary judgment the judge took into account all the relevant considerations, both those which told in favour of granting an injunction and those which told against, and in the exercise of his discretion he decided to refuse it. In my judgment his conclusion cannot be faulted.

Again, the emphasis is on ensuring equity between the parties. Awarding an injunction in this case would have been vastly disproportionate to the loss sustained by the claimant. Also, the owners of the other houses in the cul-de-sac had made no objection to the situation. Furthermore, when the house was built, the defendants were acting on the (very reasonable) belief that the cul-de-sac was owned by the local authority – at the time the building work was commenced, even the local authority believed that it owned the cul-de-sac! The claimant had had a considerable amount of time to object to the building work and had not done so. A further factor that influenced the judge at first instance was the fact that it was not believed that the defendants were acting with the deliberate intention of flouting the legal rules. Accordingly, damages were felt to be a more appropriate remedy.

Prohibitory injunctions

A prohibitory injunction is an injunction that orders the defendant to refrain from particular conduct. Accordingly, a non-molestation order (granted under s.42 of the Family Law Act 1996)[18] is a form of prohibitory injunction. In *Jaggard v Sawyer* [1995] 2 All ER

[18] (1996 c.27).

189, the injunctions sought aimed to prevent the defendants from trespassing on a stretch of road belonging to the claimant and to prevent the defendants from building a house on their land, in breach of restrictive covenants that prevented further development of the land. The particular issue before the Court of Appeal was whether the judge in the county court had been correct to award damages in lieu of an injunction. Nevertheless, the case highlights some of the ways in which a prohibitory injunction could potentially be used.

Mandatory injunctions

It is argued in some quarters that the courts are more reluctant to grant mandatory injunctions than prohibitory injunctions,[19] on the basis that a mandatory injunction causes hardship to the defendant that is disproportionate to the loss sustained by the claimant. In *Smith v Smith* (1875) LR 20 Eq 500 however, Jessel MR explains that this is not the case:

> At one time it was supposed that the Court would not issue mandatory injunctions at all. At a more recent period, in cases of nuisance, a mandatory injunction was granted under the form of restraining the Defendant from continuing the nuisance. The Court seems to have thought that there was some wonderful virtue in that form, and that extra caution was to be exercised in granting it. To that proposition I can by no means assent. Every injunction requires to be granted with care and caution, and I do not know what is meant by extraordinary caution. Every Judge ought to exercise care, and it is not more needed in one case than in another.

Nevertheless, in practice, there is a risk that a mandatory injunction will result in greater hardship for the defendant than a prohibitory injunction. There is also the greater possibility that issuing a mandatory injunction will result in disproportionate hardship for the defendant, especially where it is likely that expense has been incurred in bringing about the offending activity. That said however, there are different types of mandatory injunction and, therefore, although an order to demolish a building or a structure that has been built in breach of covenant may be less readily granted than, say, an order preventing the publication of confidential information, a mandatory injunction requiring a person to perform his or her obligations under a contract may be regarded as being no more oppressive than an injunction preventing a seller from negotiating with another potential buyer.

A mandatory injunction will be granted where damages would not offer an adequate remedy.[20] A mandatory injunction is also common where the breach is contrary to an express agreement between the claimant and the defendant.[21] Using a mandatory injunction in the situation where there has been a breach of an express agreement may in some cases result in greater hardship for the defendant than would have been the case if damages had been awarded. However, in order to achieve justice between the parties, it is sometimes considered appropriate for the defendant to be required to perform his or her obligations under the contract.[22] This is because the objective of remedies for breach of contract is to put the claimant in the position in which he or she would have been had the contract been performed.

However, despite the range of contexts in which a mandatory injunction will be awarded,[23] there are a number of situations where the courts will not award a mandatory

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[19] *Isenberg v East India House Estate Co Ltd* (1863) 3 De G J & Sm 263 at 272 per Lord Westbury LC. Cf *Kilbey v Haviland* [1871] WN 47.

[20] *Kennard v Cory Bros & Co Ltd* [1922] 2 Ch 265.

[21] *Morris v Grant* (1875) 24 WR 55; *McManus v Cooke* (1887) 35 ChD 681.

[22] *Royal Bank of Scotland v Hicks* [2010] EWHC 2568.

[23] *Jackson v Normanby Brick Co* [1899] 1 Ch 438.

injunction. Firstly, a court will not order an injunction where the contract requires the defendant to perform a personal service. For example, in *Lumley v Wagner* [1843–60] All ER Rep 368, Lord St Leonards, the Lord Chancellor explained that the court could not compel the defendant singer to sing at a particular theatre but could prevent her from performing at any other theatre. Secondly, the courts will not usually award a mandatory injunction that compels the defendant to carry out repairs, as Joyce J explains in *Attorney General v Staffordshire County Council* [1905] 1 Ch 336 at p342:

> in my opinion it is the necessary requisite of every injunction and every mandatory order that it should be certain and definite in its terms, and it must or ought to be quite clear what the person against whom the injunction or order is made is required to do or to refrain from doing. Now a mandatory order, as I understand the practice of the Court, will not be made to direct a person to repair. As we all know, the Court will not superintend works of building or of repair.

Thirdly, the court will not order a mandatory injunction where compliance would require a continuing obligation, such as the carrying on of a business, as is demonstrated in the case of *Powell Duffryn Steam Coal Company v Taff Vale Railway Company* (1874) LR 9 Ch App 331 and *Dowty Boulton Paul Ltd v Wolverhampton Corporation* [1971] 2 All ER 277.

EXTRACT

Powell Duffryn Steam Coal Company v Taff Vale Railway Company (1874) LR 9 Ch App 331

Case facts

The claimants wished to transport coal trains along a railway line belonging to the defendants. The defendants prevented this by locking the gates to the railway line.

Mellish LJ

A Court can only order the doing something which has to be done once for all, so that the Court can see to its being done. The Railway Clauses Act was passed at a time when the working of railways was not well understood. The Legislature seems to have considered that there was no more difficulty about running over a railway than along a turn-pike road. It is found now that the use of points and signals is required; but how can the Court see to the Defendants working them day after day for a series of years?

James LJ

True it is that, under the 76th and 92nd sections of the Railways Clauses Consolidation Act, the Plaintiffs appear to have the right given to them of using this railway with their engines, but, as pointed out by Vice-Chancellor Wickens, and afterwards by Vice-Chancellor Hall, it is impossible for them to exercise that right without danger, unless there is a continuous use of the signals and of the points by the Defendants' own people. Now it is, I think, impossible to say that a company ought to be compelled by this Court to trust its points and signals, upon which so much of the safety of mankind now depends, to any other persons than its own pointsmen and its own signalmen. If, therefore, relief is given to the Plaintiffs, it must in substance involve ordering the Defendants to work the points and signals. But it is not the practice of this Court to compel by injunction either a company or an individual to do a continuous act which requires the continuous employment of people.

EXTRACT

Dowty Boulton Paul Ltd v Wolverhampton Corporation [1971] 2 All ER 277

Case facts

The defendants sold a plot of land adjoining an airfield to the claimants, and permitted them to use the airfield. The airfield having fallen into disuse, the defendants decided to develop it as a housing estate. The claimants then objected to the defendants' plans, and attempted to prevent them from applying to revoke the airfield's licence to operate as an airfield.

Pennycuick VC

It seems to me that the remedy of the company must lie in damages only and that the company is not now entitled, and will not be entitled at the hearing of the action, if it is then otherwise successful, to any relief by way of injunction or mandatory order. The right vested in the company necessarily involves the maintenance of the airfield as a going concern. That involves continuing acts of management, including the upkeep of runways and buildings, the employment of staff, compliance with the Civil Aviation Act 1949, and so forth, ie in effect the carrying on of a business. That is nonetheless so by reason that so far the corporation has elected to engage Don Everall Aviation Ltd to manage the airfield on its behalf. It is very well established that the court will not order specific performance of an obligation to carry on a business or, indeed, any comparable series of activities . . . For this purpose there is no difference between an order for specific performance of the contract and a mandatory injunction to perform the party's obligation under the contract. In the present case, the notice of motion is expressed as one for a negative injunction, but one has only to look at it to see that it does involve a mandatory order on the corporation to maintain the airfield. In order that the corporation could continue to allow the company to use the airfield, it is essential that the corporation should maintain the airfield. It would be quite impossible for the company to use the airfield if the corporation did not maintain it. So an injunction in the terms asked would put on the corporation a duty, to be observed for something over 60 years, to maintain the airfield.

Outcome

Accordingly, the injunction could not be granted.

Interim injunctions

Interim injunctions are more problematic than perpetual injunctions. As they are usually granted before a matter has been tried, the courts are making decisions on liability before all the evidence has been presented. Accordingly, the courts are cautious about granting interim injunctions, and have developed safeguards to protect the respondent.

The modern law governing when an interim injunction will be granted stems from the case of *American Cyanamid v Ethicon Ltd* [1975] AC 396, which sets out three criteria to be evaluated. Firstly, there must be a serious question to be tried – in other words that the action was not ill-founded or frivolous. Secondly, the balance of convenience must favour the applicant. What this means is that if not granting the injunction would result in irreparable damage to the applicant, then the balance of convenience is in his favour, and the injunction should be awarded. If on the other hand, awarding the injunction would lead to severe unfairness for the respondent, then the injunction should not be granted. If the balance of convenience does not favour either party, then the courts

consider that the most appropriate course of action is to maintain the status quo, as was discussed by Browne LJ in the case of *Fellowes v Fisher* [1975] 2 All ER 829 at p.840. Finally, if an interim injunction is granted in favour of the applicant then he must also give an undertaking, in other words a promise to the court, to pay damages to the respondent for the inconvenience of having been subjected to an undeserved injunction if, in the final hearing, his claim is found to be unsuccessful.

EXTRACT

American Cyanamid v Ethicon Ltd [1975] AC 396

Case facts

The claimants owned a patent for sterile absorbable surgical sutures. The defendants were also the manufacturers of sutures. The claimants alleged that the defendants' sutures had been manufactured in breach of the claimants' patent. The claimants applied for an interim injunction in order to prevent the defendants from launching their product in the United Kingdom before the decision on whether the patent had been infringed had been made.

Lord Diplock

My Lords, when an application for an interlocutory injunction to restrain a defendant from doing acts alleged to be in violation of the plaintiff's legal right is made upon contested facts, the decision whether or not to grant an interlocutory injunction has to be taken at a time when *ex hypothesi* the existence of the right or the violation of it, or both, is uncertain and will remain uncertain until final judgment is given in the action. It was to mitigate the risk of injustice to the plaintiff during the period before that uncertainty could be resolved that the practice arose of granting him relief by way of interlocutory injunction; but since the middle of the 19th century this has been made subject to his undertaking to pay damages to the defendant for any loss sustained by reason of the injunction if it should be held at the trial that the plaintiff had not been entitled to restrain the defendant from doing what he was threatening to do. The object of the interlocutory injunction is to protect the plaintiff against injury by violation of his right for which he could not be adequately compensated in damages recoverable in the action if the uncertainty were resolved in his favour at the trial; but the plaintiff's need for such protection must be weighed against the corresponding need of the defendant to be protected against injury resulting from his having been prevented from exercising his own legal rights for which he could not be adequately compensated under the plaintiff's undertaking in damages if the uncertainty were resolved in the defendant's favour at the trial. The court must weigh one need against another and determine where 'the balance of convenience' lies.

In those cases where the legal rights of the parties depend upon facts that are in dispute between them, the evidence available to the court at the hearing of the application for an interlocutory injunction is incomplete. It is given on affidavit and has not been tested by oral cross-examination. The purpose sought to be achieved by giving to the court discretion to grant such injunctions would be stultified if the discretion were clogged by a technical rule forbidding its exercise if upon that incomplete untested evidence the court evaluated the chances of the plaintiff's ultimate success in the action at 50 per cent or less, but permitting its exercise if the court evaluated his chances at more than 50 per cent.

The notion that it is incumbent upon the court to undertake what is in effect a preliminary trial of the action upon evidential material different from that upon which the actual trial will be conducted, is, I think, of comparatively recent origin, though it can be supported by references

in earlier cases to the need to show 'a probability that the plaintiffs are entitled to relief' (*Preston v. Luck* (1884) 27 Ch.D. 497, 506, per Cotton L.J.) or 'a strong prima facie case that the right which he seeks to protect in fact exists' (*Smith v. Grigg Ltd.* [1924] 1 K.B. 655, 659, per Atkin L.J.) . . .

The use of such expressions as 'a probability,' 'a prima facie case,' or 'a strong prima facie case' in the context of the exercise of a discretionary power to grant an interlocutory injunction leads to confusion as to the object sought to be achieved by this form of temporary relief. The court no doubt must be satisfied that the claim is not frivolous or vexatious, in other words, that there is a serious question to be tried.

It is no part of the court's function at this stage of the litigation to try to resolve conflicts of evidence on affidavit as to facts on which the claims of either party may ultimately depend nor to decide difficult questions of law which call for detailed argument and mature considerations. These are matters to be dealt with at the trial. One of the reasons for the introduction of the practice of requiring an undertaking as to damages upon the grant of an interlocutory injunction was that 'it aided the court in doing that which was its great object, viz. abstaining from expressing any opinion upon the merits of the case until the hearing': *Wakefield v. Duke of Buccleugh* (1865) 12 L.T. 628, 629. So unless the material available to the court at the hearing of the application for an interlocutory injunction fails to disclose that the plaintiff has any real prospect of succeeding in his claim for a permanent injunction at the trial, the court should go on to consider whether the balance of convenience lies in favour of granting or refusing the interlocutory relief that is sought.

As to that, the governing principle is that the court should first consider whether, if the plaintiff were to succeed at the trial in establishing his right to a permanent injunction, he would be adequately compensated by an award of damages for the loss he would have sustained as a result of the defendant's continuing to do what was sought to be enjoined between the time of the application and the time of the trial. If damages in the measure recoverable at common law would be adequate remedy and the defendant would be in a financial position to pay them, no interlocutory injunction should normally be granted, however strong the plaintiff's claim appeared to be at that stage. If, on the other hand, damages would not provide an adequate remedy for the plaintiff in the event of his succeeding at the trial, the court should then consider whether, on the contrary hypothesis that the defendant were to succeed at the trial in establishing his right to do that which was sought to be enjoined, he would be adequately compensated under the plaintiff's undertaking as to damages for the loss he would have sustained by being prevented from doing so between the time of the application and the time of the trial. If damages in the measure recoverable under such an undertaking would be an adequate remedy and the plaintiff would be in a financial position to pay them, there would be no reason upon this ground to refuse an interlocutory injunction.

It is where there is doubt as to the adequacy of the respective remedies in damages available to either party or to both, that the question of balance of convenience arises. It would be unwise to attempt even to list all the various matters which may need to be taken into consideration in deciding where the balance lies, let alone to suggest the relative weight to be attached to them. These will vary from case to case.

Where other factors appear to be evenly balanced it is a counsel of prudence to take such measures as are calculated to preserve the status quo. If the defendant is enjoined temporarily from doing something that he has not done before, the only effect of the interlocutory injunction in the event of his succeeding at the trial is to postpone the date at which he is able to embark upon a course of action which he has not previously found it necessary to undertake; whereas to interrupt him in the conduct of an established enterprise would cause much greater inconvenience to him since he would have to start again to establish it in the event of his succeeding at the trial.

Save in the simplest cases, the decision to grant or to refuse an interlocutory injunction will cause to whichever party is unsuccessful on the application some disadvantages which his ultimate success at the trial may show he ought to have been spared and the disadvantages may be such that the recovery of damages to which he would then be entitled either in the action or under the plaintiff's undertaking would not be sufficient to compensate him fully for all of them. The extent to which the disadvantages to each party would be incapable of being compensated in damages in the event of his succeeding at the trial is always a significant factor in assessing where the balance of convenience lies, and if the extent of the uncompensatable disadvantage to each party would not differ widely, it may not be improper to take into account in tipping the balance the relative strength of each party's case as revealed by the affidavit evidence adduced on the hearing of the application. This, however, should be done only where it is apparent upon the facts disclosed by evidence as to which there is no credible dispute that the strength of one party's case is disproportionate to that of the other party. The court is not justified in embarking upon anything resembling a trial of the action upon conflicting affidavits in order to evaluate the strength of either party's case . . . Returning, therefore, to the instant appeal, it cannot be doubted that the affidavit evidence shows that there are serious questions to be tried . . . Graham J . . . came to the conclusion that the balance of convenience lay in favour of his exercising his discretion by granting an interlocutory injunction . . . The factors which he took into consideration, and in my view properly, were that Ethicon's sutures . . . were not yet on the market, so they had no business which would be brought to a stop by the injunction, no factories would be closed and no work-people would be thrown out of work . . . Cyanamid on the other hand were in the course of establishing a growing market in PHAE surgical sutures which competed with the natural catgut sutures marketed by Ethicon. If Ethicon were entitled also to establish themselves in the market for PHAE absorbable surgical sutures until the action is tried, which may not be for two or three years yet, and possibly thereafter until the case is finally disposed of on appeal, Cyanamid, even though ultimately successful in proving infringement, would have lost its chance of continuing to increase its share in the total market in absorbent surgical sutures which the continuation of an uninterrupted monopoly of PHAE sutures would have gained for it by the time of the expiry of the patent in 1980 . . . In addition there was a special factor to which Graham J. attached importance. This was that, once doctors and patients had got used to Ethicon's product XLG in the period prior to the trial, it might well be commercially impracticable for Cyanamid to deprive the public of it by insisting on a permanent injunction at the trial, owing to the damaging effect which this would have upon its goodwill in this specialised market and thus upon the sale of its other pharmaceutical products.

Outcome

An interim injunction was granted.

However, in some situations, the *American Cyanamid* criteria will not apply.[24] For example in the case of *Re J (a minor)(wardship: medical treatment)* [1992] 4 All ER 614, both the High Court and the Court of Appeal took the view that *American Cyanamid* was not appropriate in all situations. In *Re J*, a child's mother applied for a mandatory interim injunction in order to compel the defendant doctors and hospital to continue to administer life-prolonging treatment to a child with several life-threatening disabilities. However, the local authority, which shared parental responsibility with the mother, opposed the application on the basis that an injunction of this type could not be granted on an interim basis. The Judge in the High Court granted the injunction, explaining:

[24] See for example the dissenting judgment of Kerr LJ in *Cambridge Nutrition Ltd v British Broadcasting Corporation* [1990] 3 All ER 523.

> Interim relief on that footing is opposed by the local health authority on two grounds. Firstly, it is said that this is not a case in which interim relief is appropriate or possible at all. The relief claimed by the mother at this interlocutory stage is precisely what the mother will ask for at the main trial. If she fails at the substantive hearing, that will be because the court will then have decided that it would not be in [J's] best interest for his life to be artificially saved or prolonged. It could not, so the argument goes, be in [J's] interest today to have such a decision pre-empted and defeated by an interlocutory decision which would obtain the contrary result, namely mechanical ventilation, which the court at trial would wish to avoid. So powerful is that consideration, it is argued, that it lifts this case out of the ordinary *Cyanamid* considerations (see *American Cyanamid Co v Ethicon Ltd* [1975] 1 All ER 504, [1975] AC 396), in which the concern of the court is to preserve the subject matter and accept the risk that if the court should refuse the child may die before final decision, as a result of an intervening choking fit from which only ventilation could save him. Secondly and/or alternatively, it is argued that even if this is a case where the conventional Cyanamid principles fall to be applied, the mother's claim to interlocutory relief falls at the first hurdle, namely the establishment of an arguable prima facie case. The issue raised by the local authority's summons is, so it is claimed, simply not justiciable. The law is clear. The question whether artificial ventilation should or should not be applied is, so the argument proceeds, an entirely a medical one with which the courts will not interfere. Two passages are relied on to support that view from judgments of Lord Donaldson MR in recent cases. First, *Re J (a minor) (wardship: medical treatment)* [1990] 3 All ER 930 at 939, [1991] Fam 33 at 48, where he said: '. . . neither the court in wardship proceedings nor, I think, a local authority having care and control of the baby is able to require the authority to follow a particular course of treatment. What the court can do is to withhold consent to treatment of which it disapproves and it can express its approval of other treatment proposed by the authority and its doctors.' . . . It is, in my judgment, putting it too high to say that the interim relief claimed covering only five weeks before the main hearing, must be treated as pre-empting the court's powers of decision at the eventual hearing. Of course, there is a risk that if a crisis develops and mechanical ventilation is applied, the child may suffer or even die. The question, however, is whether that risk is worth taking in the interests of preserving the prospect of an informed decision when the question arises for mature consideration . . . I have no evidence one way or another as to the extent of risk of an episode occurring within five weeks but realism and common sense tells me that there is a reasonable possibility that it will not and that even if he does unfortunately suffer such a trauma, he will if his life has to be preserved by artificial means, recover sufficiently for a decision at the main hearing as to further mechanical ventilation for the future. I regard [J's] best interests as well as the interests of justice in preserving his life as both pointing in favour of granting relief.

In the Court of Appeal, Lord Donaldson reiterated this view, explaining:

> Let me say at once that, in a matter of this nature, there is absolutely no room for the application of the principles governing the grant of interlocutory relief which were laid down by Lord Diplock in *American Cyanamid Co v Ethicon Ltd* [1975] 1 All ER 504 at 510–511, [1975] AC 396 at 408. The proper approach is to consider what options are open to the court in a proper exercise of its inherent powers and, within those limits, what orders would best serve the true interests of the infant pending a final decision. There can be no question of 'balance of convenience'. There can be no question of seeking, simply as such, to preserve the status quo, although on particular facts that may well be the court's objective as being in the best interests of the infant. There

can be no question of 'preserving the subject matter of the action'. Manifestly there can be no question of considering whether damages would be an adequate remedy.

Furthermore, in *Savings and Investment Bank v Gasco Investments (Netherlands) BV* [1984] 1 All ER 296, Peter Gibson J explained that there were occasions when the court would have to consider the merits of the case in an application for an interim injunction because it is possible that the matter would never come to full trial. This is likely to be the case with applications to prevent newspapers from publishing potentially libellous or confidential material. Such cases are likely never to result in a full trial, because, by the time the interim injunction is lifted, the newspaper may no longer be interested in publishing the material.

Particular types of interim injunction: the freezing injunction and the search order

Two particular types of interim injunction are particularly worthy of mention. These are the freezing order and the search order, both developed by the courts in the 1970s under the justification that an injunction could be granted whenever it was just and convenient to do so (now contained in s.37 Senior Courts Act 1981[25]) which meant that a specific type of injunction could also be granted where it was just and convenient to do so.

EXTRACT

Senior Courts Act 1981, s.37

37 Powers of High Court with respect to injunctions and receivers

(1) The High Court may by order (whether interlocutory or final) grant an injunction or appoint a receiver in all cases in which it appears to the court to be just and convenient to do so.

(2) Any such order may be made either unconditionally or on such terms and conditions as the court thinks just.

(3) The power of the High Court under subsection (1) to grant an interlocutory injunction restraining a party to any proceedings from removing from the jurisdiction of the High Court, or otherwise dealing with, assets located within that jurisdiction shall be exercisable in cases where that party is, as well as in cases where he is not, domiciled, resident or present within that jurisdiction.

(4) The power of the High Court to appoint a receiver by way of equitable execution shall operate in relation to all legal estates and interests in land; and that power-

  (a) may be exercised in relation to an estate or interest in land whether or not a charge has been imposed on that land under section 1 of the Charging Orders Act 1979 for the purpose of enforcing the judgment, order or award in question; and

  (b) shall be in addition to, and not in derogation of, any power of any court to appoint a receiver in proceedings for enforcing such a charge.

(5) Where an order under the said section 1 imposing a charge for the purpose of enforcing a judgment, order or award has been, or has effect as if, registered under section 6 of the Land Charges Act 1972, subsection (4) of the said section 6 (effect of non-registration of writs and orders registrable under that section) shall not apply to an order appointing a receiver made either-

  (a) in proceedings for enforcing the charge; or

  (b) by way of equitable execution of the judgment, order or award or, as the case may be, of so much of it as requires payment of moneys secured by the charge.

[25] (1981 c.54).

The fact that freezing injunctions and search orders are such comparatively recent innovations displays equity's continuing capacity to develop new remedies for modern problems. These injunctions developed because the expansion of multinational companies meant that it became possible for defendants facing litigation to avoid an award of damages by moving assets to outside the jurisdiction, and because there was a growing desire to protect items that were copiable. From the 1970s onwards, there was an increasing desire to protect a 'brand' and goods bearing the logo of a particular brand, combined with an increasing commodification of intellectual property (the development of commercially available video recordings of films and cassettes and CDs of music, which meant that it became possible to make gains from selling unauthorised versions of musical and video recordings). Accordingly, EMI,[26] Columbia Pictures,[27] Universal City Studios,[28] Rank Film Distributors,[29] Naf Naf[30] and Coca Cola[31] are all claimants in notable cases, who have alleged either that the defendants have been copying their films or musical recordings, or that they have been making goods bearing the claimant's logo without the claimant having authorised such conduct.

The freezing injunction

The aim of the freezing injunction, developed in the case of *Mareva Compania Naviera SA v International Bulkcarriers SA* [1980] 1 All ER 213 (and were therefore previously known as 'Mareva injunctions'), as the current name suggests is an order granted by the courts in order to freeze a respondent's assets, in order to prevent him or her from dissipating or hiding them before trial with the consequence that any damages awarded by the court at final trial will not be paid.[32] This may be seen as the way in which the law has responded to the internationalisation of companies. Because large companies may have assets in different jurisdictions, the freezing injunction may be viewed in part as being a means of ensuring that where a company is concerned about being found liable in litigation, it may be considered expedient to remove assets to outside the jurisdiction. That said, it is not only against large multinational companies that a freezing injunction may be granted. For example, in the case of *Re Peters* [1988] QB 871 the subject of the injunction was an individual.

Freezing injunctions were first granted in the case of *Nippon Yusen Kaisha v Karageorgis* [1975] 3 All ER 282, but it was only after their acceptability was confirmed in *Mareva Compania Naviera SA v International Bulkcarriers* that their usage became more commonplace. Accordingly, these injunctions were known as Mareva injunctions after the case that legitimised them as valid forms of court order. Although the Mareva case was decided by the Court of Appeal in 1975, it is not reported until 1980, thus explaining the reference to it in the 1979 case of *Third Chandris Shipping Corporation v Unimarine* (discussed below).

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[26] *EMI Ltd v Pandit* [1975] 1 All ER 418.
[27] *Columbia Picture Industries Inc v Robinson* [1987] Ch 38 at 69–76.
[28] *Universal City Studios Inc v Mukhtar & Sons* [1976] 2 All ER 330, [1976] 1 WLR 568.
[29] *Rank Film Distributors Ltd v Video Information Centre* [1982] AC 380.
[30] *Naf Naf SA v Dickens (London) Ltd* [1993] FSR 424.
[31] *Coca-Cola Co v Gilbey* [1995] 4 All ER 711.
[32] *Z Ltd v A-Z and AA-LL* [1982] QB 558.

EXTRACT

Mareva Compania Naviera SA v International Bulkcarriers SA [1980] 1 All ER 213

Case facts

The claimant shipowners owned a ship called 'The Mareva', which they leased to the defendants. The defendants however did not pay the charter fee when it became due. The claimants treated the charter as having been repudiated, and therefore claimed for the full hire cost plus damages
for the repudiation. However, the claimants were concerned that the money paid into the defendant's bank account by the sub-charterers would disappear, and applied for an injunction to prevent the money from being disposed of.

Lord Denning

It appears that the debt is due and owing, and there is a danger that the debtor may dispose of his assets so as to defeat it before judgment, the court has jurisdiction in a proper case to grant an interlocutory judgment so as to prevent him disposing of those assets. It seems to me that this is a proper case for the exercise of this jurisdiction. There is money in a bank in London which stands in the name of these charterers. The charterers have control of it. They may at any time dispose of it or remove it out of this country. If they do so, the shipowners may never get their charter hire. The ship is now on the high seas. It has passed Cape Town on its way to India. It will complete the voyage and the cargo will be discharged. And the shipowners may not get their charter hire at all. In face of this danger, I think this court ought to grant an injunction to restrain the charterers from disposing of these moneys now in the bank in London until the trial or judgment in this action. If the charterers have any grievance about it when they hear of it, they can apply to discharge it. But meanwhile the shipowners should be protected. It is only just and right that this court should grant an injunction. I would therefore continue the injunction.

The freezing injunction is usually granted without notice – clearly giving notice to the defendant would defeat the purpose of the injunction. However, certain safeguards have been developed in order to ensure that the rights of the respondent are not unduly adversely affected. These were codified by Lord Denning in the case of *Third Chandris Shipping Corporation v Unimarine SA* [1979] QB 645, who brought together some of the guidelines mentioned by the courts in earlier cases.

EXTRACT

Third Chandris Shipping Corporation v Unimarine SA [1979] QB 645

Lord Denning

Much as I am in favour of the Mareva injunction, it must not be stretched too far lest it be endangered. In endeavouring to set out some guidelines, I have had recourse to the practice of many other countries which have been put before us. They have been most helpful. These are the points which those who apply for it should bear in mind:

(i) The plaintiff should make full and frank disclosure of all matters in his knowledge which are material for the judge to know: see *Negocios Del Mar S.A. v. Doric Shipping Corporation S.A. (The Assios)* [1979] 1 Lloyd's Rep. 331.

(ii) The plaintiff should give particulars of his claim against the defendant, stating the ground of his claim and the amount thereof, and fairly stating the points made against it by the defendant.

(iii) The plaintiff should give some grounds for believing that the defendant has assets here. I think that this requirement was put too high in *MBPXL Corporation v. Intercontinental Banking Corporation Ltd.* August 28, 1975; Court of Appeal (Civil Division) Transcript No. 411 of 1975. In most cases the plaintiff will not know the extent of the assets. He will only have indications of them. The existence of a bank account in England is enough, whether it is in overdraft or not.

(iv) The plaintiff should give some grounds for believing that there is a risk of the assets being removed before the judgment or award is satisfied. The mere fact that the defendant is abroad is not by itself sufficient. No one would wish any reputable foreign company to be plagued with a Mareva injunction simply because it has agreed to London arbitration. But there are some foreign companies whose structure invites comment. We often see in this court a corporation which is registered in a country where the company law is so loose that nothing is known about it – where it does no work and has no officers and no assets. Nothing can be found out about the membership, or its control, or its assets, or the charges on them. Judgment cannot be enforced against it. There is no reciprocal enforcement of judgments. It is nothing more than a name grasped from the air, as elusive as the Cheshire Cat. In such cases the very fact of incorporation there gives some ground for believing there is a risk that, if judgment or an award is obtained, it may go unsatisfied. Such registration of such companies may carry many advantages to the individuals who control them, but they may suffer the disadvantage of having a Mareva injunction granted against them. The giving of security for a debt is a small price to pay for the convenience of such a registration. Security would certainly be required in New York. So also it may be in London. Other grounds may be shown for believing there is a risk. But some such should be shown.

(v) The plaintiff must, of course, give an undertaking in damages – in case he fails in his claim or the injunction turns out to be unjustified. In a suitable case this should be supported by a bond or security: and the injunction only granted on it being given, or undertaken to be given.

In setting out those guidelines, I hope we shall do nothing to reduce the efficacy of the present practice. In it speed is of the essence. Ex parte is of the essence. If there is delay, or if advance warning is given, the assets may well be removed before the injunction can bite.

Lord Denning MR emphasises the need for the claimant to make a full and frank disclosure of the matters that are relevant for the court to know. Because the defendant will, necessarily, not be present when the application is heard, it is important for the claimant to make a full and frank disclosure of the case. This involves presenting a fair representation of the defendant's possible counter-argument, as well as the strengths of the claimant's own case.

The second aspect that is emphasised is that there is a need for the claimant to explain why he or she believes that there is a risk that assets will be hidden or otherwise dissipated pending trial. It is to be remembered that a freezing order will necessarily have a detrimental impact on the defendant's ability to deal with his or her own property, and therefore the freezing injunction must be more than merely a safeguard for the claimant – there must be a genuine risk that assets will be put outside the scope of judgment.

There are limitations to the types of assets that may be frozen. Firstly, the value of the assets frozen cannot exceed the value of the claim. Put simply, if one's claim is for £50,000, then one cannot apply for an order freezing £2 million of the defendant's assets.[33]

Secondly, the defendant should not be denied basic subsistence – clothing, bedding, accommodation, etc. In *Re Peters* [1988] QB 871 for example, the defendant's son's school fees were excluded from the terms of the order. Although this case was in the form of a restraining order made under s.8 of the Drug Trafficking Offences Act 1986,[34] it is also a form of ex-parte order for the purposes of freezing a defendant's assets, and therefore it is probable that a similar approach would be taken for the purposes of deciding what should be excluded from a freezing injunction.

Other aspects of the freezing injunction are:

- It does not put the applicant in a preferential position as a creditor in the event of the respondent being declared bankrupt.
- Once a freezing injunction has been obtained, the applicant must take steps to proceed with the action and not to delay in making progress with the action.[35]

Although freezing injunctions developed in the courts, they have become so formalised by now as to have a statutory basis (for example in s.4 Anti-Terrorism, Crime and Security Act 2001,[36] s.8 International Criminal Court Act 2001,[37] s.10 Crime (International Co-operation) Act 2003,[38] s.23 Pensions Act 2004, s.3 Pensions Act 2008), and standard forms of freezing injunctions have been drafted. Accordingly, the freezing injunction is an example of the operation of the common law (as distinct from statute law) being used to introduce new remedies to the law, and these remedies then becoming incorporated into statute.

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[33] *Z Ltd v A-Z and AA-LL* [1982] QB 558.
[34] (1986 c.32).
[35] *Town and Country Building Society v Daisystar Ltd and Raja* [1989] NLJR 1563.
[36] (2001 c.24).
[37] (2001 c.17).
[38] (2003 c.32).

EXTRACT

Sample freezing injunction: Ministry of Justice (2012) Civil Procedure Rules: Practice Direction 25A Interim Injunctions

FREEZING INJUNCTION

IN THE HIGH COURT OF JUSTICE
[ ] DIVISION

Before The Honourable Mr Justice

[ ]

Claim No.

Dated

Applicant

Seal

Respondent

Name, address and reference of Respondent

PENAL NOTICE

IF YOU [ ][1] DISOBEY THIS ORDER YOU MAY BE HELD TO BE IN CONTEMPT OF COURT AND MAY BE IMPRISONED, FINED OR HAVE YOUR ASSETS SEIZED.

ANY OTHER PERSON WHO KNOWS OF THIS ORDER AND DOES ANYTHING WHICH HELPS OR PERMITS THE RESPONDENT TO BREACH THE TERMS OF THIS ORDER MAY ALSO BE HELD TO BE IN CONTEMPT OF COURT AND MAY BE IMPRISONED, FINED OR HAVE THEIR ASSETS SEIZED.

1 Insert name of Respondent

THIS ORDER

1. This is a Freezing Injunction made against [] ('the Respondent') on [] by Mr Justice [] on the application of [] ('the Applicant'). The Judge read the Affidavits listed in Schedule A and accepted the undertakings set out in Schedule B at the end of this Order.
2. This order was made at a hearing without notice to the Respondent. The Respondent has a right to apply to the court to vary or discharge the order – see paragraph 13 below.

3. There will be a further hearing in respect of this order on [] ('the return date').
4. If there is more than one Respondent –
   (a) unless otherwise stated, references in this order to 'the Respondent' mean both or all of them; and
   (b) this order is effective against any Respondent on whom it is served or who is given notice of it.

FREEZING INJUNCTION

[For injunction limited to assets in England and Wales]

5. Until the return date or further order of the court, the Respondent must not remove from England and Wales or in any way dispose of, deal with or diminish the value of any of his assets which are in England and Wales up to the value of £.

[For worldwide injunction]

5. Until the return date or further order of the court, the Respondent must not –
   (1) remove from England and Wales any of his assets which are in England and Wales up to the value of £; or
   (2) in any way dispose of, deal with or diminish the value of any of his assets whether they are in or outside England and Wales up to the same value.

[For either form of injunction]

6. Paragraph 5 applies to all the Respondent's assets whether or not they are in his own name and whether they are solely or jointly owned. For the purpose of this order the Respondent's assets include any asset which he has the power, directly or indirectly, to dispose of or deal with as if it were his own. The Respondent is to be regarded as having such power if a third party holds or controls the asset in accordance with his direct or indirect instructions.
7. This prohibition includes the following assets in particular –
   (a) the property known as [title/address] or the net sale money after payment of any mortgages if it has been sold;
   (b) the property and assets of the Respondent's business [known as [name]] [carried on at [address]] or the sale money if any of them have been sold; and
   (c) any money standing to the credit of any bank account including the amount of any cheque drawn on such account which has not been cleared.

[For injunction limited to assets in England and Wales]

8. If the total value free of charges or other securities ('unencumbered value') of the Respondent's assets in England and Wales exceeds £, the Respondent may remove any of those assets from England and Wales or may dispose of or deal with them so long as the total unencumbered value of his assets still in England and Wales remains above £.

[For worldwide injunction]

8. (1) If the total value free of charges or other securities ('unencumbered value') of the Respondent's assets in England and Wales exceeds £, the Respondent may remove any of those assets from England and Wales or may dispose of or deal with them so long as the total unencumbered value of the Respondent's assets still in England and Wales remains above £.

(2) If the total unencumbered value of the Respondent's assets in England and Wales does not exceed £, the Respondent must not remove any of those assets from England and Wales and must not dispose of or deal with any of them. If the Respondent has other assets outside England and Wales, he may dispose of or deal with those assets outside England and Wales so long as the total unencumbered value of all his assets whether in or outside England and Wales remains above £.

PROVISION OF INFORMATION

9. (1) Unless paragraph (2) applies, the Respondent must [immediately] [within hours of service of this order] and to the best of his ability inform the Applicant's solicitors of all his assets [in England and Wales] [worldwide] [exceeding £ in value] whether in his own name or not and whether solely or jointly owned, giving the value, location and details of all such assets.

(2) If the provision of any of this information is likely to incriminate the Respondent, he may be entitled to refuse to provide it, but is recommended to take legal advice before refusing to provide the information. Wrongful refusal to provide the information is contempt of court and may render the Respondent liable to be imprisoned, fined or have his assets seized.

10. Within [] working days after being served with this order, the Respondent must swear and serve on the Applicant's solicitors an affidavit setting out the above information.

EXCEPTIONS TO THIS ORDER

11. (1) This order does not prohibit the Respondent from spending £ a week towards his ordinary living expenses and also £ [or a reasonable sum] on legal advice and representation. [But before spending any money the Respondent must tell the Applicant's legal representatives where the money is to come from.]

[(2) This order does not prohibit the Respondent from dealing with or disposing of any of his assets in the ordinary and proper course of business.]

(3) The Respondent may agree with the Applicant's legal representatives that the above spending limits should be increased or that this order should be varied in any other respect, but any agreement must be in writing.

(4) The order will cease to have effect if the Respondent –

(a) provides security by paying the sum of £ into court, to be held to the order of the court; or

(b) makes provision for security in that sum by another method agreed with the Applicant's legal representatives.

COSTS

12. The costs of this application are reserved to the judge hearing the application on the return date.

VARIATION OR DISCHARGE OF THIS ORDER

13. Anyone served with or notified of this order may apply to the court at any time to vary or discharge this order (or so much of it as affects that person), but they must first inform the Applicant's solicitors. If any evidence is to be relied upon in support of the application, the substance of it must be communicated in writing to the Applicant's solicitors in advance.

INTERPRETATION OF THIS ORDER

14. A Respondent who is an individual who is ordered not to do something must not do it himself or in any other way. He must not do it through others acting on his behalf or on his instructions or with his encouragement.

15. A Respondent which is not an individual which is ordered not to do something must not do it itself or by its directors, officers, partners, employees or agents or in any other way.

PARTIES OTHER THAN THE APPLICANT AND RESPONDENT

16. Effect of this order

It is a contempt of court for any person notified of this order knowingly to assist in or permit a breach of this order. Any person doing so may be imprisoned, fined or have their assets seized.

17. Set off by banks

This injunction does not prevent any bank from exercising any right of set off it may have in respect of any facility which it gave to the respondent before it was notified of this order.

18. Withdrawals by the Respondent

No bank need enquire as to the application or proposed application of any money withdrawn by the Respondent if the withdrawal appears to be permitted by this order.

[For worldwide injunction]

19. Persons outside England and Wales

(1) Except as provided in paragraph (2) below, the terms of this order do not affect or concern anyone outside the jurisdiction of this court.

(2) The terms of this order will affect the following persons in a country or state outside the jurisdiction of this court –

(a) the Respondent or his officer or agent appointed by power of attorney;

(a) any person who –

(i) is subject to the jurisdiction of this court;

(ii) has been given written notice of this order at his residence or place of business within the jurisdiction of this court; and

(iii) is able to prevent acts or omissions outside the jurisdiction of this court which constitute or assist in a breach of the terms of this order; and

(b) any other person, only to the extent that this order is declared enforceable by or is enforced by a court in that country or state.

[For worldwide injunction]

20. Assets located outside England and Wales

Nothing in this order shall, in respect of assets located outside England and Wales, prevent any third party from complying with –

(1) what it reasonably believes to be its obligations, contractual or otherwise, under the laws and obligations of the country or state in which those assets are situated or under the proper law of any contract between itself and the Respondent; and

(2) any orders of the courts of that country or state, provided that reasonable notice of any application for such an order is given to the Applicant's solicitors.

COMMUNICATIONS WITH THE COURT

All communications to the court about this order should be sent to –

[Insert the address and telephone number of the appropriate Court Office]

If the order is made at the Royal Courts of Justice, communications should be addressed as follows –

Where the order is made in the Chancery Division

Room TM 5.07, Royal Courts of Justice, Strand, London WC2A 2LL quoting the case number. The telephone number is 020 7947 6322.

Where the order is made in the Queen's Bench Division

Room WG08, Royal Courts of Justice, Strand, London WC2A 2LL quoting the case number. The telephone number is 020 7947 6010.

Where the order is made in the Commercial Court

Room EB09, Royal Courts of Justice, Strand, London WC2A 2LL quoting the case number. The telephone number is 0207 947 6826.

The offices are open between 10 a.m. and 4.30 p.m. Monday to Friday.

SCHEDULE A

Affidavits

The Applicant relied on the following affidavits –

[name] [number of affidavit] [date sworn] [filed on behalf of]

1.

2.

SCHEDULE B

Undertakings given to the court by the applicant

(1) If the court later finds that this order has caused loss to the Respondent, and decides that the Respondent should be compensated for that loss, the Applicant will comply with any order the court may make.

[(2) The Applicant will –

(a) on or before [date] cause a written guarantee in the sum of £ to be issued from a bank with a place of business within England or Wales, in respect of any order the court may make pursuant to paragraph (1) above; and

(b) immediately upon issue of the guarantee, cause a copy of it to be served on the Respondent.]

(3) As soon as practicable the Applicant will issue and serve a claim form [in the form of the draft produced to the court] [claiming the appropriate relief].

(4) The Applicant will [swear and file an affidavit] [cause an affidavit to be sworn and filed] [substantially in the terms of the draft affidavit produced to the court] [confirming the substance of what was said to the court by the Applicant's counsel/solicitors].

(5) The Applicant will serve upon the Respondent [together with this order] [as soon as practicable] –

(i) copies of the affidavits and exhibits containing the evidence relied upon by the Applicant, and any other documents provided to the court on the making of the application;

(ii) the claim form; and

(iii) an application notice for continuation of the order.

[(6) Anyone notified of this order will be given a copy of it by the Applicant's legal representatives.]

(7) The Applicant will pay the reasonable costs of anyone other than the Respondent which have been incurred as a result of this order including the costs of finding out whether that person holds any of the Respondent's assets and if the court later finds that this order has caused such person loss, and decides that such person should be compensated for that loss, the Applicant will comply with any order the court may make.

(8) If this order ceases to have effect (for example, if the Respondent provides security or the Applicant does not provide a bank guarantee as provided for above) the Applicant will immediately take all reasonable steps to inform in writing anyone to whom he has given notice of this order, or who he has reasonable grounds for supposing may act upon this order, that it has ceased to have effect.

[(9) The Applicant will not without the permission of the court use any information obtained as a result of this order for the purpose of any civil or criminal proceedings, either in England and Wales or in any other jurisdiction, other than this claim.]

[(10) The Applicant will not without the permission of the court seek to enforce this order in any country outside England and Wales [or seek an order of a similar nature including orders conferring a charge or other security against the Respondent or the Respondent's assets].]

NAME AND ADDRESS OF APPLICANT'S LEGAL REPRESENTATIVES

The Applicant's legal representatives are –

[Name, address, reference, fax and telephone numbers both in and out of office hours and e-mail]

Source: www.justice.gov.uk/courts/procedure-rules/civil/rules/pd_part25a

The development of the freezing injunction by the courts and its subsequent legitimation by Parliament demonstrate therefore that equity is not a moribund aspect of the law. It is not a 'soft' area of law, confined to the protection of family wealth. Instead it is an area of law that continues to develop, and an area of law that feeds into the content of legislation. It is an area of law that has an international dimension to it, and therefore even though it is something that originated alongside the common law of England (at a time when the law in Wales was different), it has grown into something that has a much broader significance.

Search order

Another type of interim injunction is the search order, which requires the respondent to enable the applicant to enter onto the respondent's premises, in order to inspect and remove documents and other evidence which are in the respondent's possession and which are needed in order to enable the applicant to prove his or her claim against the

respondent. It is commonly used where it is alleged that the respondent is manufacturing imitations of branded goods (pirated DVDs or fake designer clothing). Again the order is made without notice being given to the respondent.

The search order (previously known as an Anton Piller order) was first used in the case of *EMI v Pandit* [1975] 1 All ER 418 but, as with the freezing injunction, was named after the case that legitimated its use, namely *Anton Piller KG v Manufacturing Processes Ltd* [1976] Ch 55.

However, the search order is a much more draconian order than a freezing injunction, and has the potential to be far more damaging to the respondent in terms of the effect on his or her rights and civil liberties. As such, the order is granted extremely sparingly and several safeguards have been developed in order to protect the respondent. According to Lord Justice Ormerod in the *Anton Piller* case, the three main requirements are:

- an extremely strong prima facie case;
- the potential or actual damage to the applicant if the order is not made must be extremely great;
- there must be clear evidence that the respondent has in his or her possession incriminating documents or things, and there is a real possibility that he or she will destroy or dispose of such evidence before an order with notice can be made.

Lord Denning MR also took the view that a further requirement is that the order should only be granted where no real harm would occur to the respondent or his or her case. However, what this would entail is somewhat unclear. For example, in the case of *Coca Cola v Gilbey* [1995] 4 All ER 711 a search order had been granted against the respondent, who had been involved in an attempt to make and sell fake Coca-Cola products. However, he refused to disclose information about the operation because he feared that if he did so, his own safety, and that of his family would be in jeopardy. Although, this was felt to be a relevant factor in the consideration of the issue, it was felt that the interests of justice outweighed the respondent's concerns about his safety, which it was felt would be protected by the police. Lightman J explains:

> I accept that the risk of violence if disclosure is made is a factor to be taken into account. The question at issue is its weight . . . I cannot think that in any ordinary case where the plaintiff has a pressing need for the information in question, the existence of the risk of violence against the potential informant should outweigh the interest of the plaintiff in obtaining the information. In case of any unlawful threat or action directed at a party, a witness or their families, the rule of law requires that the law should in no wise be deflected from following its ordinary course and the court should proceed undeterred. Police protection is the appropriate remedy and (if the person responsible is detected) proceedings for contempt should be instituted. In a case such as the present where the evidence establishes that the person possessed of the information was a party to the infringement and passing off complained of in the action (and indeed his participation is not challenged in his evidence), I cannot think that the fact that his associates and fellow tortfeasors have a propensity towards violence and a willingness to resort to extreme measures can exempt him from the ordinary obligation imposed upon such a tortfeasor to provide the information necessary to protect and preserve the interests of the victim. The interests of the victim must prevail.
>
> The public interest (which has also to be taken into the equation) likewise requires the same result. In particular there is the public interest (1) in the suppression as soon as

possible of the fraud on the public involved in the sale to the public of the counterfeit product; (2) that tortfeasors should not have the comfort that they can avoid the obligation to make disclosure by pleading risk of danger to themselves; (3) that men of violence should not be able by threats to silence those with knowledge of their wrongdoing; and (4) that the evil men of violence who run or are behind the organisation (of whose identities Mr Pericleous states he is aware) should be identified and promptly and effectively dealt with.

Lightman J indicates very clearly therefore that the law's primary concern is the interests of the victim – it is what the victim requires, and it is also what Lightman J considers the public interest to require. He also imposes responsibility onto the defendant whose own conduct has put him at this risk. It would therefore appear that unless there is evidence that issuing the order would put the defendant in real danger that is not of his own doing, that the element of risk to the defendant is only a minimal consideration in the court's reasoning.

Material obtained as a result of the search order can only be used against the respondent in the proceedings in relation to which the order is sought – in other words it cannot be used for any other criminal or civil proceedings. If criminal activity is suspected, it is a matter for the police to obtain a search warrant if they suspect that evidence is present on the respondent's premises.

As with the freezing injunction, the search order is another type of remedy that developed in the courts and then, later, acquired a statutory basis. Section 7 of the Civil Procedure Act 1997[39] gives the search order a statutory basis. It provides that the aims of the order are:

- to preserve evidence which is or which may be relevant;
- to preserve property which is or which may be the subject of the proceedings.

In the late seventies and early eighties, search orders were 'regularly applied for and granted in all divisions of the High Court' according to Mr Justice Scott in the case of *Columbia Pictures Industries v Robinson* [1986] 3 All ER 338. He felt that the balance had swung too far in favour of the search order applicant, and that the respondent (usually, though not always the defendant in the litigation) was being deprived of fundamental rights. Accordingly, Scott J sought to introduce stricter guidelines regarding when a search order should be granted, and emphasised that a search order should only be granted sparingly. Although the rules governing the operation of search orders were originally developed by the courts in cases such as *Rank Film Distributors Ltd v Video Information Centre* [1982] AC 380 and *Columbia Picture Industries Inc v Robinson* [1987] Ch 38 these have now been incorporated into the Civil Procedure Rules. Part 25 of the Civil Procedure Rules, and specifically Practice Direction 25A, provides extensive safeguards for the respondent, such as the fact the order must be carried out by an experienced supervising solicitor, who cannot be the applicant's solicitor, or anyone working for the same firm as the applicant's solicitor, but who is familiar with the operation of search orders and who must explain in plain everyday language what the order means and its effect. The respondent must also be informed of his or her right to seek legal advice, provided that he or she does so at once.

[39] (1997 c.12).

EXTRACT

Ministry of Justice (2012) Practice Direction 25A – Interim Injunctions

SEARCH ORDERS

7.1 The following provisions apply to search orders in addition to those listed above.

7.2 The Supervising Solicitor

The Supervising Solicitor must be experienced in the operation of search orders. A Supervising Solicitor may be contacted either through the Law Society or, for the London area, through the London Solicitors Litigation Association.

7.3 Evidence:

(1) the affidavit must state the name, firm and its address, and experience of the Supervising Solicitor, also the address of the premises and whether it is a private or business address, and

(2) the affidavit must disclose very fully the reason the order is sought, including the probability that relevant material would disappear if the order were not made.

7.4 Service:

(1) the order must be served personally by the Supervising Solicitor, unless the court otherwise orders, and must be accompanied by the evidence in support and any documents capable of being copied,

(2) confidential exhibits need not be served but they must be made available for inspection by the respondent in the presence of the applicant's solicitors while the order is carried out and afterwards be retained by the respondent's solicitors on their undertaking not to permit the respondent –

(a) to see them or copies of them except in their presence, and

(b) to make or take away any note or record of them,

(3) the Supervising Solicitor may be accompanied only by the persons mentioned in the order,

(4) the Supervising Solicitor must explain the terms and effect of the order to the respondent in everyday language and advise him –

(a) of his right to take legal advice and to apply to vary or discharge the order; and

(b) that he may be entitled to avail himself of –

(i) legal professional privilege; and

(ii) the privilege against self-incrimination.

(5) where the Supervising Solicitor is a man and the respondent is likely to be an unaccompanied woman, at least one other person named in the order must be a woman and must accompany the Supervising Solicitor, and

(6) the order may only be served between 9.30 a.m. and 5.30 p.m. Monday to Friday unless the court otherwise orders.

7.5 Search and custody of materials:

(1) no material shall be removed unless clearly covered by the terms of the order,

(2) the premises must not be searched and no items shall be removed from them except in the presence of the respondent or a person who appears to be a responsible employee of the respondent,

(3) where copies of documents are sought, the documents should be retained for no more than 2 days before return to the owner,

(4) where material in dispute is removed pending trial, the applicant's solicitors should place it in the custody of the respondent's solicitors on their undertaking to retain it in safekeeping and to produce it to the court when required,

(5) in appropriate cases the applicant should insure the material retained in the respondent's solicitors' custody,

(6) the Supervising Solicitor must make a list of all material removed from the premises and supply a copy of the list to the respondent,

(7) no material shall be removed from the premises until the respondent has had reasonable time to check the list,

(8) if any of the listed items exists only in computer readable form, the respondent must immediately give the applicant's solicitors effective access to the computers, with all necessary passwords, to enable them to be searched, and cause the listed items to be printed out,

(9) the applicant must take all reasonable steps to ensure that no damage is done to any computer or data,

(10) the applicant and his representatives may not themselves search the respondent's computers unless they have sufficient expertise to do so without damaging the respondent's system,

(11) the Supervising Solicitor shall provide a report on the carrying out of the order to the applicant's solicitors,

(12) as soon as the report is received the applicant's solicitors shall –

(a) serve a copy of it on the respondent, and

(b) file a copy of it with the court, and

(13) where the Supervising Solicitor is satisfied that full compliance with paragraph 7.5(7) and (8) above is impracticable, he may permit the search to proceed and items to be removed without compliance with the impracticable requirements.

7.6 General

The Supervising Solicitor must not be an employee or member of the applicant's firm of solicitors.

7.7 If the court orders that the order need not be served by the Supervising Solicitor, the reason for so ordering must be set out in the order.

7.8 The search order must not be carried out at the same time as a police search warrant.

7.9 There is no privilege against self incrimination in –

(1) Intellectual Property cases in respect of a 'related offence' or for the recovery of a 'related penalty' as defined in section 72 Senior Courts Act 1981;

(2) proceedings for the recovery or administration of any property, for the execution of a trust or for an account of any property or dealings with property, in relation to –

(a) an offence under the Theft Act 1968 (see section 31 of the Theft Act 1968[6]); or

(b) an offence under the Fraud Act 2006 (see section 13 of the Fraud Act 2006[7]) or a related offence within the meaning given by section 13(4) of that Act – that is, conspiracy to defraud or any other offence involving any form of fraudulent conduct or purpose; or

(3) proceedings in which a court is hearing an application for an order under Part IV or Part V of the Children Act 1989 (see section 98 Children Act 1989).

However, the privilege may still be claimed in relation to material or information required to be disclosed by an order, as regards potential criminal proceedings outside those statutory provisions.

7.10 Applications in intellectual property cases should be made in the Chancery Division.

7.11 An example of a Search Order is annexed to this Practice Direction. This example may be modified as appropriate in any particular case.

Source: http://www.justice.gov.uk/courts/procedure-rules/civil/rules/pd_part25a

As with freezing injunctions, the applicant must give an undertaking in damages and an undertaking to issue the claim as soon as possible, as well as an undertaking that the material obtained must not be used for any other purpose than the litigation in relation to which the order is sought, as Lord Browne-Wilkinson confirms in *EMI Records Ltd v Spillane and others* [1986] 2 All ER 1016.

Following the case of *Guess? Inc v Lee Sek Mon* [1987] FSR 125, it was held that where there had been non-disclosure of material facts on the part of the applicant, it was a matter for the judge's discretion as to whether the yield of the search order could be used. However, even where the non-disclosure had been inadvertent, and that it had not been for improper motives, the court should be extremely wary of allowing the applicant to have the benefit of the material retrieved by the search order. The reason for this is because the damage done by a search order cannot be undone once the material has been seen, the courts should be reluctant to allow the applicant to use it if it has been obtained in a manner that is in any way unfair to the respondent.

Orders ancillary to a search order may be: an application for a freezing injunction; an injunction to ensure a defendant remains accessible; and a disclosure order. A freezing injunction would be used where the claimant wishes to search the defendant's premises for evidence of assets, with a view to freezing them in order to prevent them from being dissipated or concealed pending trial. In the case of *Bayer v AG Winter* [1986] 1 All ER 733 the respondent was restrained from leaving the jurisdiction for a specified period of time, and to deliver his passport. In this case, the claimants suspected that the defendant was in possession of certain information that would be difficult for them to obtain if the defendant was able to leave the jurisdiction. Accordingly, the injunction was granted in order to ensure that the defendant remained accessible. Finally, a disclosure order may be used to compel the defendant to disclose the whereabouts of particular information. Therefore, where it is suspected that counterfeit goods are being produced, a disclosure order may be necessary in order to identify where the goods are being manufactured.

ACTIVITY

1. If you were acting for the claimant in an application for an interim injunction, what would be the advantages to your client of obtaining a freezing injunction or a search order?
2. Think of five types of situation where applying for a freezing injunction might be appropriate. You might find it helpful to search for cases containing the key words 'freezing injunction'.
3. Think of five types of situation where applying for a search order might be appropriate.
4. You might find it helpful to search for cases containing the key words 'search order'.

5. If you were acting for the defendant in an application for a freezing injunction or a search order, what would be the disadvantages of being the subject matter of a freezing injunction or a search order? Do you consider that the effects of a search order can be undone once the claimant has seen the evidence against you? How can the law protect against this?
6. Does the law achieve a fair balance between the interests of the claimant and the defendant in relation to freezing injunctions and search orders? If yes, what arguments would you put forward in favour of this point of view? If not, what arguments would you put forward to oppose this point of view?

Specific performance

In most cases an award of damages will be an adequate remedy for a breach of contract because it will enable the claimant to purchase the goods from an alternative supplier. In essence, the award of damages puts the claimant into the position in which he or she would have been if the contract had been performed. However, damages will not always provide adequate recompense for the loss that has been sustained. Specific performance is an order requiring the defendant to perform the contract according to its terms, rather than paying damages to the claimant. Specific performance may be awarded where damages would be inadequate, as Lord Hoffmann indicates in the case *of Co-operative Insurance Society Ltd v Argyll* [1997] 3 All ER 297, where he says at p.301:

> Specific performance is traditionally regarded in English law as an exceptional remedy as opposed to the common law damages to which a successful plaintiff is entitled as of right . . . the power to decree specific performance was . . . to do justice in cases in which the remedies available at common law were inadequate . . .

Specific performance is often granted where the subject matter of the contract is unique, for example as with the case of contracts relating to land, in respect of which, according to the case of *AMEC Properties Ltd v Planning Research and Systems PLC* [1992] BCLC 1149 specific performance is a remedy that is granted as a matter of course. Other examples where specific performance is appropriate are:

- Contracts for unique personal property, as in the case of *Falcke v Gray* (1859) 4 Drew 651 which was concerned with two unusual oriental jars (although on other grounds specific performance was not granted in this case). Nevertheless, the jars were so rare that the buyer was not in a position to be able to contract with an alternative supplier.
- Where, although it is theoretically possible to use the award of damages to buy a replacement, in practical terms this is almost impossible – as in *Sky Petroleum v VIP Petroleum* [1974] 1 All ER 954.

In this case, the defendant and the claimant had contracted for the sale and purchase of petrol. Petrol prices increased significantly during the 1970s and therefore the defendant sought to terminate the contract, because the price at which it had agreed to sell petrol to the claimant was significantly lower than the price that would have been paid by a new buyer. Accordingly, the claimant sought specific performance in order to compel the defendant to sell at the agreed price. In principle, it would have been possible for the claimant to obtain petrol from another supplier. However, because the situation at the time was such that petrol was scarce and prices exceptionally high, Goulding J considered that it would be appropriate for him to grant an order of specific performance.

- Where it would be difficult to quantify how much should be payable in damages.
- Where any damages awarded would be nominal. In other words, where the loss sustained by the claimant is very small, then it is likely that damages would not adequately compensate the claimant for the loss sustained. An example of this might be in the situation of a contract for the sale and purchase of something that has very little monetary value, but which has considerable sentimental value to the claimant.

However, there are certain things that will not normally be the subject of an order for specific performance, examples being a contract of employment[40] (where requiring the contract to be performed would be akin to slavery) or an order requiring the carrying on of a business, as this would require constant supervision on the part of the court. An example of this may be seen in the case of *Ryan v Mutual Tontine Westminster Chambers Association* [1893] 1 Ch 116. The defendants owned a block of flats, in respect of which they had promised to provide a 24-hour portering service. The court declined to order specific performance as the building would need to be supervised constantly to ensure compliance. In *Co-operative Insurance Society Ltd v Argyll Stores (Holdings) Ltd* [1997] 3 All ER 297 Lord Hoffmann explained the court's reluctance to grant specific performance. Even though the physical supervision was not required, it was felt that the arrangement would be the subject of repeated applications to the court, and that therefore specific performance would ultimately prove to be an expensive course of action for the parties and the legal system.

Nevertheless, it has since been argued that where the obligation can be performed with sufficient precision, specific performance should be available as a remedy. For example in the case of *Posner v Scott Lewis* [1987] Ch 25 specific performance could be awarded if the following criteria could be met

(a) is there a sufficient definition of what has to be done in order to comply with the order of the court?

(b) Will enforcing compliance involve superintendence by the court to an unacceptable degree?

(c) what are the respective prejudices or hardships that will be suffered by the parties if an order is not made?[41]

Other aspects that will not be the subject of specific performance are agreements made without consideration being given (remember – equity will not assist a volunteer),[42] contracts where the terms of the agreement are insufficiently precise and contracts for transient interests,[43] such as where a contract is made in relation to tickets to watch a football match. Clearly, once is has become clear that the defendant is not going to perform his obligation, the match has already taken place, and specific performance is ineffective.

Specific performance and the mandatory injunction

In many respects, the remedy of specific performance is similar to a mandatory injunction. However, there are some key differences. Specific performance can only be used in relation to positive contractual obligations, whereas the mandatory injunction can be

[40] *Page One Records Ltd v Britton* [1967] 3 All ER 822.
[41] Mervyn Davies J [1987] Ch 25 at p. 36.
[42] *Penn v Lord Baltimore* (1750) 1 Ves Sen 444.
[43] *Watts v Spence* [1975] 2 All ER 528.

used in a wider range of circumstances. Consider for example the search order – this is a mandatory injunction that is not dependent on a contract subsisting between the claimant and the defendant. Nevertheless, the fact that the remedy of specific performance is limited to contractual obligations does not preclude the claimant for applying for a mandatory injunction, which may be more appropriate in some cases where a contract has been breached. For example, specific performance cannot be granted on an interim basis, whereas an injunction can. Therefore an injunction may be awarded in order to prevent removal of the subject matter of the contract from the jurisdiction.[44]

Also, a mandatory injunction may be appropriate in situations where a court is unlikely to order specific performance. For example, an injunction may be more effective than specific performance as a means of preventing an employee from accepting work with a rival employer, as in the case of *Warner Brothers v Nelson* [1937] 1 KB 209. Therefore, if the defendant is prevented from working for a rival employer, then in practice it may become necessary for him to continue working for the claimant, with the result that the court cannot compel slavery, but it can nevertheless restrict the defendant's alternative options, thus ensuring that the defendant cannot realistically do anything but work for the claimant.

EXTRACT

Warner Brothers v Nelson [1937] 1 KB 209

Case facts

The defendant, a film actress, entered into a contract with the claimant film production company. She agreed to work exclusively for Warner Brothers, and not to work for any other film company. She breached the contract, and the defendants sought an order for specific performance.

Branson J

It is conceded that our Courts will not enforce a positive covenant of personal service; and specific performance of the positive covenants by the defendant to serve the plaintiffs is not asked in the present case. The practice of the Court of Chancery in relation to the enforcement of negative covenants is stated on the highest authority by Lord Cairns in the House of Lords in *Doherty v. Allman* [(1878) 3 App Cas 709]. His Lordship says: 'My Lords, if there had been a negative covenant, I apprehend, according to well-settled practice, a Court of Equity would have had no discretion to exercise. If parties, for valuable consideration, with their eyes open, contract that a particular thing shall not be done, all that a Court of Equity has to do is to say, by way of injunction, that which the parties have already said by way of covenant, that the thing shall not be done; and in such case the injunction does nothing more than give the sanction of the process of the Court to that which already is the contract between the parties. It is not then a question of the balance of convenience or inconvenience, or of the amount of damage or of injury – it is the specific performance, by the Court, of that negative bargain which the parties have made, with their eyes open, between themselves . . . Nor will the Court, true to the principle that specific performance of a contract of personal service will never be ordered, grant an injunction in the case of such a contract to enforce negative covenants if the effect of so doing would be to drive the defendant either to starvation or to specific performance of the positive covenants: see *Whitwood Chemical Co. v. Hardman* [[1891] 2 Ch 416] . . . where a contract of personal service contains negative covenants the enforcement of

[44] *Hart v Herwig* (1873) 8 Ch App 860.

which will not amount either to a decree of specific performance of the positive covenants of the contract or to the giving of a decree under which the defendant must either remain idle or perform those positive covenants, the Court will enforce those negative covenants; but this is subject to a further consideration. An injunction is a discretionary remedy, and the Court in granting it may limit it to what the Court considers reasonable in all the circumstances of the case . . . this Court never will enforce an agreement by which one person undertakes to be the servant of another; and if this agreement were enforced in its terms, it would compel this gentleman personally to serve the plaintiffs for the period of ten years. That the Court never does. Therefore an injunction in these terms cannot be granted, although the agreement to serve the plaintiffs and give his whole care, time, and attention to their business, and not to engage in any other business during his engagement,
is valid in point of law. But the plaintiffs do not ask for an injunction in the terms of that agreement.' Before parting with that case, I should say that the Court there proceeded to sever the covenants and to grant an injunction, not to restrain the defendant from carrying on any other business whatsoever, but framed so as to give what was felt to be a reasonable protection to the plaintiffs and no more. The plaintiffs waived an option which they possessed to extend the period of service for an extra five years, and the injunction then was granted for the remaining period of unextended time . . . The case before me is, therefore, one in which it would be proper to grant an injunction unless to do so would in the circumstances be tantamount to ordering the defendant to perform her contract or remain idle or unless damages would be the more appropriate remedy . . . With regard to the first of these considerations, it would, of course, be impossible to grant an injunction covering all the negative covenants in the contract. That would, indeed, force the defendant to perform her contract or remain idle; but this objection is removed by the restricted form in which the injunction is sought. It is confined to forbidding the defendant, without the consent of the plaintiffs, to render any services for or in any motion picture or stage production for any one other than the plaintiffs. This appears from the judgment of Lord St. Leonards in *Lumley v. Wagner* [(1852) 5 De G & Sm 485], where he used the following language: 'It was objected that the operation of the injunction in the present case was mischievous, excluding the defendant J. Wagner from performing at any other theatre while this Court had no power to compel her to perform at Her Majesty's Theatre. It is true, that I have not the means of compelling her to sing, but she has no cause of complaint, if I compel her to abstain from the commission of an act which she has bound herself not to do, and thus possibly cause her to fulfil her engagement . . .'

Outcome

An injunction was granted preventing the claimant from breaching the terms of the contract.

Another point to note about specific performance is that although it relates to contractual obligations, it is not vital for the contract to have been breached in order for the court to order specific performance. Consider the case of *Marks v Lilley* [1959] 2 All ER 647 for example. Here the claimant and the defendant had entered into a contract for the sale and purchase of land. The defendant did not complete the transaction on the agreed date. However, this was not a breach of the contract, as the completion date was not a crucial term in the contract – time was not of the essence. However, the claimant was entitled to the remedy of specific performance – he could require the defendant to perform his obligations in accordance with the terms of the contract.

Although specific performance is only awarded where damages would be inadequate, sometimes it is necessary to award damages or some other remedy in lieu of specific performance. In the case of *Johnson v Agnew* [1980] AC 367 for example the claimant and the defendant entered into a contract for the sale and purchase of land. The claimant

obtained an order for specific performance requiring the land to be transferred to the defendant. However, the defendant delayed in effecting payment for the land, and the mortgage lenders who had issued loans in respect of the land took steps to sell the land to recover their loan. Clearly, the claimant could not therefore require that the defendant completed on the sale of the land – the land had already been sold. Accordingly it was possible for the claimant to be awarded damages instead of specific performance. The case of *Shelfer v City of London Electric Lighting Company* [1895] 1 Ch 287 sets out some guidelines where although an equitable remedy may be theoretically possible, damages are a more appropriate remedy. Situations where damages are a more appropriate remedy than an equitable remedy are:

- where the damage to the claimant is small;
- where the damage to the claimant can be evaluated in monetary terms;
- where financial compensation would provide an adequate remedy;
- where granting an injunction/specific performance would result in undue hardship for the defendant.

Subrogation

The remedy of subrogation applies when a third party pays a debt owed by a debtor to a creditor. The third party is then able to claim any assets that the debtor gave as security for the loan. An example of this can be seen in the case of *Filby v Mortgage Express (No 2)* [2004] EWCA Civ 759. Here, a married couple bought their house by way of a mortgage. Later, the husband paid off the mortgage using money obtained from another loan. He did this by forging his wife's signature on the application. She therefore claimed that she had no obligation to repay this loan, but the court held that the second lender took the place of the first, and that therefore, just as the house was a security for the original mortgage, it could also be used as security in the case of the second mortgage.

Rectification

Equity, because of its focus on looking to the substance rather than the form, can apply the remedy of rectification to provide relief in cases where a mistake or fraud has been operative. In other words, it is used where a written document fails to reflect the true nature of the parties' agreement. An example can be seen in the case of *Joscelyne v Nissen* [1970] 2 QB 86 where a woman and her father had entered into an arrangement whereby the daughter would pay the household expenses. The daughter later refused to do so, on the basis that this was not what the written form of their agreement stated. The court ordered that the written form of the agreement could be rectified. Generally rectification is used where the document fails to reflect what was the common intention of the two parties, and will not generally be available where there is an unilateral mistake on the part of one of the parties.

Rescission

Rescission allows a party to a contract to have the contract set aside and for him or her to be returned to his or her original (pre-contractual) position. This differs from rescission

at common law, which refers to some factor that means that the contract never came into existence. Rescission in equity is where the contract has been created, but is later set aside because of mistake, misrepresentation or undue influence. An example of a contract being rescinded for mistake can be seen in the case of *Cooper v Phibbs* (1867) LR 2 HL 149. Here the parties entered into a contract for a lease and operated on the basis that the lessee had no equitable right over the land that was to be leased. It turned out that this was not the case, and the parties sought to rescind the agreement on the basis that they had been operating under a common mistake as to the nature of the lessee's rights over the land. Rescission was allowed. The equitable remedy of rescission is applicable in relation to contracts that are voidable, in other words, contracts that were seemingly validly created, and then rescinded. Rescission can only occur where it is possible to restore the parties to their original positions, and is not therefore available where it is not possible to do this. Neither is rescission available where the party is deemed to have accepted the breach, or where third parties have acquired rights in the property in good faith and for value. Remember also that delay defeats equity, and therefore rescission must occur within a reasonable time.

Other equitable remedies

Other equitable remedies include account, where the court assesses how much is owed by one party to another, or the appointment of a receiver, which may be awarded in order to preserve property in danger or to ensure payment of a debt where other remedies are inadequate. Account might be used where there has been a breach of trust, where the trustee must repay the beneficiary the amount owed, as well as any gain that has been made by the trustee while the beneficiary's money was in his or her possession. Another possibility is for the court to require that a document is delivered to it and cancelled, which is used in situations where an apparently valid document is voidable by virtue of being fraudulent. Finally there is *ne exeat regno* – an order that enables a debtor to be arrested if he or she is about to leave the jurisdiction without paying the debt. Clearly this is very draconian, and is seldom used, especially where a freezing injunction would have the same effect.

Chapter summary

This chapter may be useful for assignments and assessments on:

- Equity's capacity to innovate
- The relationship between equity and the common law
- Equity's role
- The differences in approach between equity and the common law.

Further reading

Hayton, D. (2012) 'The Extent of Equitable Remedies: Privy Council v Court of Appeal' 33(6) *The Company Lawyer* 161.

Herman, S. (2003) 'Specific Performance: A Comparative Analysis: Part 1' 7(1) *Edinburgh Law Review* 5.

Herman, S. (2003) 'Specific Performance: A Comparative Analysis: Part 2' 7(2) *Edinburgh Law Review* 194.

Martin, J.E. (1993) 'Subrogation and the insurer's lien' 143 *New Law Journal* 1061.

McGrath, P. (2012) 'The freezing injunction: a constantly evolving jurisdiction' *Civil Justice Quarterly* 12.

Smith, M. (2007) 'Rectification of contracts for common mistake: Joscelyne v Nissen and subjective states of mind' *Law Quarterly Review* 116.

Part 2

The trust

6

An overview of trusts

Chapter outline

This chapter will cover:

- The historical development of the trust
- Creating a valid trust
- Reasons for creating a trust
- The characteristics of a trust
- The trust compared with other types of legal relationship.

Introduction

In this chapter, the concept of the trust will be introduced. The trust is the most important invention of equity and, as will be seen, the remainder of this book will be devoted almost exclusively to the intricacies of the trust concept. However, although the operation of the law of trusts is complex and intricate, its core principle is extremely simple. The essence of the trust is that one person owns property for the benefit of another. That is all. Lear is the legal owner of a piece of property, whether that is land, chattels, money, choses in action etc. for the benefit of Cordelia, who is regarded as the owner in equity. Cordelia acquires all the advantages of ownership but none of the responsibility. Lear has all the responsibilities of ownership, but none of the attendant advantages. This simple principle has been adapted to apply to a vast array of different situations, and in order to fulfil a wide range of different functions, but its essential characteristic – ownership of X by A for the benefit of B remains constant throughout the law of trusts.

The historical origins of the trust

The origins of the trust in the law of England and Wales is extremely old, and even as early as the sixth century AD, there is evidence of property being owned *ad opus* – meaning 'on his behalf' and this appears to have been recognised in law, although Maitland[1] suggests that this relationship was more similar to the modern concept of agency than the modern notion of a trust. There is also an indication that the arrangement was generally a temporary situation, such as where the owner of a fee simple wishes to convert the fee into a fee tail. He could not simply change the nature of the fee. It was necessary to convey the fee simple to a friend to the use of (*ad opus*) the original owner, and the friend would reconvey the land in tail.

However, by the 13th century, it becomes evident that land is being held by A *ad opus* B on a permanent basis. During this period Franciscan friars came to England, and their vows of poverty meant that they were not permitted to own land either individually or collectively. However others could own land *ad opus* the friars.

By the 14th century, the 'use' as it came to be known was being used in other situations as well. For example, during this period, a person could not transfer land by will. The reason for this was that the law required that land was to be inherited by one's eldest son. However, for families who had other children, this situation was extremely unsatisfactory, especially if it was feared that the eldest son would not provide for his siblings – and would feel even less of an obligation to provide for his half-siblings. Accordingly, the use was employed in order to convey the land to a friend, to the use of the original owner, and then in accordance with the owner's directions on the owner's death (for example in order to provide for the deceased's spouse and for the deceased's children). This mechanism had been employed for many years as regards chattels, but its adoption in relation to land is a significant milestone in the development of the trust.

A further advantage of the use was that it was a clever method of avoiding a number of taxes that would become payable on death. If the land was conveyed to a group of co-owners (known as feoffees) rather than to one individual, the taxes that would become payable if land was inherited by a minor could be avoided. If the land was owned by a group of feoffees, who could be replaced if one died, the land was never inherited

[1] Maitland, F.W. (1949) *Equity: A Course of Lectures.* Cambridge: Cambridge University Press, p.24.

by a minor, and therefore no taxes were owed. Over time, it came to be realised that this simple mechanism was extremely flexible and very advantageous as a means of preserving wealth, and minimising or avoiding tax.

This system would have been undermined significantly if the common law had been able to recognise who the 'true' owner was, and to identify that the feoffee(s) were merely what Maitland[2] terms 'screens' or 'agents'. But the common law did no such thing. The common law merely looked at who owned the legal title to the land, and legal title to the land was owned by the feoffees. The common law therefore had no interest in the feoffor (the 'true' owner) and his family (known as the *cestuis que* use). In some ways this may be viewed as extremely advantageous to the feoffor, in that the law did not look at who was benefiting from the arrangement, and making them as liable to taxation as they would have been had they been the legal owners.

On the other hand, it could be problematic. The mechanism of the use worked well provided that the feoffees adhered to their obligation, but the common law offered no remedy if the feoffees did not keep their promise, although Maitland argues[3] that, in theory, this should not have presented any significant difficulty for the common law courts:

> The feoffee to uses did agree, as the modern trustee does agree that he will deal with the land or goods in a certain way. If therefore in the fourteenth century our law of contract had taken its modern form, I think the courts of law would have been compelled to say 'Yes, there is an agreement; therefore it is a legally enforceable contract, and if it be broken by an action for damages it will lie in the infringer.' This might well have been done if the feoffee had covenanted by deed to observe the confidence that was reposed in him; and in case there was no deed any difficulty arising from want of consideration might have been evaded with a little ingenuity.

Enforcing the use therefore fell to the Chancellor, who recognised that which the courts of law did not, namely that the feoffees had *agreed* to own the land to the use of the feoffor, and even though there was no consideration that would provide the feoffee with any benefit, the detriment to the feoffor was significant, because he transfers the title to his land on the basis of the agreement. Therefore because '*men ought to fulfil their promises, their agreements; and they ought to be compelled to do so*'[4] the Chancellor began to enforce the feoffee's promise in the same way, and for the same justification, as contracting parties were compelled to fulfil their promises.

It is important to note that the Chancellor could not require the transfer of the property either to the feoffor or to those whom the feoffor had directed would receive the benefit of the obligation, as this would have interfered with the concept of title at common law. Instead, the feoffee's obligation was to own the land for the benefit of the feoffor or the *cestui(s) que* use – the obligation was a personal obligation, known as an obligation *in personam*. Essentially, the feoffee remained as the owner of the asset, but could derive no personal benefit from it.

Because uses were enforced by the Chancellor, they were employed with increasing frequency, until 1535, when the Statute of Uses was enacted. Henry VIII objected to the avoidance of tax, as he was the ultimate beneficiary of any taxes paid. That they were routinely avoided was therefore extremely unsatisfactory.

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[2] Ibid., p.27.
[3] Ibid., p.28.
[4] Ibid., p.29.

Accordingly the Statute of Uses executed certain types of use. This meant that where the land was held by feoffees to the use of an infant *cestui que* use with a view to avoiding taxes that would become payable if the land was owned by an intent, execution of the use would mean that the *cestui que* use would be deemed to be the owner of the land, and therefore liable to pay any taxes owed by virtue of his minority. Yet, the Statute of Uses did not abolish uses entirely, and therefore there were a number of uses that were unaffected by the Statute. Personal chattels, copyhold tenures, certain types of leases, and active uses (whereby the feoffee was given the obligation to sell the land and give the proceeds of sale to the *cestuis que* use) were unaffected.

Uses continued to be employed therefore, especially once it was realised that the Statute of Uses did not execute that which was called the use upon a use. The use upon a use operated thus. A feoffor (Donna) would convey land to a feoffee (Russ) to the use of a *cestui que* use (Benny). The *cestui que* use (Benny) would then be directed to hold the land for the benefit of a second *cestui que* use (Lucy). The first use (Ross) owning land to the use of (Benny) was promptly executed – (Benny) became the legal owner. However, the second use – the use upon a use – was not, and therefore Donna could convey land to Benny for the benefit of Lucy.

By the 17th century, the second use was known as a trust. Therefore Donna conveyed land to Russ for the use of Benny upon trust for Lucy. Therefore, Lucy came to be known as the *cestui que* trust. The Law of Property Act 1925 repealed the Statute of Uses, with the result that there is now no need to employ the use upon a use. Gradually, the term settlor came to replace the feoffor to uses, the term trustee replaced the feoffee to uses, and although the term *cestui(s) que* trust is still in common usage, the term beneficiary is perhaps now more common and familiar.

How a trust may arise

Essentially there are four ways a trust may arise:

- intentionally,
- by implication,
- by operation of law, and
- by court imposition.

Intentionally

A trust may be created intentionally. The owner of property, known as the **settlor** (not a settler irrespective of what the autocorrect function on a computer may assert!) may transfer the trust property to a second person, known as a **trustee** for the benefit of a third person, known as the **beneficiary**. A common example of this type of trust could be a will, where the settlor creates a trust that will become operative on his or her death and require the trustee to transfer the settlor's property to the beneficiary or beneficiaries named in the will. Another example is a donation to a charitable cause. It is probable that many people have at some point in their lives donated money or goods to a charity, by way of a donation in a collection pot, sponsoring a friend or a relative to raise money or giving unwanted goods to a charity shop. The donation in each of these cases is not given to the charity for the benefit of the charity. Instead, the donation is given to enable the charity to benefit the cause for which it was established. Accordingly, a person who donates to a charity is an example of a settlor under a trust. A trust that is created intentionally is known as an express trust.

By implication

A trust may also arise by implication. In other words, the court will imply the existence of a trust from the conduct of the settlor. Such a trust may arise because the court is able to discern a common intention between the settlor and the beneficiary that a trust will be created. For example, if a couple agree that a cohabitational home belongs to both of them, even though only the settlor's name is recorded on the Land Register, the court will imply a trust (known as a constructive trust) if the beneficiary relies on this to his or her detriment. Similarly, if a person contributes to the acquisition cost of an asset – such as land, then it is implied that the person who is recorded as the owner acts as a trustee of the donor's contribution, unless it may be proved that the donation was given by way of a gift. This is called a resulting trust. A resulting trust will also arise where a trust fails, for example where the trust property is transferred to the trustee but the beneficiaries have not been identified with sufficient precision. In all these cases, the court will imply that the property is being held on a trust.

By operation of law

Alternatively, a trust may be created by the operation of law. In essence what this means is that where one puts oneself in a particular situation, then one is automatically in the relationship of a trust. For example where a couple buys a house together, they will become co-owners of that house. Co-ownership of property creates a trust whereby the co-owners are made into trustees of the trust property for the benefit of themselves and the other co-owner. Here, the settlors, the trustees, and the beneficiaries are the same people, but this does not preclude the relationship from being that of a trust. During the period of ownership, this may have very little tangible relevance. However, when the co-owners sell the trust property, the law of trusts is used to uphold the division of the proceeds of sale between the co-owners, either according to their respective contributions or according to some alternative agreement they may have reached between themselves. If one co-owner were to die, then their share of the co-owned property may need to be dealt with by the survivor as a trustee, who will own it for his or her own benefit and also for the benefit of any person(s) entitled to inherit the deceased's asset under a will or under the rules on intestacy.

Equally, where one is the director of a company, or the treasurer of a club or society, the law recognises that a trust relationship exists in that the director or the treasurer deals with property for the benefit of another (legal or human) person.

Put simply, a trust that arises through the operation of law is a relationship that the law deals with as a trust, whether or not this was the parties' intention. Essentially, what the statute says is 'if you find yourself in this situation, then you will be a trustee and a trust will exist'. Examples of trusts that arise by operation of law are s.33 Administration of Estates Act 1925 and s.34 and s.36 of the Law of Property Act 1925.

EXTRACT

Administration of Estates Act 1925, s.33

33 Trust for sale

[(1) On the death of a person intestate as to any real or personal estate, that estate shall be held in trust by his personal representatives with the power to sell it.]

(2) [The personal representatives shall pay out of-

(a) the ready money of the deceased (so far as not disposed of by his will, if any); and

(b) any net money arising from disposing of any other part of his estate (after payment of costs), all] such funeral, testamentary and administration expenses, debts and other liabilities as are properly payable thereout having regard to the rules of administration contained in this Part of this Act, and out of the residue of the said money the personal representative shall set aside a fund sufficient to provide for any pecuniary legacies bequeathed by the will (if any) of the deceased.

(3) During the minority of any beneficiary or the subsistence of any life interest and pending the distribution of the whole or any part of the estate of the deceased, the personal representatives may invest the residue of the said money, or so much thereof as may not have been distributed, [under the Trustee Act 2000].

(4) The residue of the said money and any investments for the time being representing the same, [and any part of the estate of the deceased which remains] unsold and is not required for the administration purposes aforesaid, is in this Act referred to as 'the residuary estate of the intestate.'

(5) The income (including net rents and profits of real estate and chattels real after payment of rates, taxes, rent, costs of insurance, repairs and other outgoings properly attributable to income) of so much of the real and personal estate of the deceased as may not be disposed of by his will, if any, or may not be required for the administration purposes aforesaid, may, however such estate is invested, as from the death of the deceased, be treated and applied as income, and for that purpose any necessary apportionment may be made between tenant for life and remainderman.

(6) Nothing in this section affects the rights of any creditor of the deceased or the rights of the Crown in respect of death duties.

(7) Where the deceased leaves a will, this section has effect subject to the provisions contained in the will.

The essence of this provision is that a trust is created automatically on a person's death, and that his or her property is legally owned by the personal representatives who are trustees for those who are entitled to inherit under the rules on intestacy contained in s.46 of the Administration of Estates Act 1925.[5] However, if the deceased person has written a valid will, the personal representatives will be any executors and/or trustees named in the will.

EXTRACT

Law of Property Act 1925, s.34 and s.36

34 Effect of future dispositions to tenants in common

(1) An undivided share in land shall not be capable of being created except as provided by the Settled Land Act 1925 or as hereinafter mentioned.

(2) Where, after the commencement of this Act, land is expressed to be conveyed to any persons in undivided shares and those persons are of full age, the conveyance shall (notwithstanding anything to the contrary in this Act) operate as if the land had been expressed to be conveyed to the grantees, or, if there are more than four grantees, to the four first named in the conveyance, as joint tenants [in trust for the persons interested in the land]:

[5] (1925 c.23).

Provided that, where the conveyance is made by way of mortgage the land shall vest in the grantees or such four of them as aforesaid for a term of years absolute (as provided by this Act) as joint tenants subject to cesser on redemption in like manner as if the mortgage money had belonged to them on a joint account, but without prejudice to the beneficial interests in the mortgage money and interest.

(3) A devise bequest or testamentary appointment, coming into operation after the commencement of this Act, of land to two or more persons in undivided shares shall operate as a devise bequest or appointment of the land to the personal representatives of the testator, and (but without prejudice to the rights and powers of the personal representatives for purposes of administration) [in trust for the persons interested in the land].

[(3A) In subsections (2) and (3) of this section references to the persons interested in the land include persons interested as trustees or personal representatives (as well as persons beneficially interested).]

(4) . . .

36 Joint tenancies

(1) Where a legal estate (not being settled land) is beneficially limited to or held in trust for any persons as joint tenants, the same shall be held [in trust], in like manner as if the persons beneficially entitled were tenants in common, but not so as to sever their joint tenancy in equity.

(2) No severance of a joint tenancy of a legal estate, so as to create a tenancy in common in land, shall be permissible, whether by operation of law or otherwise, but this subsection does not affect the right of a joint tenant to release his interest to the other joint tenants, or the right to sever a joint tenancy in an equitable interest whether or not the legal estate is vested in the joint tenants:

Provided that, where a legal estate (not being settled land) is vested in joint tenants beneficially, and any tenant desires to sever the joint tenancy in equity, he shall give to the other joint tenants a notice in writing of such desire or do such other acts or things as would, in the case of personal estate, have been effectual to sever the tenancy in equity, and thereupon [the land shall be held in trust on terms] which would have been requisite for giving effect to the beneficial interests if there had been an actual severance.

[Nothing in this Act affects the right of a survivor of joint tenants, who is solely and beneficially interested, to deal with his legal estate as if it were not held [in trust].]

(3) Without prejudice to the right of a joint tenant to release his interest to the other joint tenants no severance of a mortgage term or trust estate, so as to create a tenancy in common, shall be permissible.

Therefore, where land is co-owned, the Law of Property Act 1925 operates to create a trust, whereby the legal owners own the property on trust for themselves and the other legal co-owners, or in the case of a tenancy in common the other grantees or those who are entitled to inherit their share.

Trust imposed by the court

The third possibility is that a relationship may be recognised as that of a trust through the intervention of the courts. An example of this might arise where a person moves in with

his or her partner in order to cohabit. The partner is the owner of the home. However, where the parties' conduct, either by virtue of an agreement or by contributions to the acquisition cost, gives rise to an expectation of a shared entitlement, the courts may declare that the homeowner is a trustee of the house for the benefit of him or herself and his or her cohabitant. In other words, what happens here is that the courts either create a trust in order to rectify a relationship or a transaction that has resulted in an actionable loss to the claimant, or they will identify a trust as having been created on a particular date, and formally recognise its existence. In this way, the trust is used as a form of remedy.

This type of trust is known as an implied trust, and takes two forms: the first being a resulting trust, whereby the trust fund reverts – or results – back to the settlor. A resulting trust would arise by implication where a trust fails, such as where a legacy is left in a will to a beneficiary who predeceases the settlor. A resulting trust may also arise where a person has made a contribution to the purchase of an asset such as land. When the land is sold there is an expectation that the contributor expects to be given a share of the proceeds of sale proportionate to his or her contribution. A second type of implied trust is a constructive trust, whereby the court construes a trust as having arisen in order to prevent a person from unconscionably denying another that to which they have been led to understand that they are entitled. A constructive trust may arise where a cohabitant has contributed to the acquisition cost of the home, and has relied to his or her detriment on the understanding that ownership would be shared. A constructive trust may also be imposed where a person has acted fraudulently in order to deprive another of an entitlement. Resulting and constructive trusts will be discussed further in Chapters 14 and 22.

Reasons for creating a trust

These different mechanisms for creating a trust help to explain why a trust might be created. A trust might be created intentionally in order to provide for people who would not otherwise be capable of owning property on their own behalf. Accordingly, a parent might wish to create a trust intentionally in order to provide for a child who is unable to own property on their own behalf, either for reasons of youth or, if the child has reached adulthood, or a parent may wish to provide for them because of their incapacity, or simply from a desire to protect one's offspring from their own capriciousness and folly. This is an example of what is known as an express trust, and may be created during one's lifetime (known as an *inter vivos* trust) or in a will.

Similarly, the trust could be used as a mechanism for providing for an adult beneficiary or beneficiaries in the event of the settlor's death. Accordingly, a settlor may wish to provide for his or her spouse, or to provide financial security for a person such as a cohabitant who would not automatically inherit under the intestacy rules (discussed in Chapter 15) in the event of a person's death.

Another motivation is privacy. Whereas a will becomes a public document on the death of the settlor, a trust does not. Accordingly, a trust may be a way of ensuring that secrets remain hidden from view after one's death – something that may be advantageous if a person has children that he or she does not want to acknowledge openly either to one's 'legitimate' family or to the press.

Trusts are also used in a range of commercial contexts as well. For example the *Quistclose*[6] trust may be used in order to ringfence money paid by customers for

[6] *Barclays Bank Investments v Quistclose Investments Ltd* [1970] AC 567.

undispatched orders, but may also be used more widely in order to protect company assets from creditors.

Trusts also have advantages from the viewpoint of minimising the amount of tax that would otherwise be payable. If the settlor is a higher-rate tax payer, taxed at 40 per cent or even higher, then it may be beneficial to put money into the hands of trustees so as to minimise the amount of tax that would be payable, and to take advantage of any tax allowances that may be availed of. Both individuals and corporations may use the trust for the purposes of minimising the amount of tax payable. If it is done in accordance with the law, no criminal offence is committed – all the settlor does is to transfer the trust fund into the hands of a person who would, legitimately, pay less tax on it. A trust may also be created during one's lifetime in order to minimise – or eliminate the amount of inheritance tax that would be payable on it on death.

Trusts may also be used for charitable purposes. Therefore in order to facilitate a purpose that benefits the public generally, a trust will be used, as, in such circumstances, it would not be possible to fulfil the purpose by dividing the trust fund between the beneficiaries, who, being the public generally would often consist of an incalculable number.

Clubs and societies also make use of the trust. In essence, a group of people who receive money for the benefit of the group will be trustees for that group. Therefore a political party, a football supporters club or an amateur sports team are all likely to acquire money from members either in the form of subscriptions or by paying to attend events organised by the society. This money is likely to be given in the form of a trust for the benefit of the group collectively, or for the benefit of each of the group's members. If that is the case, then the law governing the relationship is a trust.

On the other hand, a trust might be imposed by the law in order to ensure that a person does not act out of self-interest when their obligation is in fact owed to another person. A pension plan and a charity are forms of trust, and it is imperative in such situations that the trustees do not act in a way that benefits their own interests because the essence of their role is to ensure that the trust assets exist for the benefit of the beneficiaries. Co-ownership of land is also a form of trust imposed by law, as is the administration of the estate of a person who has died intestate.

The trust may also be used as a remedy, in other words as a means of ensuring that a person is not able to continue to treat property as their own, when it would be unjust for them to do so. An example of this is seen above in relation to contributions by the non-owner to the acquisition cost of a cohabitational home, leading to the imposition of a constructive trust. A further example may be encountered in cases where money paid to a company that has gone into liquidation may be regarded as belonging to the donors in the event that the goods they have ordered cannot be delivered.

The parties to a trust

Accordingly, because the trust has such a wide range of usages, it is an extremely versatile legal tool. Further manifestation of its versatility may be demonstrated both by the fact that the parties to the trust relationship may be multiple, and also by the fact that one person may fulfil multiple roles within the trust relationship. Accordingly, multiple settlors may create a trust for the benefit of one person, such as where a child's parents wish to create a trust of co-owned assets for the child's benefit. Also, it is possible for trusts to have multiple trustees – and indeed this may be essential with some types of trusts, such as trusts of land, and desirable in relation to other types of trusts, such as

wills. It is also possible for a trust to have multiple beneficiaries. Accordingly, it is possible to create a trust for the benefit of multiple family members, such as a trust fund that is to be divided equally between one's children or a trust fund that allows the trustees a measure of discretion to give more money to one's neediest child.

The trust relationship also allows one person to fulfil several roles within the trust relationship. For example, a settlor may create a trust for the benefit of him- or herself. An example of this might arise where a person wishes to safeguard assets from creditors. On the other hand, it may be possible for the settlor to declare him- or herself a trustee for the benefit of a third party. Finally, it may be possible for a person to be both a trustee and a beneficiary under a trust. This will occur when there is co-ownership, as well as when one person partly contributes to the acquisition costs of the home. Figure 6.1 summarises the requirements that must be fulfilled in order for a trust to be valid, while the following discussion provides a more detailed outline of these requirements.

Characteristics

Capacity to create a trust

The person creating a trust must be capable of doing so. In other words, a trust cannot be created if the settlor lacks the capacity to create the trust,[7] or does not own the purported trust property. For example, a child cannot legally own land, and cannot therefore create a valid trust of land.[8]

Certainty of subject matter (trust property)

In order to identify that the relationship between the parties is that of a trust, certain characteristics must be identified. There must, for example, be property that is capable of being the subject of a trust. Although this aspect of the trust will be discussed in greater detail later (in Chapter 10), this requirement essentially means that ownership of the trust property is transferred to the trustee (where appropriate)[9] and that it is defined with sufficient precision,[10] and that it is capable of being owned in the manner of a trust.[11] For example, land, money and chattels may all be valid as the subject matter of a trust because the separation of legal and equitable ownership may be envisaged. Intellectual property on the other hand, or the goodwill owned by a business, may be owned and traded as assets, but could not be the subject matter of a trust because it is impossible to conceive of these assets as being owned by one person for the benefit of another.

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[7] See for example the Wills Act 1837, s.7.
[8] Law of Property Act 1925, s.1(6).
[9] *Sprange v Barnard* (1789) 2 Bro CC 585.
[10] *Re Goldcorp Exchange Ltd* [1995] AC 74.
[11] *Re Ellenborough, Towry Law v Burne* [1903] 1 Ch 697.

Certainty of intention

There must generally be an intention for a trust to come into existence.[12] With an intentionally created trust, this intention will usually (though not always, as we shall see in Chapter 10) be manifest from the settlor's actions, such as the writing and execution (i.e. the actions required for validation) of a will. With trusts imposed by the law, perhaps the intention is not necessarily to create a trust, but the intention exists to create the type of relationship that would be governed by the law of trusts. For example, the cohabitant who allows his or her partner to contribute to the cost of the couple's home may not be intending to become a trustee, but is nevertheless intending to own an asset to which more than one person has contributed, and is therefore recognised as a trustee even if this was not a consciously formed intent.

Certainty of objects

There is a need for clarity regarding who the beneficiaries of the trust are. A trust will fail if it is not possible to identify who the beneficiaries are. Sometimes this will be very precisely defined – as in the situation where a trust is created for a named individual. However, it is possible to create a trust for the benefit of a group of persons, although in this situation, as we shall see, it will be necessary to identify who falls within the group and who does not. A trust may also operate for the benefit of a purpose. However, trusts of this type will either need to be charitable (discussed further in Chapters 19–21) or for a valid purpose that is not charitable.

Workability of the trust

As a matter of practicality, the trust must be workable. Therefore, while intellectually it would be possible to create a trust whose assets are an amorphous mass, and whose beneficiaries are all the inhabitants of a large city, in the real world such a trust would be so difficult to administer that it would be impossible to determine whether it has been administered correctly.[13] The inhabitants of a large city are ever changing, through the effects of births, deaths and migration, and therefore identifying who the beneficiaries might be at any given time becomes an impossible task. Accordingly, the law requires that the trust is sufficiently small as to be manageable. Nevertheless, as with many aspects of the law, what exactly this means is imprecisely defined. The extremities may be clear – a trust for the benefit of one specific beneficiary, 'my son John', may be readily identified as workable, but a trust for 'anyone living in England' may be readily defined as unworkable. However, where precisely the dividing line between workable and unworkable is may depend entirely on the situations created by an individual, objected to by another, then litigated through the hierarchy of the courts, and decided by the Supreme Court.

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[12] *Re Williams, Williams v Williams* [1897] 2 Ch 12.

[13] *R v District Auditor No 3 Audit District of West Yorkshire Metropolitan County Council, ex p West Yorkshire Metropolitan County Council* [1986] RVR 24.

Formalities

Often there are obligations imposed by the law regarding the validity of a trust. For example, a trust of land must be in writing, and there must be at least two, and no more than four, trustees.[14] By the same token, a will must be in writing and complying with the requirements of the Wills Act 1837.[15] Nevertheless, not all trusts will require adherence to such formalities and in some situations a purely oral declaration will suffice.

Legality

A trust cannot be created for an illegal purpose or a trust that is contrary to public policy, and the courts will strike down any trust that appears to have been made for a sham purpose, such as the deliberate attempt to prevent creditors from enforcing a debt.

The trust must be completely constituted

It is also necessary, in order for a trust to be valid, for the settlor to have done everything in his or her power to completely constitute the trust. If the trust is incomplete, then there can be no obligation imposed on the trustees. Therefore, a trust under a will is incomplete until the death of the settlor, and accordingly he or she may change his or her mind about the provisions of a will at any point. Generally, in order for the trust to be completely constituted, there needs to be either an effective declaration that the settlor is a trustee, or the trust property must have been transferred to the trustee(s). Accordingly, a trust where an intention has been manifested to transfer the trust property to the trustees at some future date is not completely constituted, even though the intention to create a trust has been manifested, and the trust property and the beneficiaries have been identified. With some types of trust, the intervention of a third party will be required before the trust is completely constituted. Accordingly, with a trust of land, for example, the land must have been transferred to the trustee and the trustee must have been registered by HM Land Registry as the legal proprietor of that land. Similarly, with a trust constituted of shares, the trust will not be complete until the share transfer certificate has been issued by the company.

The trust must not offend the rule against perpetuities

Useful though the trust is as a tool, it cannot be denied that it impedes the unrestricted ownership of the asset. Both the trustee and the beneficiaries are fettered in their capacity to use and to sell the asset. Accordingly, the law will not generally allow property to be held on trust on an indefinite basis. This is known as the rule against perpetuities and the remoteness of vesting, and is justified on the following basis:

> the mischief that would arise to the public from estates remaining for ever or for a long time inalienable or untransferable from one hand to another, being a damp to industry and prejudice to trade, to which may be added the inconvenience and distress that would be brought on families whose estates are so fettered.
>
> (Jekyll MR in *Stanley v Leigh* (1732) 2 P Wms 686 at 688)

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[14] Law of Property Act 1925, s.34.
[15] Wills Act 1837, s.9.

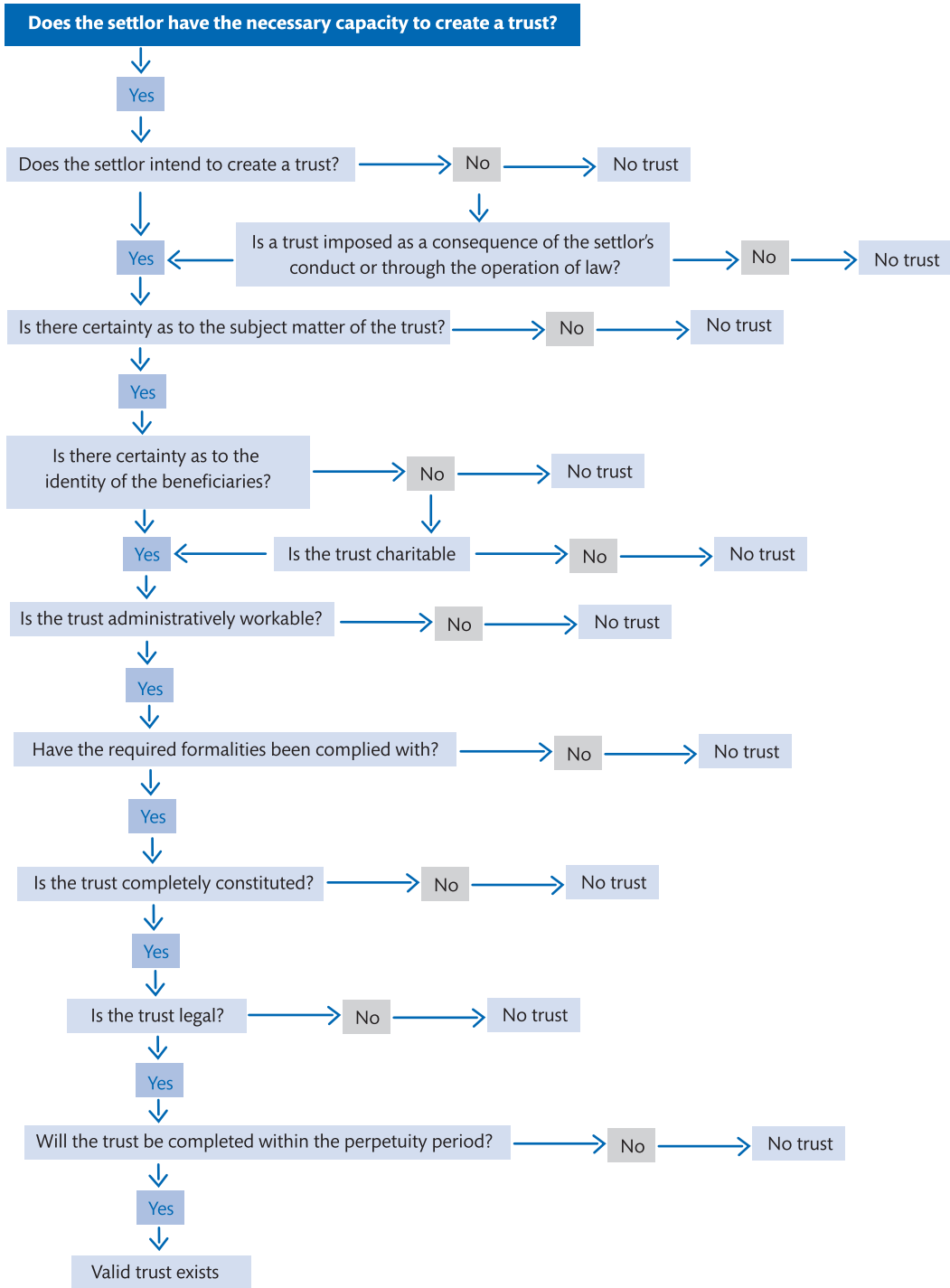

Figure 6.1 A flowchart for deciding validity

The trust and other obligations

Subject to these requirements and formalities, the trust is an extremely flexible concept. However, the trust may overlap considerably with other types of relationship recognised by the law, such as agency, bailment, contract, and powers of appointment.

Trust and agency

There is considerable overlap between the relationship between a trustee and the settlor and the beneficiary, and the relationship between a principal and an agent. For example, both a trustee and an agent have a fiduciary duty to the trust which means that their own interests should not be permitted to conflict with those to whom they owe the obligation (the beneficiary under a trust, and the principal in an agency relationship). However, an agent acts on the principal's behest, whereas it is the settlor under a trust who imposes the obligation on the trustee, and that obligation is owed to the beneficiary, who has not solicited the trustee's services. Secondly, the function of the agent is to enter into contractual relationships in place of the principal, and he or she does not judge on the wisdom or viability of the transaction. However, the trustee's obligation is to benefit the beneficiary, and therefore he or she must evaluate how the interests of the trust are best served.

Trust and bailment

Bailment arises where one entrusts one's property to the safekeeping of another. For example, if Billy takes a suit to a dry cleaners' shop then the dry cleaners are bailees of Billy's suit. The hiring of equipment, such as a car or a skip, is another form of bailment, as is the obligation imposed on the neighbour whose garden is the subject of a child's (or an adult's) misaimed football. Bailment differs from the trust in two significant ways. Firstly, only chattels may be the subject of bailment, whereas other types of property, including land, may be the subject of a trust. Secondly, the trustee becomes the legal owner of the trust property, whereas the bailee is merely in possession of the bailed goods, and cannot therefore pass the title to the goods to a third party.

Trust and contract

Although a trust and a contract both arise from an agreement followed by a transfer of property, there are significant differences between a trust and a contract. Firstly, a contracting party acts for his or her own benefit, where as a trustee acts for the benefit of the beneficiary. Secondly, a contract requires an exchange of obligation in the form of consideration. However, a trust may impose an obligation on the trustee without the trustee being able to derive any benefit from it – indeed, in most situations it is imperative that a trustee must derive no benefit from the trust obligation. Thirdly, whereas the rules of privity of contract require that only the parties to a trust may enforce the obligations under the trust, it is the beneficiary who enforces the trust against the trustee in the event of a breach. On the other hand, despite having created the trust, the settlor has no further entitlement to the trust property unless he or she is also a beneficiary.

Trusts and powers

A power is a similar type of obligation to a trust, and powers are often given to the trustee alongside a trust. However the key difference is that, whereas a trust imposes an obligation

on the trustee, the donee of a power is simply that – a person who is given the power to act in a particular way, but is under no obligation to do so, and will not be in breach of any obligation if he or she does not exercise the power.

In this chapter, the aim has been to outline the trust relationship. In the chapters that follow, these aspects will be considered in greater detail.

Chapter summary

This chapter may be useful for assessments and assignments on:

- The development of the trust
- Reasons for employing the trust mechanisms
- Comparisons between trusts and other legal relationships.

Further reading

Jones, N.G. (2010) 'Wills, Trusts and Trusting from the Statute of Uses to Lord Nottingham' 31(3) *Journal of Legal History* 273.

Rosenberg, G. and Faibish, I. (2007) 'Agent or trustee?' 92 *Trusts and Estates Law and Tax Journal* 26.

Shindler, G.A. (2001) 'Equity, law, rules and attitudes' 31 *Trusts and Estates Law and Tax Journal* 2.

7

The settlor

Chapter outline

In the last chapter, an overview of the trust was provided. This chapter will consider:

- The role of the settlor
- The testator or a testatrix.

A person who creates a trust is known as a settlor. The term testator is used to describe a person of either gender who writes a will. In some of the older cases, the term testatrix will also be found. This is the term used to describe a woman who writes a will.

Capacity

As a general principle, a person or corporation that is able to own property is able to create a trust of that property, or more precisely, as Romilly MR confirms in *Tierney v Wood* (1854) 52 ER 377:

> the proper person to create the trust in personal property is the person in whom the beneficial interest of the property is vested, and the trust being created by the beneficial owner, the trustee is bound, and, if disposed to refuse, may be compelled to obey it.

Therefore, any person, including a child, may create a valid trust of personal property[1] or of an equitable interest in property,[2] although, because a child cannot be the legal owner of land,[3] a child cannot therefore be the settlor for a trust of land. Furthermore, a child cannot create a valid will,[4] but can make a valid *inter vivos* trust,[5] although the trust would be voidable.[6] It is likely that the question of a person's capacity to create a trust will depend on the complexity of the trust created. Therefore, the law is not likely, in the normal course of events, to dispute the validity of a donation given by a child or a person suffering from some mental incapacity to a friend who is doing a sponsored activity for charity, but may be more reluctant to accept a formally created trust of valuable property as being valid without proof that the person had sufficient understanding of what the relationship entails.

EXTRACT

Re Beaney [1978] 1 WLR 770

Case facts

The settlor, who was suffering from dementia, attempted to give her house, which was the only asset of any significant value, to her eldest daughter, Valerie, who lived with her. However, the fact that she gave the house to her daughter meant that there was nothing left in her estate for her younger daughter and her son.

Martin Nourse QC

The degree or extent of understanding required in respect of any instrument is relative to the particular transaction which it is to effect. In the case of a will the degree required is always high. In the case of a contract, a deed made for consideration or a gift *inter vivos*, whether by deed or otherwise, the degree required varies with the circumstances of the transaction. Thus, at one extreme, if the subject-matter and value of a gift are trivial in relation to the donor's other assets a low degree of understanding will suffice. But, at the other, if its effect is to dispose of the donor's only asset of value and thus for practical purposes to pre-empt the devolution of his estate under his will or on his intestacy, then the degree of understanding required is as high as that required for a will, and the donor must understand the claims of all potential donees and the extent of the property to be disposed of.

Outcome

The settlor was deemed not to have the requisite capacity to transfer the land as she did.

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[1] *M'Fadden v Jenkyns* (1842) 1 Ph 153.
[2] Law of Property Act 1925, s.53(1)(c).
[3] Law of Property Act 1925, s.1(6).
[4] Wills Act 1837, s.7.
[5] *Edwards v Carter* [1893] AC 360.
[6] Ibid.

Creating the trust

The settlor creates the trust by transferring the trust property to the trustees with the intention that it should be held on trust for specified beneficiaries. The trust is not completely constituted until the transfer of the property has occurred, indicating that the settlor must not only manifest an intention, but that his or her conduct must also be in accordance with that intention.[7] However, the court will compel the completion and execution of the trust if the beneficiary has given valuable consideration in exchange for the creation of the trust, as Jessel MR explains in *Lee v Lee* (1876) 4 Ch D 175.

EXTRACT

Lee v Lee (1876) 4 Ch D 175

Case facts

Thomas and Mary Shaw had six children. They created a trust in relation to land belonging to Mary Shaw whereby Mary was entitled to a life interest in the land, and then after her death, her husband, Thomas Shaw, was entitled to a life interest in the land, and then after his death, their six children would divide the land equally between them, or if one or more of the children had died, the others would be entitled to a larger share. One of the children, Marion, was to marry a man called Arthur Lee. A pre-nuptial agreement was made between Arthur Lee, Marion Shaw and Marion's parents, regarding Marion's share of the trust property. In exchange Arthur Lee agreed that he would create trusts of the land for the benefit of himself and Marion Shaw and any children Arthur and Marion might have in the future. Arthur Lee and Marion Shaw married, and had two children. One of Marion's siblings died, as did her mother. Thomas Shaw then divided the deceased sibling's share between his five remaining children, one of whom was Marion. There was an indication that this was the sum that was to fulfil the pre-nuptial agreement. Accordingly, when Marion died, the one-sixth of the land to which she had been entitled originally, went to her eldest child, while the one-thirtieth share that represented Marion's one-fifth share of her deceased sibling's one-sixth entitlement was to be used to fulfil Arthur Lee's obligation under the pre-nuptial agreement. Arthur Lee and his younger child therefore requested specific performance of the pre-nuptial agreement in relation to Marion's entire entitlement to the land as one-fifth of the estate rather than one-thirtieth.

Jessel MR

Their agreement so to exercise their power is expressed to be in consideration of her intended marriage, and their object in entering into the agreement is to enable the husband to make a settlement. Then the husband proceeds to settle, or agree to settle, what does not belong to him, as indeed appears by the instrument itself. Unquestionably, the property was not his to settle; it was his wife's, and he could not settle it himself, because, during the lives of the wife's father and mother he could have no interest whatever, therefore his covenant or agreement to settle was a covenant or agreement to settle not his own estate but somebody else's. But the wife was an assenting party to this agreement. It was, therefore, simply an agreement by A., with B.'s assent, to settle B.'s estate, and in such a case it is clear that B. is bound. So that even if it is treated as a covenant by the husband alone, yet it is for valuable consideration and with the assent of the wife, and she is therefore bound. That is rudimentary law. In the two cases which were referred to, *Young* v. *Smith* [(1865) LR 1 Eq 180] and *Ramsden* v. *Smith* [(1854) 61 ER 734], the covenant was to settle the after-acquired property of the wife, and the real question

[7] *Bizzey v Flight* (1876) 3 Ch D 269.

was, what property was included in the covenant. The property which was to be the subject of the covenant was described in general terms, and the question in both cases was whether the covenant was intended to apply to a legacy bequeathed to the wife subsequently to the marriage. But those cases have no application to the case now before me, where the property agreed to be settled is specifically described, and there is, therefore, no doubt whatever as to what property is included in this covenant. The agreement by the husband that he would settle this particular property was clearly binding on the wife, she having assented to it by being a party to the agreement, and is equally so on her heir-at-law, and therefore there will be judgment for the Plaintiffs.

The settlor may also specify the terms of the trust and any conditions or restrictions that he or she wishes to impose. Therefore, the settlor may specify when the beneficiary is to receive the trust fund[8] – something that might be important where the beneficiary is a child, as the settlor may wish to ensure that the beneficiary does not become entitled to the fund until they reach majority, or until they are considered to be old enough to act responsibly in relation to the wealth they will acquire. The trustees' responsibility is to administer the trust in accordance with the settlor's wishes,[9] and the wishes of the settlor cannot be departed from, even though the trust may be varied or terminated by the beneficiaries, as shown in Chapter 12. Nevertheless, it is to be emphasised that the extent to which the variation of the trust is permitted is limited, and that although the beneficiaries may wish to introduce variations in terms of which beneficiaries receive what proportion of the trust fund, there is no scope to rewrite the trust so that it no longer achieves the outcomes the settlor broadly intended.[10]

The settlor may also stipulate the rules under which the trustee must operate. Therefore, the settlor may specify for example whether the trustee is to be remunerated for his or her endeavours,[11] or may stipulate when the beneficiary should become entitled to the trust property.[12] The settlor may also confer upon the trustees an element of discretion in terms of selecting beneficiaries and determining how much of the trust fund each beneficiary is to receive.[13]

Although an *inter vivos* trust (i.e. a trust which is made, and which takes effect during the settlor's lifetime) of personal property need not be made in writing,[14] writing may be valuable evidence of the settlor's intention, and may be advisable where substantial trusts of significant trust property is concerned. Therefore, the simple trust of an insignificant sum (a donation put into a charity collector's tin) might not be viewed as justifying documentary evidence of the settlor's intentions. On the other hand, a trust fund of £1 million to be divided between a large number of beneficiaries, and subject to a number of conditions could be made orally, but the prudent settlor would probably view this as being unduly risky and would prefer to provide written evidence confirming that the relationship is that of a trust rather than an absolute gift to the persons named as the trustees. Wills,[15] trusts of land[16] and trusts of equitable interests[17] must, however, be made in writing.

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[8] *Re Clore's Settlement Trusts; Sainer and Others v Clore and Others* [1966] 2 All ER 272.
[9] *Re Turner's Will Trusts; District Bank Ltd v Turner* [1937] Ch 15.
[10] *Wilkinson v Parry* (1828) 4 Russ 272 at 276 per Leach MR.
[11] *Ayliffe v Murray* (1740) 2 Atk 58.
[12] *Re Clore's Settlement Trusts; Sainer and Others v Clore and Others* [1966] 2 All ER 272.
[13] *Sainsbury's v Inland Revenue Commissioners* [1970] Ch 712.
[14] *M' Fadden v Jenkyns* (1842) 1 Ph 153.
[15] Wills Act 1837, s.9.
[16] Law of Property Act 1925, s.53(1)(b).
[17] Law of Property Act 1925, s.53(1)(c).

EXTRACT

Wills Act 1837, s.9

No will shall be valid unless-

(a) it is in writing, and signed by the testator, or by some other person in his presence and by his direction;

EXTRACT

Law of Property Act 1925, s.53

53 Instruments required to be in writing

1. (1) Subject to the provisions hereinafter contained with respect to the creation of interests in land by parol-

   (a) no interest in land can be created or disposed of except by writing signed by the person creating or conveying the same, or by his agent thereunto lawfully authorised in writing, or by will, or by operation of law;

   (b) a declaration of trust respecting any land or any interest therein must be manifested and proved by some writing signed by some person who is able to declare such trust or by his will;

   (c) a disposition of an equitable interest or trust subsisting at the time of the disposition, must be in writing signed by the person disposing of the same, or by his agent thereunto lawfully authorised in writing or by will.

Once the trust has been created and the trust property transferred to the trustee, the settlor is no longer able to intervene in the trust relationship. This is confirmed by the judgment in *Paul v Paul* (1882) 20 Ch D 742, a case which concerned a husband and a wife who created a trust, and then wished to use the fund for a different purpose.

EXTRACT

Paul v Paul (1882) 20 Ch D 742

Case facts

A husband and wife created a trust whereby if they had no children, the estate would go to the wife if she survived her husband, and if the husband outlived the wife, the estate would be given to the wife's next of kin. The couple had no children, and because of the wife's age, there was no possibility that they would have children in the future. Accordingly when the husband and wife separated, they wished to divide the trust fund equally between them.

Cotton LJ

The next of kin of the lady are *cestuis que* trust under the settlement, although they are not yet ascertained. I assume that the trust would not have been enforced if it were still executory. But this trust is executed, and the next of kin have an interest as *cestuis que* trust. It is immaterial that they are volunteers. The trust cannot be broken on that account, and if the trustees were to part with the fund they would be guilty of a breach of trust.

Accordingly, once created, the trust cannot be revoked, because the settlor has parted with title to the trust property. However, an incomplete *inter vivos* trust or a will trust may be revoked once created (as Cotton LJ confirms in *Paul v Paul*), because in this situation, the trust property has not been transferred, and therefore, although the settlor has manifested an intention to create a trust, his or her conduct is inconsistent with that intention. Therefore, if the settlor wishes to reserve for him- or herself the power to deal with the trust property, then it is necessary for him or her either to declare him or herself to be the trustee, or alternatively the beneficiary, of the trust fund.

Declaring oneself to be a trustee

If the settlor declares him- or herself to be the trustee (though the reader will doubtlessly appreciate that this option is not available to the testator!) then there is no need for the property to be transferred. However, there must be an effective declaration of trust. Accordingly, the trust will not be used as a means of correcting an incomplete gift.

EXTRACT

Jones v Lock (1865) LR 1 Ch App 25

Case facts

On his return from a business trip, the deceased was scolded for not bringing a present for his baby son. He therefore wrote out a cheque and gave it to the child, later taking it back and putting it in a safe. The following week, he met his solicitor and made arrangements to visit the solicitor in order to amend his will in order to make provision for the baby. However, he died before making a new will, and the court had to decide whether the cheque and the deceased's conduct were sufficient to constitute a trust in the baby's favour.

Lord Cranworth

It was all quite natural, but the testator would have been very much surprised if he had been told that he had parted with the £900, and could no longer dispose of it. It all turns upon the facts, which do not lead me to the conclusion that the testator meant to deprive himself of all property in the note, or to declare himself a trustee of the money for the child. I extremely regret this result, because it is obvious that, by the act of God, this unfortunate child has been deprived of a provision which his father meant to make for him.

This case demonstrates that where one declares oneself to be a trustee, there must be some conduct that indicates when the trust is to be effective, and that the relationship intended is that of the trust. In *Jones v Lock*, it was not clear whether the deceased intended to give the money to the baby or whether he intended to act as the trustee for the benefit of the baby. The money could not have been transferred to the baby when the cheque was written, thus precluding the donation from being a gift. However, it was not clear from the deceased's words and actions that he was intending to declare himself as the trustee of the money for the benefit of the child. Furthermore, it was not clear when the donation was to take effect. On the one hand, it might have been viewed as being effective when the cheque was given to the child. On the other hand, it might have been viewed as a symbolic gesture that manifested the deceased's future intention to amend his will.

On the basis that the deceased's words and actions were more indicative of a gift than a trust, the court declined to find that a trust had been created, and on the basis that the deceased was planning to amend his will it was unlikely that he would also have intended to give him a gift of money as well as a legacy in a will. Therefore, the action of declaring oneself to be a trustee must be unambiguous both as to the intention to create a trust rather than any other type of relationship, and must also be clear regarding when the trust becomes operative.

The settlor-beneficiary

It is also possible for the settlor to create a trust whereby he or she is a sole or a joint beneficiary. In this situation, clearly, the settlor will be in a position to enforce the trust qua beneficiary, but once the trust has been created he cannot direct its conditions qua settlor. In this situation, the settlor plays two roles – that of the settlor and that of the beneficiary – and although manifested by the same person, the settlor's role as settlor is completely different from his or her role as beneficiary, which will be discussed further in Chapter 12. However, the fact that the settlor may also be the beneficiary is increasingly seen as having many advantages. The fact that a person may simultaneously be the settlor and the beneficiary tended to be viewed almost as an unremarkable consequence of the trust relationship, such as where a legacy in a will fails, and the property reverts back to the trust estate, or where a person transfers land from their sole ownership into joint ownership with another person. Increasingly however, it is being recognised that the situation of the settlor-beneficiary is extremely useful because the settlor qua beneficiary is able to continue to direct how the trust is to operate, in that the settlor-as-beneficiary is then able to require the variation of the trust (something that will be discussed further in Chapter 23).

Nevertheless, the scope for intervention as a beneficiary is limited, with the result that Tsun Hang Tey argues in favour of ensuring that settlors are able to reserve powers for themselves.

EXTRACT

Tsun Hang Tey (2009) 'Settlor's Reserved Powers' 4 *Trusts Law International* 183–199

The changing nature of the trust instrument has promoted the desire for more reserved powers for settlors in modern trusts. Trusts are no longer restricted to their traditional functions of holding, protecting and transferring real property. Instead, modern trusts are used as investment tools aimed at enhancing the value of financial assets . . . Expanding the scope of the settlor's reserved powers – thereby assuring the settlor of the trustee's fidelity to his wishes – increases the settlor's willingness in creating trusts. A settlor who reserves the power of modification of trust terms is able to continually impose his financial judgments on the future investment directions of the trust assets. This is in contrast to the present legislative regimes in various Commonwealth jurisdictions, where there is no guarantee that the settlor's express intentions indicated in the trust instrument would always be followed. Scholars also pointed to the emerging trend of trust protectors in offshore trust jurisdictions as a response, and also a remedy, to the settlor's uncertainty about the future. The settlor, by appointing a trusted person

as the protector, and granting him the authority to replace trustees, or make modifications to the trust instrument, etc. is able to indirectly manoeuvre the performance of the trust according to the settlor's preferences. As a trust protector can be granted the power to appoint his successor, the office of trust protector allows for a lengthier settlor oversight. Bearing the contemporary development of trust protectors in offshore trust jurisdictions in mind, allowing a more extensive scope of settlor's reserved powers would be the straightforward answer to the settlor's preference for greater certainty under the modern trust regime . . .

The success of a trust critically hinges on the strength of the mechanism for monitoring trustee performance. This mechanism is normally provided by the fiduciary duties imposed on trustees, which are enforceable by beneficiaries. However, the mechanism of fiduciary duty litigation has several deficiencies. Firstly, the beneficiaries' preferences may not be perfectly aligned with the settlor's. A trustee is unlikely to face any action for breach of fiduciary duty when it takes action with the approval of the beneficiaries, even though the settlor and the beneficiaries may have had divergent preferences. This reduces the value of fiduciary duty litigation as a mechanism for monitoring agency costs. Secondly, fiduciary duty litigation assumes the existence of rational and educated beneficiaries. This is seldom the case. If the settlor had confidence in the financial acumen of the beneficiaries in the first place, practically, he ought to have transferred his assets to the beneficiaries, thus preventing the problem of agency costs from ever arising. It is likely that trustees as a group understand the limited capacity of the beneficiaries. To make matters worse, if the trust beneficiaries are minor, incompetent or financially unsophisticated, they may not be effective monitors of the trustee's performance. This reduces the effectiveness of fiduciary duty litigation as a mechanism for ensuring that the trustee acts in the interests of the settlor. Lastly, trustees recognise that beneficiaries would have to bear certain costs in commencing an action against the trustees for breach of fiduciary duties – the most obvious of which are the litigation costs. Even if the beneficiaries succeed in an action against the trustee for breach of fiduciary duty, they may only be able to recover the litigation costs from the trust estate. This would be a hollow victory since the beneficiaries – as the equitable owners of the trust estate – would in substance be recovering from their own pockets.

Academics have suggested that granting the settlor the *locus standi* to enforce the trustee's duties would minimise beneficiaries' supervisory costs by making the threat of litigation more viable as a deterrent against trustee misconduct. It has been suggested that the settlor's reserved power to remove trustees would also provide a 'deterrent' to safeguard against trustee misconduct – the exercise of which does not require any proof of trustee misconduct.

The trust must be completely constituted

Ordinarily, however, once the trust has been created, the settlor plays no further part in the trust relationship, unless he or she assumes another role in the trust relationship. Nevertheless, before the settlor (qua settlor) is able to withdraw from the trust relationship, he or she must ensure that the trust is completely constituted. This means that the settlor must do everything within his or her power to transfer the trust property to the trustees. In the case of *Re Rose* [1952] Ch 499 the trust property comprised of a number of company shares. The settlor had completed the relevant share transfer form. However, the transfer of the shares had to be authorised by the company directors. This had not occurred before the death of the settlor. However, the Court of Appeal concluded that the settlor had done everything that was expected of him in order to effect the transfer. The trust had been completely constituted at the time of the settlor's death, as Jenkins LJ explains:

> If the deceased had in truth transferred the whole of his interest in these shares so far as he could transfer the same, including such right as he could pass to his transferee to be placed on the register in respect of the shares, the question arises, what beneficial interest had he then left? The answer can only be, in my view, that he had no beneficial interest left whatever: his only remaining interest consisted in the fact that his name still stood on the register as holder of the shares; but having parted in fact with the whole of his beneficial interest, he could not, in my view, assert any beneficial title by virtue of his position as registered holder. In other words, in my view the effect of these transactions, having regard to the form and the operation of the transfers, the nature of the property transferred, and the necessity for registration in order to perfect the legal title, coupled with the discretionary power on the part of the directors to withhold registration, must be that, pending registration, the deceased was in the position of a trustee of the legal title in the shares for the transferees. Thus in the hypothetical case put by the Crown of a dividend being declared and paid (as it would have been paid in accordance with the company's articles) to the deceased as registered holder, he would have been accountable for that dividend to the transferees, on the ground that by virtue of the transfers as between himself and the transferees the owners of the shares were the transferees, to the exclusion of himself.

However, if the settlor has not fulfilled all the obligations required of him or her, no valid trust will have been created. For example, if the situation in *Re Rose* is modified slightly, such that the settlor has completed the share transfer form, but has not signed it, or has completed it but not posted it, the trust is likely to fail because the settlor has not done everything that he or she was required to do in order to constitute the trust completely.

The sham trust and the illegal trust

Although a settlor has considerable freedom to specify the terms of the trust and its obligations, the courts will set aside any trust that appears to have been made as a result of a sham intention. In the case of *Midland Bank v Wyatt* [1995] 3 FCR 11, the trust was set aside because the defendant had no intention to confer a benefit on the purported beneficiaries – the aim of the trust was to put the trust property out of the reach of creditors. It would seem therefore that the principle that a trust once made cannot be unmade, encountered in *Re Rose*, is not sacrosanct, and a trust may be unmade, even to the extent of the purported beneficiaries where the trust appears to be a sham.

EXTRACT

Midland Bank v Wyatt [1995] 3 FCR 11

Case facts

The defendant and his wife bought a house in their joint names. When the defendant decided to set up his own company, he created a trust of the house whereby he and his wife declared themselves to be trustees of the house for the benefit of the wife and the couple's two children. Although she had signed the document, the wife was found to have no knowledge of the trust. When the defendant's business went into receivership, the claimants attempted to enter into possession in order to sell the house to recover the value of its mortgage loan, but the defendant argued that he owned the house solely as a trustee. The court held that the trust was a mere sham.

Mr D.E.M. Young QC

I do not believe Mr Wyatt had any intention when he executed the trust deed of endowing his children with his interest in Honer House, which at the time was his only real asset. I consider the trust deed was executed by him, not to be acted upon but to be put in the safe for a rainy day – as Mr Wyatt states in his affidavit, as a safeguard to protect his family from long-term commercial risk should he set up his own company. As such I consider the declaration of trust was not what it purported to be but a pretence or, as it is sometimes referred to, a 'sham'. The fact that Mr Wyatt executed the deed with the benefit of legal advice from Mr Ellis does not in my view affect the status of the transaction. It follows that even if the deed was entered into without any dishonest or fraudulent motive but was entered into on the basis of mistaken advice, in my judgment such a transaction will still be void and therefore an unenforceable transaction if it was not intended to be acted upon but was entered into for some different or ulterior motive. Accordingly, I find that the declaration of trust sought to be relied upon by Mr Wyatt is void and unenforceable.

I should add as a general matter it is clear that when it was expedient to do so Mr Wyatt was prepared to allow the bank to remain in ignorance of the true position (both with regard to the loan being unsecured and with regard to the existence of the trust deed and/or the fact that he no longer had any beneficial interest in Honer House) or even to mislead (as he admits was the case with Mr Howick over outstanding debts to him). From his dealings with his own solicitors, it appears that when it suited him to do so he did not disclose the full facts, in particular his failure to tell either Mr Minton or Mrs Bevis about the trust deed can only be explained on the basis of Mr Wyatt having forgotten all about it or deliberately concealing it.

Furthermore, a trust that is created for some immoral or illegal purpose will not be valid: a trust made in contemplation of a marriage was held to be void for illegality because the settlor and the beneficiary could not legally be married to each other (*Philips* v *Probyn* [1899] 1 Ch 811).

A trust that offends against the rule against perpetuities when it is created will also be void for illegality. Therefore a trust that is specified as being of perpetual duration will be automatically void as being contrary to either the common law or the Perpetuities and Accumulations Act 1964[18] (for trusts created after 16 July 1964) or the Perpetuities and Accumulations Act 2009[19] (for trusts created after 6 April 2010). Nevertheless, under the two statutes, there is scope for a trust to be valid until it becomes apparent that it is of perpetual duration. The law on Perpetuities and Accumulations will be discussed further later (in Chapter 9).

In this chapter therefore, the part played by the settlor has been considered. In the chapters that follow, the requirements that the settlor must fulfil in order for the trust to be valid will be addressed.

[18] (1964 c.55).
[19] (2009 c.18).

Chapter summary

This chapter may be useful for assignments and assessments on:

- The role of the settlor
- The parties to a trust.

Further reading

Halliwell, M. (2003) 'Perfecting imperfect gifts and trusts have we reached the end of the Chancellor's foot?' *Conveyancer and Property Lawyer* 192.

Luxton, P. (2012) 'In search of perfection: the Re Rose rule rationale' *Conveyancer and Property Lawyer* 70.

Matthews, P. (2002) 'Capacity to create a trust: the onshore problem, and the offshore solutions' *Edinburgh Law Review* 176.

Morris, J. (2003) 'Questions: when is an invalid gift a valid gift? When is an incompletely constituted trust a completely constituted trust? Answer: after the decisions in *Choithram* and *Pennington*' *Private Client Business* 393.

8

The three certainties

Chapter outline

This chapter will cover:

- Certainty of intention to create a trust
- Certainty of subject matter
- Certainty of objects.

Introduction

As was outlined earlier (in Chapter 7), in order for a trust to exist, it is necessary for the courts to be certain of three things. These are known as the three certainties, and were defined by Lord Langdale in the case of *Knight v Knight* (1840) 3 Beav 148:

> As a general rule, it has been laid down, that when property is given absolutely to any person, and the same person is, by the giver who has power to command, recommended, or entreated, or wished, to dispose of that property in favour of another, the recommendation, entreaty, or wish shall be held to create a trust. First, if the words are so used, that upon the whole, they ought to be construed as imperative; Secondly, if the subject of the recommendation or wish be certain; and, Thirdly, if the objects or persons intended to have the benefit of the recommendation or wish be also certain.

Firstly, there must be certainty that there was an intention to create a trust. Secondly, there must be certainty as to the trust property, known as certainty of subject matter, and thirdly, there must be certainty as to the identity of the beneficiaries, known as certainty of objects. Students often get confused between certainty of subject and certainty of objects, and this is understandable as objects are often used to denote 'things' while citizens are regarded as 'subjects' of the Crown. However, it is easier to distinguish between subject and object if one considers them in terms of grammar. The subject is the thing that performs the action of the verb (e.g. in the sentence 'John is riding the bicycle', John is the subject because he is performing the action of riding), while the object is the thing that is having something done to it or with it (in the above example, the object is therefore the bicycle). Accordingly, in the context of the law of trusts, the trust property is therefore the subject – it 'performs' the trust, and the beneficiary is the object – it has the trust performed upon it.

The reasoning behind these three requirements is in reality very simple. Consider the following example. If Donna says, 'I'd like to give something to somebody', it is not likely to be sufficient to create a trust. There is a lack of precision as to whether there is any intention to create a relationship that might be enforceable in a court of law, and whether the relationship envisaged would take the form of a trust, as opposed to a gift.

There is also a lack of precision regarding the subject matter and the object – what is Donna intending to give, and to whom? Is there anyone who could legitimately claim that they have not received that to which Donna's remarks entitled them? It is unlikely that anyone would bring such a claim, and even less likely that such a claim would succeed.

Accordingly, the courts must be satisfied that there was an intention to create a relationship that could be enforced by the law, and that that relationship is in fact a trust, rather than a gift or a contract. The courts must also be satisfied that the subject matter of the trust exists, that the settlor has sufficient rights over it to be able to create a trust from it, and that it is defined with sufficient precision so as to distinguish it from other items that the settlor may own that match the description. Thirdly, the courts must be satisfied that beneficiaries have been identified, and that they have been defined sufficiently narrowly and precisely that it is possible to administer the trust in their favour. Nevertheless, what will be shown in this chapter is that the wording of a trust, and intervening circumstances, mean that identifying the three certainties in each case results in a number of ambiguities and problems for the courts.

The certainty of intention

A trust will be discovered if the wording used by the settlor, or his or her conduct, is sufficient to indicate that a trust was intended. In the case of *Tanna v Tanna* [2001] All ER (D) 333, Sir Andrew Morritt VC went so far as to state that '*Certainty of intention is in many ways the most important certainty. If the court is satisfied that the alleged declarant had the requisite intention it will strive to validate it*.' Often, with a deliberately created document such as a will, the intention to create a trust will easily be demonstrated – the settlor has engaged in a deliberate action with a deliberate intention. Nevertheless, with *inter vivos* trusts, particularly those created orally, or as part of a document that does not appear primarily to be a trust, a court will have to look very carefully at the wording used in order to ascertain that a trust was intended, and the fact that the matter has proceeded as far as a court hearing gives a clear suggestion that there is an ambiguity in what was intended.

The words used

Accordingly, the courts will consider whether the wording used suggests an intention to create an obligation, or merely an indication of what might be desirable for the recipient to consider – the latter being termed precatory words. The words used by the settlor may be spoken words,[1] or more commonly the words written by the settlor or the testator in the trust instrument. For example, the question of what the words used by the settlor mean often arises in the context of wills where a legacy is left to a specific beneficiary with a direction as to how that legacy might be used for the benefit of others.

However, the problem of whether the wording used by the testator invokes an intention to create a trust, or merely a wish on the testator's behalf, will also arise in the context of other situations where a trust might be created, as is seen in the case of *Re Farepak Food and Gifts Ltd (In Administration)* [2006] All ER (D) 265 (Dec). In some instances, the wording adopted has been regarded as being sufficient to give rise to a trust, while in other cases it has been viewed merely as a suggestion of how the legacy might be used, but does not create an obligation that the courts would enforce. The distinction is discussed in the case of *Williams v Williams* [1897] 2 Ch 112.

EXTRACT

Williams v Williams [1897] 2 Ch 12

Case facts

Here the testator, William Williams, wrote a will leaving the residue of his estate, after specific legacies had been given, to his wife, Lucy Williams, 'in the fullest confidence that she will carry out my wishes' in relation to two specific matters. Firstly, Mrs Williams was required to continue paying the premiums on a life assurance policy on her own life. Secondly, she was to ensure that the moneys payable under both her life assurance policy, and the testator's own life assurance policy, were to be paid to the testator's daughter. On Lucy Williams' death, it was

[1] *Moore v Williamson* [2011] EWHC 672 (Ch).

discovered that the daughter would receive the moneys from her father's life assurance policy, but would not receive the moneys payable under her mother's life assurance policy. Accordingly, the issue to be decided by the court was whether the wording of William Williams' will created an obligation that required his wife to leave the moneys payable from both life assurance policies to their daughter, also called Lucy.

Lindley LJ

There can be no doubt that equitable obligations, whether trusts or conditions, can be imposed by any language which is clear enough to shew an intention to impose an obligation, and is definite enough to enable the Court to ascertain what the precise obligation is and in whose favour it is to be performed. There is also abundant authority for saying that, if property is left to a person in confidence that he will dispose of it in a particular way as to which there is no ambiguity, such words are amply sufficient to impose an obligation . . . But still in each case the whole will must be looked at; and unless it appears from the whole will that an obligation was intended to be imposed, no obligation will be held to exist; yet, moreover, in some of the older cases obligations were inferred from language which in modern times would be thought insufficient to justify such an inference.

It would, however, be an entire mistake to suppose that the old doctrine of precatory trusts is abolished. Trusts – i.e., equitable obligations to deal with property in a particular way – can be imposed by any language which is clear enough to shew an intention to impose them.

The term 'precatory' only has reference to forms of expression. Not only in wills but in daily life an expression may be imperative in its real meaning although couched in language which is not imperative in form. A request is often a polite form of command. A trust is really nothing except a confidence reposed by one person in another, and enforceable in a court of equity. In one sense it is true to say that a trust of property cannot be created by a person who is not entitled to that property. But there is no difficulty in disposing of one's own property upon condition express or implied that the person who takes it shall do something himself, e.g., shall dispose of his property in a particular way indicated by the owner of the property which he accepts. Moreover, a condition of this kind is enforceable in equity, and need not amount to a common law condition – i.e., a condition involving a forfeiture of the property taken subject to the condition – if that condition is not performed.

The particularity with which the testator has stated what his wishes were removes all difficulty in giving effect to those wishes if they are expressed in language which is shewn by the will to be intended to be imperative; but such particularity does not supply the want of imperative language. The testator has employed the same language with respect to his own policy as with respect to his wife's. He has shewn no intention of imposing an obligation on her in respect of one of them and not in respect of the other. I feel great difficulty in holding that he has not left his own policy to her absolutely free from all trust and condition, and the difficulty of making any distinction between the two policies forces me to the conclusion that the widow is not put to her election as regards her own policy. I might not have come to this conclusion if he had not dealt with both policies in the same way, for to put her to her election as to her property does not fetter her enjoyment of his. The case is in my opinion one of great difficulty, and I am quite aware that there are decisions in the books which if followed would be in the daughter's favour. But our task is to construe the will before us, and other cases are useless for that purpose except so far as they establish some principle of law. There is no principle except to ascertain the intention of the testator from the words he has used, and to ascertain and give effect to the legal consequences of that intention when ascertained.

Having given the case my best attention, I have arrived at the conclusion that the testator has not used language sufficiently clear to impose upon his widow an obligation to leave either

policy to his daughter. I believe, further, that he refrained from language imperative in its terms, such as upon trust or upon condition, and that he used the language which he did because he really intended to trust his widow's discretion with respect to his daughter, and not to provide for his daughter himself by putting a legal fetter on his widow's power of disposition of her own policy or of the property which he left her. I read the will as expressing a wish that his daughter should have both policies unless his widow should see reason for otherwise disposing of them, and I do not find in the will a command to his widow to leave the policies to his daughter if his widow should think right to dispose of them otherwise.

A.L. Smith LJ

It should be noticed that when the testator wished to create a trust, he does so by apt words – 'in trust for her sole and separate use,' and he appoints trustees, obviously well knowing what the words 'trust' and 'trustees' mean. Why am I to hold that the testator, after such a clear gift to his wife absolutely, as I read it, for her own absolute benefit, when he used the words 'in the fullest confidence that she will carry out my wishes in the following particulars,' meant and intended the same thing as if he had said 'in trust for my daughter Lucy.' It seems to me erroneous to say that each expression means the same thing. Why use different words? It would not, I think, be in accordance with the ordinary canon of construction to hold that the different expressions meant one and the same thing. That the testator had implicit faith in his wife appears to me clear, for he left her everything in the world which he had to leave, with the meagre exception of the medical books and instruments. And that he placed full reliance in her carrying out his wishes I do not doubt. I cannot understand, if he had intended an obligation by way of trust, why he did not say so. Instead thereof he merely expresses a confidence – that is, a reliance or hope, that she would carry out his wishes. In the will the words 'confidence' and 'trust' are used in contrast to each other. Moreover, how could the testator have meant to impose a trust as regards property which did not belong to him, but to her?

Outcome

The Court of Appeal considered that there was no trust in Lucy's favour.

The distinction between Lindley LJ and A.L. Smith LJ's approaches to this issue is particularly interesting. Lindley LJ begins by considering that William Williams could not dictate what should happen to his wife's life assurance policy. Therefore, if he could not dictate what Lucy Williams should do with her own property, the fact that the directions concerning what she should do with his life assurance policy were contained in the same clause meant that he could not have intended for her to hold his life assurance policy on trust for his daughter either.

Essentially, although William Williams' words were sufficient to create a trust, the fact that the trust was purportedly created partly from property that William Williams did not own meant that his intention to create a trust was negated. It is likely that Lindley LJ might have identified that there was a trust in existence as regards the testator's own life assurance policy if this had been dealt with separately from his wife's life assurance policy. However, because they were discussed together, Lindley LJ considered that no trust could have been intended; what was intended was that Lucy Williams should become the owner of the moneys payable under his life assurance policy, and though he expressed a wish for her to leave this to his daughter, it did not create an obligation enforceable at law.

A.L. Smith LJ characterises the problem slightly differently. He argues that where the testator intended to create a trust, he uses a consistent form of wording. Accordingly, the

other clauses in his will, where he disposes of his books and medical instruments, are identically worded as regards the obligations imposed. The clause at issue contains a different form of words, and therefore A.L. Smith LJ concludes that the testator's intentions as regards this clause must have been different. Therefore, if the earlier clauses were intended to create a trust, then the final clause was not written with this intention, because if it were, the testator would have been expected to use the same form of wording as he had used in relation to each of the previous clauses.

The wording of the trust will therefore be extremely important in order to determine whether a trust was intended. Using the word 'trust' will suggest that there was an intention to create a trust (see for example the judgment of Hart J in *Bath and North East Somerset Council v Attorney General* [2002] EWHC 1623 (Ch), where he explains):

> It does not seem to me that the fact that the trusts declared were invalid . . . assists on the question whether a trust in the true sense was intended. To read the words 'upon trust that' as merely precatory[2] something more is required than to show that, unless so read, the provision is unenforceable. In the first place, if all that had been intended was a reference to the statutory purposes, it would have been simple for the conveyance to have been so expressed. Instead one finds an elaborate formula which is plainly trying to do something more . . . In the second place, the words 'upon trust' cannot, in my judgment, simply be ignored.

This may however be rebutted by evidence to the contrary, such as where the settlor either uses the word trust but describes an entirely different relationship, or where he or she uses the word trust in the sense of 'I trust' (i.e. anticipate or expect) that this will be the case.

Nevertheless, a trust may have been intended even where the word trust is not used.[3] In the case of *Paul v Constance* [1977] 1 All ER 195 for example, the fact that the settlor had told his partner that the money in his bank account belonged as much to her as it did to him was sufficient evidence of an intention to create a trust, especially as they had routinely used the bank account as though it were a joint account. Accordingly, when Mr Constance died intestate, his wife (to whom he was still legally married, although they had separated many years before) did not succeed in claiming that as she was the sole inheritor of his estate under the law on intestacy, she was entitled to inherit the money in the account. Instead, the court found that Mr Constance had created a trust of the bank account for the benefit of himself and his partner, Mrs Paul. Accordingly, on his death, Mrs Paul was entitled to the money in the account.

ACTIVITY

Consider the following legacies. Does the wording give rise to a trust, or do the words used merely indicate the testator's preference concerning the use of the property?

(a) A leaves his entire estate to his wife 'in full confidence that she would do what was right as to the disposal thereof between his children, either in her lifetime or by will after her decease'.

(b) B leaves 'the whole of my real and personal estate and property absolutely in full confidence that she will make such use of it as I should have made myself and that at her

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[2] Precatory means relating to a wish or desire, a hope or an expectation that something will happen as opposed to conferring a binding obligation.

[3] *Twinsectra Ltd v Yardley* [2002] UKHL 12.

death she will devise it to such one or more of my nieces as she may think fit and in default of any disposition by her thereof by her will or testament I hereby direct that all my estate and property acquired by her under this my will shall at her death be equally divided among the surviving said nieces'.

1. Do you consider that there was an intention for the wife in each of these cases to become a trustee for the benefit of the children/nieces?
2. These clauses derive from two cases – *Adams v Kensington Vestry* (1884) 27 Ch D 394 and *Comiskey v Bowring Hanbury* [1905] AC 84. Read these cases and consider whether or not a trust had been created. How did the judges in each case justify their conclusions?

Both *Adams v Kensington Vestry* (1884) 27 Ch D 394 and *Comiskey v Bowring Hanbury* [1905] AC 84 concerned testators who had each written a will leaving his estate to his wife, and then containing a direction as to what other beneficiaries should be considered. In *Adams v Kensington Vestry* no trust was found, as the wording used by the testator did not indicate that a trust was intended. On the other hand, in *Comiskey v Bowring Hanbury,* a trust was upheld for the benefit of the testator's nieces. A number of possible explanations may be given for this difference.

Firstly, the difference in wording may be considered. For example 'doing what is right' does not necessarily mean 'giving money to' whereas 'to devise' means 'to give'. Accordingly, the fact that both wills use the phrase 'in full confidence' is somewhat misleading – the other words in the clauses indicate that *Adams* and *Comiskey* are not similar in terms of the obligations they impose.

Secondly, it may be considered that there is a greater need for a trust to be recognised in *Comiskey* than in *Adams*. The significance here is the nature of the relationship between the apparent trustee and the apparent beneficiary. In *Adams*, the obligation was imposed on a mother to care for her own children, and it might be considered that a parent would do this without the compulsion of a legal obligation. In *Comiskey* however, the apparent beneficiaries were the testator's nieces, who were therefore persons with no connection to the apparent trustee. It might be considered that a person would not provide for their spouse's nieces unless there was some formal obligation to do so.

Similarity of wording will not therefore necessarily lead to two cases being decided in the same way. Much will depend on the context in which the words were used, and the wider implications of those words. For example, in the case of *Re Steele's Will Trusts* [1948] Ch 603, the testatrix had written a will which, on the face of it, expressed a general wish, but no trust regarding her intentions for the future of the property. The relevant clause stated:

> I give my diamond necklace to my son to go and be held as an heirloom by him and by his eldest son on his decease and to go and descend to the eldest son of such eldest son and so on to the eldest son of his descendants as far as the rules of law and equity will permit (and I request my said son to do all in his power by his will or otherwise to give effect to this my wish).

The problematic part of this clause was the request contained in the parentheses. Did this make the son a trustee of the necklace, or was the obligation merely the expression of a hope or a wish? Earlier cases[4] might have regarded the words used as being

[4] *Re Adams and Kensington Vestry* (1884) 27 ChD 394, 410.

sufficient to create a trust as opposed to being merely precatory, but by 1948, the words used were generally not regarded as being sufficient to give rise to a trust.[5] However, because the testatrix had specifically indicated that she had adopted the wording used in an earlier (valid) trust,[6] it was held that there had been a sufficiently strongly manifested intention to create a trust, and a trust was upheld. Accordingly the wording used must be sufficiently unambiguous, although what is unambiguous will depend on context, and, of course, the extent to which the lawyers are able to convince the court of their point of view.

Conduct

In addition to considering the words used by the settlor, the court will also look at the settlor's conduct, and consider whether he or she has acted in a manner that is consistent with an intention to create a trust – and, where applicable, whether the settlor's conduct is consistent with his or her stated intention. Therefore if Donna states 'I am creating a trust' but her conduct is not consistent with that statement, the words used, despite being unambiguous, will not be sufficient to create a trust. After all, one may say 'I am riding a bicycle' but saying so does not mean that one is in fact riding a bicycle. The character of the settlor's conduct is likely to be particularly important in the context of *inter vivos* trusts where there may not be a written document to which the court may refer – with a will, the fact that a person has deliberately written a will provides at least some manifestation of an intention to create a trust. With an *inter vivos* trust, the intention may not be as readily discerned, especially as people may say things that they do not mean, or say things that they do not intend as legally binding statements. Accordingly, with an *inter vivos* trust, a much greater emphasis is placed on ensuring that the settlor's conduct is consistent with an intention to create a trust. The case of *Re Kayford* [1975] 1 All ER 604 represents an interesting example of a trust where the intention is identified from the settlor's conduct.

EXTRACT

Re Kayford [1975] 1 All ER 604

Case facts

Kayford Limited was a mail order company. It operated on the basis that customers would order goods and payment was due when the order was made. By November 1972 the company was in considerable financial difficulty and sought the advice of its accountants on how it could protect its customers in the event of it becoming insolvent. Kayford was advised to open a separate bank account called the Customers' Trust Deposit Account into which it should place any money received from customers until such time as the goods those customers had ordered had been shipped. Therefore, if Kayford went into liquidation before any customers had received their goods, the customers' money could be returned to them. As had been foreseen, Kayford did go into liquidation, and therefore the matter to be decided by the High Court was whether a valid trust had been created.

Megarry J

When I take as a whole the affidavits of Mr Wainwright [the accountant], Mr Kay [Kayford's Managing Director] and Mr Hall (the bank manager) I feel no doubt that the intention was that

[5] *Re Hamilton* [1895] 2 Ch. 370, *Re Williams* [1897] 2 Ch. 12 and *Re Hill* [1902] 1 Ch. 537.
[6] *Shelley v Shelley* (1868) LR 6 Eq 540.

there should be a trust. There are no formal difficulties. The property concerned is pure personalty, and so writing, though desirable, is not an essential. There is no doubt about the so-called 'three certainties' of a trust. The subject-matter to be held on trust is clear, and so are the beneficial interests therein, as well as the beneficiaries. As for the requisite certainty of words, it is well settled that a trust can be created without using the words 'trust' or 'confidence' or the like: the question is whether in substance a sufficient intention to create a trust has been manifested.

In *Re Nanwa Gold Mines Ltd* the money was sent on the faith of a promise to keep it in a separate account, but there is nothing in that case or in any other authority that I know of to suggest that this is essential. I feel no doubt that here a trust was created. From the outset the advice (which was accepted) was to establish a trust account at the bank. The whole purpose of what was done was to ensure that the moneys remained in the beneficial ownership of those who sent them, and a trust is the obvious means of achieving this. No doubt the general rule is that if you send money to a company for goods which are not delivered, you are merely a creditor of the company unless a trust has been created. The sender may create a trust by using appropriate words when he sends the money (though I wonder how many do this, even if they are equity lawyers), or the company may do it by taking suitable steps on or before receiving the money. If either is done, the obligations in respect of the money are transformed from contract to property, from debt to trust. Payment into a separate bank account is a useful (though by no means conclusive) indication of an intention to create a trust, but of course there is nothing to prevent the company from binding itself by a trust even if there are no effective banking arrangements.

Nevertheless, as with the wording of the trust, interpreting what was intended by the settlor's conduct is often a difficult task. Accordingly, in the case *of Re Farepak Food and Gifts Ltd* [2006] All ER (D) 265, although it depended on similar facts to those seen in *Kayford*, no trust was discovered in this case, with the High Court in this instance being reluctant to construe the company's conduct as giving rise to a trust.

EXTRACT

Re Farepak Food and Gifts Ltd [2006] All ER (D) 265 (Dec)

Case facts

Farepak was a Christmas savings club. Farepak agents collected money during the year from customers, and then in December, customers could use the money they had saved in order to buy food and Christmas gifts. The company went into liquidation. Most of the money the customers had saved was swallowed up by Farepak's considerable debts. However, three days before Farepak had gone into administration, it had sought to protect money paid by customers from that date onwards. A deed of trust was drawn up, but this document contained a number of fundamental flaws, including identifying the wrong bank account as the subject matter of the trust.

The first argument

The customers argued that three types of trust might have been created for their benefit. The first of these was a Quistclose trust (after the case of *Barclays Bank v Quistclose Ltd* [1970]

AC 567) whereby a trust was created when the customers paid their money to Farepak's agents. Mann J dismissed this argument.

Mann J

He [counsel for the customers] argued that an analysis of the facts and the customer conditions showed that there was a payment for a specific purpose, and that since that purpose had not been fulfilled the customer money was held on resulting trust. The purpose in question was the provision of vouchers (or other products elected by the customer). So far as the customer conditions are concerned he relied on a term which provided that payments must be 'completed in full' before any entitlement arose, and that as between categories of goods ordered the payment would be allocated in a given priority – first vouchers, the frozen hampers, then grocery hampers and so on down the line. He pointed out that if the price were altered the customer has the right to the return of the contributions in full, and the same was true if there were a substitution.

This argument, if good, would work to the theoretical benefit of all customers of Farepak in the 2006 Farepak year, and not just those whose payments were received at the time under consideration in this application (though there is no practical benefit to most of them because most of the money has gone anyway). Unfortunately, on the material that I have had the argument fails. I have already held that the money is taken by the Agents as agent for Farepak. That of itself does not militate against the existence of a Quistclose trust. However, there is no suggestion that the Agent was expected to keep the money separate from other money (or indeed his or her own), and it is indeed known that it was mixed with the money of others and paid over to Farepak with the money of others. Again, that of itself it not inconsistent with a Quistclose trust, but it does not help. But crucially, there is no suggestion that the money ought to have been put on one side by Farepak pending the transmutation from credited money to goods or vouchers. If there were a Quistclose trust then that obligation would have been inherent in it, but the business model would have made no sense. It would have required Farepak to have kept all the customer moneys in a separate account from January until November, untouched until the time when the goods or vouchers were acquired and then sent out. That is completely implausible. It would turn Farepak into a very odd savings organisation. Even banks do not have to do that. Mr Trace [counsel] urged on me that the description of this as a savings scheme (which is how it was described in some publicity) indicated that there was a trust until the vouchers/goods were provided, and pointed to an OED definition which he said supported him. I am afraid it gives him no support at all. The concept of a trust is not inherent in the use of the word 'savings'; indeed, most savings organisations do not operate via a trust at all. They operate at the level of contract and debt.

On analysis it is apparent enough that what the customer was making was advance payments towards the purchase price of goods or vouchers. The payments were noted on the relevant cards. When the price had been paid the customer was entitled to the chosen goods or vouchers. That describes, and is, a contractual relationship. The provision for the return of money if the price went up, or if acceptable goods were not provided, are contractual terms for the return of an equivalent amount of money, not money held on trust.

The second argument

The second argument was that a constructive trust had been created. Any money in the company's bank account during its last three days of trading should be construed as belonging to the customers. This argument was also rejected on the basis that the money in the account during those last three days might have been paid into the account several days beforehand, before being credited to the account. Also, money may have been paid to the agents some time before they paid the money into the account. Accordingly, it was impossible to say what amount of money should form the subject matter of the trust.

Mann J

I am afraid that I cannot determine that all the moneys in relation to which I am asked to make a decision fall within that line of argument. If I am to apply the underlying principles which are demonstrated by *Neste Oy* then I have to apply them by reference to the time at which the moneys should be taken to have been paid to and received by Farepak. That is not necessarily the same date as the credit appeared in the current account, and that is for two reasons. First, in the case of items with a three day clearing cycle, some of the items credited on 11th October will be items which were 'paid into' the HOCA on 9th October (outside the period) and some items credited on 12th October will be items 'paid into' HOCA on 10th October (again outside the period). It is not clear on the citation of authorities that I have referred to that it is right to take the date at the end of the clearing cycle as being the date of receipt for these purposes. If the correct analysis is a mistake analysis, at the time when the payment was made in the sense of moneys being paid to the bank there was no relevant mistake because the company had not yet decided to cease trading. The same is true of payments directly into the current account – some of those credited on 11th and 12th October will represent moneys paid in on 9th and 10th October though probably not much money falls into this category. But second, it is in fact even more complicated than that. All the money thus credited is money that had been paid, by some mechanism or another, to Agents before they ever got anywhere near a Natwest account. Since the Agents are agents of the company, receipts by those Agents fall to be treated as receipts by the company. If, as is possible on a scale unknown to me at present, those Agents received cash but paid in with their own cheques, then in a real sense the company has already received the money. Much of that money is likely to have been collected by the Agents outside the hiatus period . . . I very much regret coming to this decision. Had it been possible to arrive at a firmer conclusion, applying an appropriate degree of robustness, I would very much have liked to have done so. However, I consider that even allowing for the desirability of distributing now, if at all possible, the material does not exist which makes it sufficiently clear for present purposes that the sums which are said to come within the constructive trust do in fact do so. It is not clear to me whether it is possible to determine that at least some relevant sums do come within the possible trust. I suspect that that will take some work to ascertain that, and that work will be difficult.

The third argument

The customers' third argument was that the trust deed that Farepak had executed was sufficient to give rise to a trust. Although Mann J conceded that it was possible that an intention to create a valid trust might be identified if the document was rectified so as to identify the subject matter of the trust accurately, then a valid trust might exist. However, one difficulty was that when the money was paid into the bank account, the customers were already creditors – in that they had already paid their money to the agents. They could not therefore use the trust deed to acquire preferential treatment over Farepak's other creditors. But, if any customers could be identified as having paid their money directly to Farepak rather than to the agents, then a trust in favour of those customers only might be possible. Mann J conceded that these customers might be few and far between and difficult to identify, but if those obstacles could be overcome, they might legitimately be construed as beneficiaries under a trust.

The outcome

Ultimately, very few customers received a very small amount of money. Therefore, despite an attempt to create a trust, and conduct that might have been construed as giving rise to a trust, the High Court was not willing to identify Farepak's conduct as amounting to the conduct of a settlor.

In order to create a valid trust, the settlor must not only declare an intention to create a trust, he or she must also act upon that intention. Accordingly, declaring a trust is not sufficient unless, in situations where the settlor does not intend to act as trustee him- or herself, there is a transfer of the trust property to the trustee. Where there is such a transfer of property, a trust is more readily discovered. However, where the settlor declares him- or herself to be the trustee, the courts must find that an intention to create a trust has been demonstrated, and as is shown in the case of *Jones v Lock* (1865) LR 1 Ch App 25 (see Chapter 7) and *Richards v Delbridge* (1874) LR 18 Eq 11, this can be problematic.

In *Richards v Delbridge*, John Delbridge was the owner of a lease over a mill. He wrote a memorandum which he attached to the lease indicating that from the date of the memorandum, the lease belonged to John Delbridge's grandson, Edward Richards. The memorandum was not sufficient to transfer the lease to Edward Richards as a gift because the leasehold title to the mill was not transferred to him. Neither was there a trust in Edward's favour. There had been no valid transfer of the lease to any trustee, but John Delbridge had not declared himself to be the trustee of the mill either. George Jessel MR explains:

> The principle is a very simple one. A man may transfer his property, without valuable consideration, in one of two ways: he may either do such acts as amount is law to a conveyance or assignment of the property, and thus completely divest himself of the legal ownership, in which case the person who by those acts acquires the property takes it beneficially, or on trust, as the case may be; or the legal owner of the property may, by one or other of the modes recognised as amounting to a valid declaration of trust, constitute himself a trustee, and, without an actual transfer of the legal title, may so deal with the property as to deprive himself of its beneficial ownership, and declare that he will hold it from that time forward on trust for the other person. It is true he need not use the words, 'I declare myself a trustee,' but he must do something which is equivalent to it, and use expressions which have that meaning; for, however anxious the Court may be to carry out a man's intention, it is not at liberty to construe words otherwise than according to their proper meaning.

It was clear here that what John Delbridge intended was to transfer the lease to his grandson, and not to declare himself to be the trustee for Edward Richards' benefit. Accordingly, because he had failed to do this in the appropriate form, the courts were not willing to construe a trust as a method of circumventing the law. John Delbridge's intention was to give a gift. Neither his words nor his conduct suggested the intention to create a trust, and the court declined to find one.

Both these cases indicate that a clear intention to give specific property to a specific person do not necessarily demonstrate an intention to create a trust. What the courts look for is an intention to create a trust, and therefore no trust will exist if no such intention may be discerned from either the words used by the settlor (in the case of a will) or the combination of his or her words and his or her conduct in the case of *inter vivos* trusts. With no intention there is no trust. With the other two certainties, there may be a trust, albeit one that fails. But with no certainty of intention, the courts will not create a trust from nothing – not even a desire to confer a benefit.

As with other areas of the law of England and Wales, there are no precise rules regarding what conduct or wording will be sufficient to manifest an intention to create a trust. Accordingly, it is the responsibility of the settlor to declare his or her intentions as clearly and as unambiguously as possible. However, what is unambiguous to one person is extremely unclear from the point of view of another. Unfortunately, in the

context of trusts, because the ambiguity relates to one's entitlement to property, it is an area where any lack of certainty of intention may be emphasised by those who may stand to gain from there not being a trust, and conversely, any suggestion of the settlor having intended to create a trust will be emphasised by those who stand to gain from the trust. The responsible lawyer acting for the settlor must therefore ensure that the wording of any trust document (*inter vivos* or will) is unambiguous. Where one acts for those who may benefit if no trust exists (who may be those who will inherit if a deceased settlor dies intestate as the result of an invalid will, or a defunct company's non-customer creditors), then the skill of the lawyer is to maximise the ambiguity of the declaration of a purported trust, and to argue that no such relationship was envisaged by the putative settlor. On the other hand, where one acts for the apparent beneficiaries, then the emphasis must be on establishing that the settlor's words and conduct can only have been intended to be used in order to declare that A owns something for the benefit of B.

The certainty of subject matter

The second of the three certainties is the certainty of subject matter. Certainty of subject matter incorporates a number of aspects. Firstly, the trustee(s) must be able to distinguish the subject matter of the trust from the settlor's other property. Accordingly, one aspect of this certainty is the need to ensure that the subject matter of the trust is defined and identified with sufficient precision. Therefore if Donna creates a trust of a necklace for the benefit of Benny, the trustees must be sufficiently clear as to which necklace was intended. The reasoning behind this is fairly straightforward. Essentially, the courts exist to resolve disputes that lead to litigation. Accordingly, the courts need to be able to identify whether or not the trustees have breached their obligations. If the trustees have not given the trust property to the beneficiaries, or have not given the correct property, then the courts are able to identify that a breach of trust has occurred. On the other hand, if the courts are only able to conclude that the trustees might or might not have given the correct property to the beneficiaries, then the courts are not able to discharge their function of resolving disputes between parties. Therefore, from a legal point of view, it is imperative that the trust property is defined sufficiently precisely.

The second element of certainty as regards subject matter is the need to ensure that the trust property can properly form the subject matter of a trust. Accordingly, no trust can be created from that which cannot be owned and, more specifically, no trust can be created from property that the settlor does not own.

Defining the trust property with sufficient certainty

In relation to both will trusts and *inter vivos* trusts, there is a need for the declaration of trust to identify the trust property with sufficient precision. As was outlined above 'my necklace' is insufficiently precise if the settlor owns several necklaces, particularly if they have different value. Accordingly, imprecise quantities such as 'the bulk of my estate' (the wording used in *Palmer v Simmonds* (1854) 61 ER 704) are insufficiently precise for the purposes of identifying the subject matter of the trust with sufficient certainty.

Nevertheless, the courts have been willing to quantify the subject matter of the trust where they are able to make a judgment as to what would be appropriate. In the case of *Re Golay* [1965] 2 All ER 660 for example, the settlor wrote a will that allowed the

beneficiary to live in one of the flats he owned for her lifetime, and to derive a reasonable income from his other properties. Although it would appear that 'one of my flats' is imprecise in the will, the imprecision is removed on the settlor's death when the beneficiary is able to choose which one from a precise class of property ('flats') she wishes to inhabit. Accordingly, this aspect of the will was not problematic, although as we shall see below, uncertainty may arise from this approach to identifying the subject matter of the trust. More problematic for the courts, however, was the direction that the beneficiary should receive a reasonable income from the settlor's other properties. Ungoed-Thomas J explains however in *Re Golay* that there is no reason why such wording would be uncertain:

> Another question that arises is whether this gift of reasonable income fails for uncertainty. There are two classes of case with which I am concerned in interpreting this particular provision in the will: the first is where a discretion is given to specified persons to quantify the amount; the other class of case is where no such discretion is expressly conferred on any specified person. It is common ground that in this case the trustees are not given that discretion, so that, if 'reasonable income' does not fail for uncertainty, then it would be open to a beneficiary to go to court to ascertain whether any amount quantified by the trustees was a 'reasonable' amount in accordance with the provisions of the will. The question therefore comes to this: whether the testator by the words 'reasonable income' has given a sufficient indication of his intention to provide an effective determinant of what he intends so that the court in applying that determinant can give effect to the testator's intention.
>
> Whether the yardstick of 'reasonable income' were applied by trustees under a discretion given to them by a testator or applied by a court in course of interpreting and applying the words 'reasonable income' in a will, the yardstick sought to be applied by the trustees in the one case and the court in the other case would be identical. The trustees might be other than the original trustees named by the testator and the trustees could even surrender their discretion to the court. It would seem to me to be drawing too fine a distinction to conclude that an objective yardstick which different persons sought to apply would be too uncertain, not because of uncertainty in the yardstick but as between those who seek to apply it.
>
> In this case, however, the yardstick indicated by the testator is not what he or any other specified person subjectively considers to be reasonable but what he identifies objectively as 'reasonable income'. The court is constantly involved in making such objective assessments of what is reasonable and it is not to be deterred from doing so because subjective influences can never be wholly excluded. In my view the testator intended by 'reasonable income' the yardstick which the court could and would apply in quantifying the amount so that the direction in the will is not in my view defeated by uncertainty.

In essence, what Ungoed-Thomas J says here is that what is uncertain is the judgment of different people regarding what is reasonable, that one person's view of what is reasonable may differ from another. However, that is not what the settlor advocates – the settlor advocates an objective evaluation of what would be reasonable under the circumstances, and that this is something that the courts are well accustomed to evaluating. Accordingly, he saw no difficulty with the subject matter of this trust, and it did not fail for want of certainty.

A further difficulty is that the trust property may be defined with sufficient precision, but the apportionment of such property between different classes of beneficiary has

not been precisely defined. As we saw in the context of *Re Golay* above, this is often not problematic. In *Re Golay* we saw how the beneficiary could enjoy one of the settlor's flats, and any uncertainty as regards subject matter was resolved once she had selected which flat was to be the subject matter of the trust. However, a trust may fail for uncertainty where the beneficiary makes no selection. This problem is illustrated with reference to the case of *Boyce v Boyce* (1849) 16 Sim 476.

EXTRACT

Boyce v Boyce (1849) 16 Sim 476

Case facts

The settlor created a trust comprising of the houses he owned. The terms of the trust were that one of his daughters, Maria Boyce, was to select which house she wished to receive, and once she had made her choice, the testator's other daughter, Charlotte Boyce, was to be entitled to the settlor's other houses. However, Maria Boyce died before having selected which of the houses she wished to have.

Judgment

THE VICE-CHANCELLOR, without hearing them, said that the gift in favour of Charlotte was a gift, not of all the testator's freehold houses situate on the North Cliff in Southwold, but of all the other of his freehold houses which Maria should not choose; and, therefore, it was only a gift of the houses that should remain, provided Maria should choose one of them: that no choice had been, or, indeed, could have been made by Maria, and, therefore, the gift in favour of Charlotte had failed.

This case illustrates that although it is possible for people other than the settlor to define the trust property, there are pitfalls of which the prudent settlor and solicitor need to be aware.

Identification of the trust property is often easier in the context of an express *inter vivos* trust where there is a transfer of the trust property to the trustee. In this situation it is far clearer which 'necklace' for example is to be the subject matter of the trust, than is the case where the settlor declares him- or herself to be the trustee. However, in relation to *inter vivos* trusts, further problems arise when the purported trust property has not been separated from the larger bulk of the trustee's assets.

Separating the trust property from other property

In relation to will trusts, it is sufficient that the subject matter of the trust is defined with sufficient precision according to the wording of the trust. However, with *inter vivos* trusts, it is necessary also to separate the trust property from the larger bulk of the settlor or trustee's property. Accordingly, where customer's money has been kept apart from money belonging to the company, a number of cases, such as *Re Kayford* (above) have identified the money that is kept apart from the company's other assets as being held on trust for customers in the event that the company becomes insolvent and is unable to fulfil customers' orders. An example of this can be seen from the case of *Barclays Bank v Quistclose Investments* [1970] AC 567.

EXTRACT

Barclays Bank v Quistclose Investments [1970] AC 567

Case facts

A company called Rolls Razor Ltd were in financial difficulties, to the extent that they had exceeded their overdraft limit with Barclays Bank by a considerable sum. Barclays Bank refused to lend Rolls Razor any more money. Accordingly, Rolls Razor succeeded in obtaining a loan from Quistclose. One of the conditions of Quistclose's loan was that it was used to pay a dividend that was to become payable to Rolls Razor's shareholders. Furthermore, the loan was to be paid into a separate account. Rolls Razor went into voluntary liquidation without having paid the dividend. Quistclose therefore took action against Rolls Razor arguing that the loan had been given by way of a trust in order to pay the dividend to the shareholders, and when that trust failed, the money was to be held on a resulting trust for Quistclose as the settlors. Because Barclays Bank had notice of the trust, it too should be treated as a constructive trustee for the benefit of Quistclose.

Lord Wilberforce

Two questions arise, both of which must be answered favourably to the respondents if they are to recover the money from the bank. The first is whether as between the respondents and Rolls Razor Ltd. the terms upon which the loan was made were such as to impress upon the sum of £209,719 8s. 6d. a trust in their favour in the event of the dividend not being paid. The second is whether, in that event, the bank had such notice of the trust or of the circumstances giving rise to it as to make the trust binding upon them.

It is not difficult to establish precisely upon what terms the money was advanced by the respondents to Rolls Razor Ltd. There is no doubt that the loan was made specifically in order to enable Rolls Razor Ltd. to pay the dividend. There is equally, in my opinion, no doubt that the loan was made only so as to enable Rolls Razor Ltd. to pay the dividend and for no other purpose. This follows quite clearly from the terms of the letter of Rolls Razor Ltd. to the bank of July 15, 1964, which letter, before transmission to the bank, was sent to the respondents under open cover in order that the cheque might be (as it was) enclosed in it. The mutual intention of the respondents and of Rolls Razor Ltd., and the essence of the bargain, was that the sum advanced should not become part of the assets of Rolls Razor Ltd., but should be used exclusively for payment of a particular class of its creditors, namely, those entitled to the dividend. A necessary consequence from this, by process simply of interpretation, must be that if, for any reason, the dividend could not be paid, the money was to be returned to the respondents: the word 'only' or 'exclusively' can have no other meaning or effect. That arrangements of this character for the payment of a person's creditors by a third person, give rise to a relationship of a fiduciary character or trust, in favour, as a primary trust, of the creditors, and secondarily, if the primary trust fails, of the third person, has been recognised in a series of cases over some 150 years . . .

The second, and main, argument for the appellant was of a more sophisticated character. The transaction, it was said, between the respondents and Rolls Razor Ltd., was one of loan, giving rise to a legal action of debt. This necessarily excluded the implication of any trust, enforceable in equity, in the respondents' favour: a transaction may attract one action or the other, it could not admit of both.

My Lords, I must say that I find this argument unattractive. Let us see what it involves. It means that the law does not permit an arrangement to be made by which one person agrees to advance money to another, on terms that the money is to be used exclusively to pay debts

of the latter, and if, and so far as not so used, rather than becoming a general asset of the latter available to his creditors at large, is to be returned to the lender. The lender is obliged, in such a case, because he is a lender, to accept, whatever the mutual wishes of lender and borrower may be, that the money he was willing to make available for one purpose only shall be freely available for others of the borrower's creditors for whom he has not the slightest desire to provide.

I should be surprised if an argument of this kind – so conceptualist in character – had ever been accepted. In truth it has plainly been rejected by the eminent judges who from 1819 onwards have permitted arrangements of this type to be enforced, and have approved them as being for the benefit of creditors and all concerned. There is surely no difficulty in recognising the co-existence in one transaction of legal and equitable rights and remedies: when the money is advanced, the lender acquires an equitable right to see that it is applied for the primary designated purpose (see *In re Rogers*, 8 Morr. 243 where both Lindley L.J. and Kay L.J. recognised this): when the purpose has been carried out (i.e., the debt paid) the lender has his remedy against the borrower in debt: if the primary purpose cannot be carried out, the question arises if a secondary purpose (i.e., repayment to the lender) has been agreed, expressly or by implication: if it has, the remedies of equity may be invoked to give effect to it, if it has not (and the money is intended to fall within the general fund of the debtor's assets) then there is the appropriate remedy for recovery of a loan. I can appreciate no reason why the flexible interplay of law and equity cannot let in these practical arrangements, and other variations if desired: it would be to the discredit of both systems if they could not. In the present case the intention to create a secondary trust for the benefit of the lender, to arise if the primary trust, to pay the dividend, could not be carried out, is clear and I can find no reason why the law should not give effect to it.

I pass to the second question, that of notice. I can deal with this briefly because I am in agreement with the manner in which it has been disposed of by all three members of the Court of Appeal. I am prepared, for this purpose, to accept, by way of assumption, the position most favorable to the bank, i.e., that it is necessary to show that the bank had notice of the trust or of the circumstances giving rise to the trust, at the time when they received the money, viz., on July 15, 1964, and that notice on a later date, even though they had not in any real sense given value when they received the money or thereafter changed their position, will not do. It is common ground, and I think right, that a mere request to put the money into a separate account is not sufficient to constitute notice. But on July 15, 1964, the bank, when it received the cheque, also received the covering letter of that date which I have set out above: previously there had been the telephone conversation between Mr. Goldbart and Mr. Parker, to which I have also referred. From these there is no doubt that the bank was told that the money had been provided on loan by a third person and was to be used only for the purpose of paying the dividend. This was sufficient to give them notice that it was trust money and not assets of Rolls Razor Ltd.: the fact, if it be so, that they were unaware of the lender's identity (though the respondent's name as drawer was on the cheque) is of no significance. I may add to this, as having some bearing on the merits of the case, that it is quite apparent from earlier documents that the bank were aware that Rolls Razor Ltd. could not provide the money for the dividend and that this would have to come from an outside source and that they never contemplated that the money so provided could be used to reduce the existing overdraft. They were in fact insisting that other or additional arrangements should be made for that purpose. As was appropriately said by Russell L.J., ([1968] Ch. 540, 563F) it would be giving a complete windfall to the bank if they had established a right to retain the money.

Outcome

Because of the specific purpose for which the loan had been granted, and the emphasis on separating the loan money from other assets, there was clearly a trust in existence, the subject matter of which was defined with sufficient precision.

However, where goods ordered by customers have not been separated from a larger bulk, the courts have tended to find that no trust can exist, particularly in relation to tangible goods. This rule has come about as a result of a number of cases where it was argued that a trust existed for the benefit of a defunct company's customers. In each case, the court declined to find that there was a trust in existence. However, it may be that in each of these cases, the existence of a trust would have rendered the company's customers as preferential creditors. In a situation where a company's debts outweigh its assets, this could be regarded as an undesirable outcome, as there would be less scope for other creditors to be repaid.

Therefore, in cases where the situation does not involve a company in liquidation, the courts may wish to distinguish these authorities, and indeed this is what Dillon LJ attempted to do in *Hunter v Moss* [1994] 3 All ER 215, but this was later interpreted as an attempt to distinguish between tangible and intangible goods. Accordingly, the general rules appear to be that in relation to *inter vivos* trusts there is a need to separate the trust property from the larger bulk of the settlor's other property, especially where the trust relates to tangible goods. In the case of *Re London Wine Co (Shippers)* [1986] PCC 121 for example, a company of wine merchants became insolvent, and the company's customers sought to argue that the wine they had bought was held on trust for them.

However, because the wine that had been bought had not been separated from the company's other stock, it was not sufficiently certain what wine should form the subject matter of the trust. In the context of wine in a warehouse, it may be argued that this is justified, in that it may be unclear what type of wine was intended to form the subject matter of the trust, and even in the context of particular wine from a particular vintage, there may be considerable variations in the quality of the bottles. This justification may be less apparent where all the goods have equal value, as in the case of the gold bullion in the Privy Council case of *Re Goldcorp Exchange* [1995] 1 AC 74 (below), although the same approach was used.

In relation to intangible assets, such as money in a bank account, separation of the money from the company's other assets is advantageous (see *Re Kayford* and *Barclays Bank v Quistclose Investments,* above) but may not always be necessary. However, the fact that intangible assets are not separated from the company's other assets may be interpreted as meaning that no intention to create a trust has been manifested (*Re Farepak Food and Gifts Ltd*, above).

In the context of trusts where the alleged trustee is not insolvent, the courts have taken a broader view of the rules regarding the separateness of the trust property, and have recognised that there is a trust even though the goods have not been separated. The authorities on this point have all related to intangible assets, and therefore how the courts would deal with trusts of tangible goods where the trust property has not been separated from the larger bulk in cases where the trustee is not an insolvent company remains to be seen. This is an interesting example therefore of the law having developed into what it is simply as a consequence of the types of situations that have led to the litigation being pursued as far as the higher courts.

EXTRACT

Re Goldcorp Exchange Ltd [1995] 1 AC 74

Case facts

This case concerned three classes of claimant. The first group of claimants had bought gold bullion from Goldcorp itself. The second claimant, an individual, had bought some rare maple

coins from Goldcorp, and the third group of customers had bought gold from a company called Walker & Hall which had been taken over by Goldcorp Exchange. Goldcorp Exchange became insolvent, and all three groups of claimants argued that Goldcorp Exchange were trustees on their behalf of the gold they had purchased.

Lord Mustill

The claim by Goldcorp Exchange's customers

Their Lordships begin with the question whether the customer obtained any form of proprietary interest, legal or equitable, simply by virtue of the contract of sale, independently of the collateral promises. In the opinion of their Lordships the answer is so clearly that he did not that it would be possible simply to quote section 18 of the Sale of Goods Act 1908 (New Zealand) (corresponding to section 16 of the Sale of Goods Act 1893 (56 & 57 Vict. c. 71)) and one reported case, and turn to more difficult issues. It is, however, convenient to pause for a moment to consider why the answer must inevitably be negative, because the reasons for this answer are the same as those which stand in the way of the customers at every point of the case. It is common ground that the contracts in question were for the sale of unascertained goods. For present purposes, two species of unascertained goods may be distinguished. First, there are 'generic goods.' These are sold on terms which preserve the seller's freedom to decide for himself how and from what source he will obtain goods answering the contractual description. Secondly, there are 'goods sold ex-bulk.' By this expression their Lordships denote goods which are by express stipulation to be supplied from a fixed and a pre-determined source, from within which the seller may make his own choice (unless the contract requires it to be made in some other way) but outside which he may not go. For example, 'I sell you 60 of the 100 sheep now on my farm.'

Approaching these situations a priori common sense dictates that the buyer cannot acquire title until it is known to what goods the title relates. Whether the property then passes will depend upon the intention of the parties and in particular on whether there has been a consensual appropriation of particular goods to the contract . . . Their Lordships therefore turn to consider whether there is anything in the collateral promises which enables the customers to overcome the practical objections to an immediate transfer of title. The most direct route would be to treat the collateral promises as containing a declaration of trust by the company in favour of the customer. The question then immediately arises – What was the subject matter of the trust? The only possible answer, so far as concerns an immediate transfer of title on sale, is that the trust related to the company's current stock of bullion answering the contractual description; for there was no other bullion to which the trust could relate. Their Lordships do not doubt that the vendor of goods sold ex-bulk can effectively declare himself trustee of the bulk in favour of the buyer, so as to confer *pro tanto* an equitable title. But the present transaction was not of this type. The company cannot have intended to create an interest in its general stock of gold which would have inhibited any dealings with it otherwise than for the purpose of delivery under the non-allocated sale contracts. Conversely the customer, who is presumed to have intended that somewhere in the bullion held by or on behalf of the company there would be stored a quantity representing 'his' bullion, cannot have contemplated that his rights would be fixed by reference to a combination of the quantity of bullion of the relevant description which the company happened to have in stock at the relevant time and the number of purchasers who happened to have open contracts at that time for goods of that description. To understand the transaction in this way would be to make it a sale of bullion ex-bulk, which on the documents and findings of fact it plainly was not.

Nor is the argument improved by reshaping the trust, so as to contemplate that the property in the *res vendita* did pass to the customer, albeit in the absence of delivery, and then merged in a general equitable title to the pooled stock of bullion. Once again the argument contradicts the

transaction. The customer purchased for the physical delivery on demand of the precise quantity of bullion fixed by his contract, not a shifting proportion of a shifting bulk, prior to delivery . . .

The next group of arguments for the non-allocated claimants all turn on an estoppel, said to derive from the collateral promises . . . No such estoppel could assist the customers here, for the problem facing them at every turn is not section 18 of the Sale of Goods Act 1908, but the practical reality underlying it which Lord Blackburn called 'the very nature of things:' namely that it is impossible to have a title to goods, when nobody knows to which goods the title relates . . . there was no existing bulk and therefore nothing from which a title could be carved out by a deemed appropriation. The reasoning of *Knights* v. *Wiffen* [(1870) LR 5 QB 660] does not enable a bulk to be conjured into existence for this purpose simply through the chance that the vendor happens to have some goods answering the description of the res vendita in its trading stock at the time of the sale – quite apart, of course, from the fact that if all the purchasers obtained a deemed title by estoppel there would not be enough bullion to go around.

Having for these reasons rejected the submission that the non-allocated claimants acquired an immediate title by reason of the contract of sale and the collateral promises their Lordships turn to the question whether the claimants later achieved a proprietary interest when the company purchased bullion and put it into its own stock. Broadly speaking, there are two forms which such an argument might take.

According to the first, the contracts of sale were agreements for the sale of goods afterwards to be acquired. It might be contended that quite independently of any representation made by the company to the non-allocated claimants, as soon as the company acquired bullion answering the contractual description the purchaser achieved an equitable title, even though the passing of legal title was postponed until the goods were ascertained and appropriated at the time of physical delivery to the purchaser. In the event this argument was not separately pursued, and their Lordships mention it only by way of introduction. They will do so briefly, since it was bound to fail. The line of old cases, founded on *Holroyd* v. *Marshall* (1862) 10 H.L.Cas. 191., was concerned with situations where the goods upon acquisition could be unequivocally identified with the individual contract relied upon. As Lord Hanworth M.R. demonstrated in *In re Wait* [1927] 1 Ch. 606, 622, the reasoning of these cases cannot be transferred to a situation like the present where there was no means of knowing to which, if any, of the non-allocated sales a particular purchase by the company was related. Since this objection on its own is fatal, there is no need to discuss the other obstacles which stand in its way . . .

The second category of argument asserts, in a variety of forms, that the collateral promises operated to impress on the bullion, as and when it was acquired by the company, a trust in favour of each purchaser. If the scheme had contemplated that, properly performed, it would have brought about a transfer of title to the individual customer before that customer's appropriated bullion was mixed in the undifferentiated bulk, analogies could have been drawn with decisions such as *Spence* v. *Union Marine Insurance Co. Ltd.* (1868) L.R. 3 C.P. 427 . . . Since, however, even if the company had performed its obligations to the full there would have been no transfer of title to the purchaser before admixture, these cases are not in point. The only remaining alternative, consistently with the scheme being designed to give the customer any title at all before delivery, is that the company through the medium of the collateral promises had declared itself a trustee of the constantly changing undifferentiated bulk of bullion which should have been set aside to back the customers' contracts. Such a trust might well be feasible in theory, but their Lordships find it hard to reconcile with the practicalities of the scheme, for it would seem to involve that the separated bulk would become the source from which alone the sale contracts were to be supplied: whereas, as already observed, it is impossible to read the collateral promises as creating a sale ex-bulk.

This being so, whilst it is easy to see how the company's failure to perform the collateral obligations has fuelled the indignation created by its failure to deliver the bullion under the sales to non-allocated purchasers, their Lordships are far from convinced that this particular breach has in fact made any difference.

Let it be assumed, however, as did McKay J. [1993] 1 N.Z.L.R. 257, 284 in his dissenting judgment, that the creation of a separate and sufficient stock would have given the non-allocated purchasers some kind of proprietary interest, the fact remains that the separate and sufficient stock did not exist.

The customers' first response to this objection is that even if the concept of an immediate trust derived from a bailment arising at the time of the original transactions cannot be sustained, the collateral promises created a potential or incomplete or (as it was called in argument) 'floating' bailment, which hovered above the continuing relationship between each purchaser and the company, until the company bought and took delivery of bullion corresponding to the claimant's contract, whereupon the company became bailee of the bullion on terms which involved a trust in favour of the purchaser. Their Lordships find it impossible to see how this ingenious notion, even if feasible in principle, could be put into practice here, given that the body of potential beneficiaries was constantly changing as some purchasers called for and took delivery whilst others came newly on the scene, at the same time as the pool of available bullion waxed and waned (sometimes to zero as regards some types of bullion) with fresh deliveries and acquisitions. Even if this is left aside, the concept simply does not fit the facts. True, there is no difficulty with a transaction whereby B promises A that if in the future goods belonging to A come within the physical control of B he will hold them as bailee for A on terms fixed in advance by the agreement. But this has nothing to do with a trust relationship, and it has nothing to do with the present case, since in the example given A has both title to the goods and actual or constructive possession of them before their receipt by B, whereas in the present case the non-allocated claimants had neither. The only escape would be to suggest that every time the company took delivery of bullion of a particular description all the purchasers from the company of the relevant kind of bullion acquired both a higher possessory right than the company (for such would be essential if the company was to be a bailee) and a title to the goods, via some species of estoppel derived from this notional transfer and retransfer of possession. Their Lordships find it impossible to construct such a contorted legal relationship from the contracts of sale and the collateral promises.

Next, the claimants put forward an argument in two stages. First, it is said that because the company held itself out as willing to vest bullion in the customer and to hold it in safe custody on behalf of him in circumstances where he was totally dependent on the company, and trusted the company to do what it had promised without in practice there being any means of verification, the company was a fiduciary. From this it is deduced that the company as fiduciary created an equity by inviting the customer to look on and treat stocks vested in it as his own, which could appropriately be recognised only by treating the customer as entitled to a proprietary interest in the stock. To describe someone as a fiduciary, without more, is meaningless. Here, the argument assumes that the person towards whom the company was fiduciary was the non-allocated claimant. But what kind of fiduciary duties did the company owe to the customer? None have been suggested beyond those which the company assumed under the contracts of sale read with the collateral promises; namely to deliver the goods and meanwhile to keep a separate stock of bullion (or, more accurately, separate stocks of each variety of bullion) to which the customers could look as a safeguard for performance when delivery was called for. No doubt the fact that one person is placed in a particular position vis-à-vis another through the medium of a contract does not necessarily mean that he does not also owe fiduciary duties to that other by virtue of being in that position. But the essence of a

fiduciary relationship is that it creates obligations of a different character from those deriving from the contract itself. Their Lordships have not heard in argument any submission which went beyond suggesting that by virtue of being a fiduciary the company was obliged honestly and conscientiously to do what it had by contract promised to do. Many commercial relationships involve just such a reliance by one party on the other, and to introduce the whole new dimension into such relationships which would flow from giving them a fiduciary character would (as it seems to their Lordships) have adverse consequences far exceeding those foreseen by Atkin L.J. in *In re Wait* [1927] 1 Ch. 606. It is possible without misuse of language to say that the customers put faith in the company, and that their trust has not been repaid. But the vocabulary is misleading; high expectations do not necessarily lead to equitable remedies.

Let it be assumed, however, that the company could properly be described as a fiduciary and let it also be assumed that notwithstanding the doubts expressed above the non-allocated claimants would have achieved some kind of proprietary interest if the company had done what it said. This still leaves the problem, to which their Lordships can see no answer, that the company did not do what it said. There never was a separate and sufficient stock of bullion in which a proprietary interest could be created. What the non-allocated claimants are really trying to achieve is to attach the proprietary interest, which they maintain should have been created on the non-existent stock, to wholly different assets. It is understandable that the claimants, having been badly let down in a transaction concerning bullion should believe that they must have rights over whatever bullion the company still happens to possess. Whilst sympathising with this notion their Lordships must reject it, for the remaining stock, having never been separated, is just another asset of the company, like its vehicles and office furniture. If the argument applies to the bullion it must apply to the latter as well, an obviously unsustainable idea.

Finally, it is argued that the court should declare in favour of the claimants a remedial constructive trust, or to use another name a restitutionary proprietary interest, over the bullion in the company's vaults. Such a trust or interest would differ fundamentally from those so far discussed, in that it would not arise directly from the transaction between the individual claimants, the company and the bullion, but would be created by the court as a measure of justice after the event. Their Lordships must return to this topic later when considering the Walker & Hall claimants who, the trial judge has held, did acquire a proprietary interest in some bullion, but they are unable to understand how the doctrine in any of its suggested formulations could apply to the facts of the present case. By leaving its stock of bullion in a non-differentiated state the company did not unjustly enrich itself by mixing its own bullion with that of the purchasers: for all the gold belonged to the company. It did not act wrongfully in acquiring, maintaining and using its own stock of bullion, since there was no term of the sale contracts or of the collateral promises, and none could possibly be implied, requiring that all bullion purchased by the company should be set aside to fulfil the unallocated sales. The conduct of the company was wrongful in the sense of being a breach of contract, but it did not involve any injurious dealing with the subject matter of the alleged trust. Nor, if some wider equitable principle is involved, does the case become any stronger. As previously remarked the claimants' argument really comes to this, that because the company broke its contract in a way which had to do with bullion the court should call into existence a proprietary interest in whatever bullion happened to be in the possession and ownership of the company at the time when the competition between the non-allocated claimants and the other secured and unsecured creditors first arose. The company's stock of bullion had no connection with the claimants' purchases, and to enable the claimants to reach out and not only abstract it from the assets available to the body of creditors as a whole, but also to afford a priority over a secured

creditor, would give them an adventitious benefit devoid of the foundation in logic and justice which underlies this important new branch of the law. For these reasons their Lordships reject, in company with all the judges in New Zealand, the grounds upon which it is said that the customers acquired a proprietary interest in bullion.

Their Lordships now turn to the proposition, which first emerged during argument in the Court of Appeal, and which was not raised in the *London Wine case* [1986] P.C.C. 121, that a proprietary interest either sprang into existence on the sales to customers, or should now be imposed retrospectively through restitutionary remedies, in relation not to bullion but to the moneys originally paid by the customers under the contracts of sale. Here at least it is possible to pin down the subject matter to which the proprietary rights are said to relate. Nevertheless, their Lordships are constrained to reject all the various ways in which the submission has been presented, once again for a single comparatively simple reason.

The first argument posits that the purchase moneys were from the outset impressed with a trust in favour of the payers. That a sum of money paid by the purchaser under a contract for the sale of goods is capable in principle of being the subject of a trust in the hands of the vendor is clear. For this purpose it is necessary to show either a mutual intention that the moneys should not fall within the general fund of the company's assets but should be applied for a special designated purpose, or that having originally been paid over without restriction the recipient has later constituted himself a trustee of the money: see *Quistclose Investments Ltd.* v. *Rolls Razor Ltd.* [1970] A.C. 567, 581–582. This requirement was satisfied in *In re Kayford Ltd. (In Liquidation)* [1975] 1 W.L.R. 279 where a company in financial difficulties paid into a separate deposit account money received from customers for goods not yet delivered, with the intention of making withdrawals from the account only as and when delivery was effected, and of refunding the payment to customers if an insolvency made delivery impossible. The facts of the present case are, however, inconsistent with any such trust. This is not a situation where the customer engaged the company as agent to purchase bullion on his or her behalf, with immediate payment to put the agent in funds, delivery being postponed to suit the customer's convenience. The agreement was for a sale by the company to, and not the purchase by the company for, the customer. The latter paid the purchase price for one purpose alone, namely to perform his side of the bargain under which he would in due course be entitled to obtain delivery. True, another part of the consideration for the payment was the collateral promise to maintain separate cover, but this does not mean that the money was paid for the purpose of purchasing gold, either to create the separate stock or for any other reason. There was nothing in the express agreement to require, and nothing in their Lordships' view can be implied, which constrained in any way the company's freedom to spend the purchase money as it chose, or to establish the stock from any source and with any funds as it thought fit. This being so, their Lordships cannot concur in the decision of Cooke P. [1993] 1 N.Z.L.R. 257, 272–273, that the purchase price was impressed with a continuing beneficial interest in favour of the customer, which could form the starting point for a tracing of the purchase moneys into other assets.

The same insuperable obstacle stands in the way of the alternative submission that the company was a fiduciary. If one asks the inevitable first question – What was the content of the fiduciary's duty? – the claimants are forced to assert that the duty was to expend the moneys in the purchase and maintenance of the reserved stock. Yet this is precisely the obligation which, as just stated, cannot be extracted from anything express or implied in the contract of sale and the collateral promises. In truth, the argument that the company was a fiduciary (as regards the money rather than the bullion) is no more than another label for the argument in favour of an express trust and must fail for the same reason.

The claim by the individual claimant

The claim by the second respondent differs in only three respects from those of the non-allocated claimants as a whole. First, it is very much larger. He agreed to purchase 1,000 gold maple coins at a price of $732,000. While this entirely explains his special indignation at the conduct of the company, and his consequent decision to pursue a separate claim, it plainly makes no difference to the outcome . . . Acknowledging this, their Lordships cannot find that the distinction makes any difference. Whatever the second respondent may have thought, and whatever the special features of the transaction, the fact remains that it was an agreement for the purchase of generic goods. For the reasons already given such contract even when accompanied by the collateral promises could not create a proprietary interest of any kind . . . The second respondent's purchase was so large by comparison with the company's ordinary retail bullion transactions that the company felt it prudent to reduce its 'short' position in maples by buying in a substantial quantity of extra coins. It was argued on behalf of the second respondent that the coins so purchased were earmarked for the second respondent's purchases and hence through ascertainment and appropriation became his immediate property, only afterwards being wrongfully admixed with the bulk of the bullion in the vault. If this argument were correct, it would follow that not only was the company not entitled to deal with the coins in any other way than to deliver them to the second respondent when called, but also that it could not supply him with coins from any other source. No doubt if the facts were strong enough the court would be able to conclude that this was what the company had done with the implied consent of the second respondent. In the event, however, the evidence of the bullion manager and clerk, upon which the second respondent relied before Thorp J. to prove the appropriation, was (as the judge put it) 'demonstrably against the proposition that the maples purchased by Exchange were purchased expressly for [the second respondent] and therefore appropriated to his contract.' The judge went on to give reasons for this opinion, and nothing in the analysis of the facts presented to the Board gives their Lordships any reason to doubt that the judge's conclusion was correct.

In these circumstances their Lordships are constrained to allow the appeal of the bank in respect of the second respondent for the same reasons as those already given in relation to the non-allocated claimants.

The claim by Walker & Hall's customers

These claims are on a different footing. It appears that until about 1983 the bullion purchased by customers of the predecessor of Walker & Hall Commodities Ltd. was stored and recorded separately. Thereafter, the bullion representing purchases by customers was stored en masse, but it was still kept separate from the vendor's own stock. Furthermore, the quantity of each kind of bullion kept in this pooled mass was precisely equal to the amount of Walker & Hall's exposure to the relevant categories of bullion and of its open contracts with customers. The documentation was also different from that received by the customers who later became the non-allocated claimants. The documents handed to the customer need not be quoted at length, but their general effect was that the vendor did not claim title in the bullion described in the document and that the title to that bullion, and the risk in respect of it, was with the customer. The document also stated that the vendor held the bullion as custodian for the customer in safe storage. These arrangements ceased when the shares of Walker & Hall were purchased by the company, and the contractual rights of the customers were transferred. The features just mentioned persuaded Thorp J. at first instance to hold, in contrast to his conclusion in relation to the non-allocated claimants and the second respondent, that there had been a sufficient ascertainment and appropriation of goods to the individual contracts to transfer title to each customer; and that thereafter the customers as a whole had a shared interest in the pooled bullion, which the vendors held on their behalf.

Accordingly, although the Walker & Hall customers could be regarded as beneficiaries under a trust because their gold bullion had been stored and recorded separately, no such argument could be sustained in relation to the other claimants. Lord Mustill's judgment in relation to the claims made by the Goldcorp customers consistently turns on the same points, which may be summarised as follows:

1. Did the customers acquire a proprietary interest in the gold bullion (a claim for the bullion itself rather than an award of damages for breach of contract) from the date of the contract?

   No, because the property in which the customers claimed to have an interest had not been ascertained.
2. Did the customers collectively have an equitable interest in the gold bullion that Goldcorp had that could be divided between them?

   No, because that was not the nature of the transaction they had entered into.
3. Is there an estoppel that would prevent Goldcorp from reneging on its agreement?

   No, because the subject matter of the estoppel has not been clearly defined.
4. Did the customers acquire a proprietary interest after the date of the contract, when Goldcorp had purchased the gold bullion?

   No, because it was not clear what gold belonged to which customer.
5. Did Goldcorp's promises that were collateral to the contract, whereby title to the gold bullion might be regarded as transferring to the customers prior to delivery, give rise to a trust?

   The Privy Council concluded not, and even if there could have been, it would have been impossible to administer in practice.
6. Could there be a floating entitlement over the bullion that Goldcorp owned?

   No – that was not the nature of the transaction.
7. Was Goldcorp in a fiduciary relationship towards its customers?

   Again, the answer is no – Goldcorp was in a situation where it owed no further obligation beyond the contract. Even if a fiduciary duty were owed, this could not possibly be fulfilled in relation to all the claimants because there was less gold bullion than there were claimants.
8. If there was no express trust, the claimants then posited the argument, was there a constructive trust?

   Again the answer to this question is no because Goldcorp's stock of bullion had no connection with the claimants' purchases.
9. The argument then turned on whether a trust should be imposed retrospectively. Again this was rejected – the relationship was not the type of relationship encountered in *Quistclose* or *Kayford*, and therefore there was nothing that the court could identify as being customers' property as opposed to Goldcorp's property. Neither was there anything to which a fiduciary duty could attach – no-one could identify precisely what property Goldcorp would have a duty to safeguard in the event that the company was to be regarded as a trustee.

Essentially, therefore the trust argument fails on two premises – the relationship of Goldcorp and its customers were as contracting parties not trustee-beneficiary, and even if a trust relationship could be construed, there was no distinction between Goldcorp's own property and that of its customers. Accordingly, the claim of both the first and the second groups of claimants failed.

As a footnote to this discussion, however, the position of the customers would now be different as a matter of contract law, as s.20A of the Sale of Goods Act

1979[7] would permit customers to claim an entitlement to a specified quantity of unascertained goods which form part of a bulk which is identified either in the contract or by subsequent agreement between the parties. However, this is governed by the law of contract – the customers' entitlement derives from the law of contract not the law of trusts. In relation to the law of trusts, the authority of *Re Goldcorp Exchange* remains good law – a trust cannot be created from unascertained goods, and customers, whatever the position in contact law, will have no entitlement *under the law of trusts* to delivery of goods they have ordered if those goods have not been separated from the larger bulk.

ACTIVITY

A declares that £100,000 of the £1 million she owns is to be held on trust for the benefit of B. Assuming that the declaration of trust is validly made, do you consider it likely that the courts will uphold this trust on the basis of certainty of subject matter?

Consider in particular the following:

- Does the trust suffer from the same problems as Goldcorp where there were fewer assets than there were claimants?
- Does the trust suffer from the problem that others have competing claims to the same fund?
- Could a court identify the subject matter of the trust with certainty, and administer the trust in the event of A's death or incapacity?

In all of the above cases on certainty of subject matter, a particular difficulty was that the company was insolvent. Accordingly, finding that a trust had been created in favour of customers would have been problematic because customers would have been preferential creditors, and in cases such as *Goldcorp* and *Farepak*, the claims of the beneficiaries exceeded the company's remaining assets. Accordingly, in cases where the trustee was not insolvent, the courts have been more willing to acknowledge the existence of the trust even in cases where the trust property has not been separated from the larger bulk of the trustee's assets. One such example is the case of *Hunter v Moss* [1994] 2 All ER 215, the judgment in which was interpreted and applied in *Re Harvard Securities* [1997] 2 BCLC 369.

EXTRACT

Hunter v Moss [1994] 2 All ER 215

Case facts

The defendant owned 950 shares in a company. The claimant argued that a clause in his employment contract allowed him to be given 50 shares in the company. The defendant refused to transfer the shares. Accordingly, the question to be considered by the court was whether the defendant had declared himself to be a trustee of the shares for the benefit of the claimant. The factual issue to be decided at first instance was whether the defendant had declared himself to be a trustee for the benefit of the claimant. The trial judge heard evidence

[7] (1979 c.54).

on this point and concluded that a declaration of trust had been validly made. When the matter came to appeal, the emphasis was on a second line of argument, namely that the subject matter of the trust had not been adequately identified – which of the defendant's 950 shares were to be the subject matter of the trust?

Dillon LJ

I pass then to the second point of uncertainty. It is well established that for the creation of a trust there must be the three certainties referred to by Lord Langdale in his judgment in *Knight v Knight* (1840) 3 Beav 148, 49 ER 68. One of those is, of course, that there must be certainty of subject matter. All these shares were identical in one class: 5% was 50 shares and Mr Moss held personally more than 50 shares. It is well known that a trust of personalty can be created orally . . . In the present case there was no question of an imperfect transfer. What is relied on is an oral declaration of trust. Again, it would not be good enough for a settlor to say, 'I declare that I hold fifty of my shares on trust for B', without indicating the company he had in mind of the various companies in which he held shares. There would be no sufficient certainty as to the subject matter of the trust. But here the discussion is solely about the shares of one class in the one company.

It is plain that a bequest by Mr Moss to Mr Hunter of 50 of his ordinary shares in MEL would be a valid bequest on Mr Moss's death which his executors or administrators would be bound to carry into effect. Mr Hartman sought to dispute that and to say that if, for instance, a shareholder had 200 ordinary shares in ICI and he wanted to give them to A, B, C and D equally he could do it by giving 200 shares to A, B, C and D as tenants in common, but he could not validly do it by giving 50 shares to A, 50 shares to B, 50 shares to C and 50 shares to D because he has not indicated which of the identical shares A is to have and which B is to have. I do not accept that. That such a testamentary bequest is valid, appears sufficiently from the cases of *Re Clifford, Mallam v McFie* [1912] 1 Ch 29 and *Re Cheadle, Bishop v Holt* [1900] 2 Ch 620. It seems to me, again, that if a person holds, say, 200 ordinary shares in ICI and he executes a transfer of 50 ordinary shares in ICI either to an individual donee or to trustees, and hands over the certificate for his 200 shares and the transfer to the transferees or to brokers to give effect to the transfer, there is a valid gift to the individual or trustees/transferees of the 50 shares without any further identification of their numbers. It would be a completed gift without waiting for registration of the transfer. (See *Re Rose (decd), Rose v IRC* [1952] 1 All ER 1217, [1952] Ch 499.) In the ordinary way a new certificate would be issued for the 50 shares to the transferee and the transferor would receive a balance certificate in respect of the rest of his holding. I see no uncertainty at all in those circumstances.

Mr Hartman, however, relied on two authorities in particular. One is a decision of Oliver J in the case of *Re London Wine Co (Shippers) Ltd* [1986] PCC 121 which was decided in 1975 . . . It seems to me that that case is a long way from the present. It is concerned with the appropriation of chattels and when the property in chattels passes. We are concerned with a declaration of trust, accepting that the legal title remained in Mr Moss and was not intended, at the time the trust was declared, to pass immediately to Mr Hunter. Mr Moss was to retain the shares as trustee for Mr Hunter.

Mr Hartman also referred to *Mac-Jordan Construction Ltd v Brookmount Erostin Ltd* [1992] BCLC 350, a decision of this court. The position there was that Mac-Jordan were sub-contractors for Brookmount as main contractors. There was retention money kept back by Brookmount which, on the documents, was to be held on a trust for the sub-contractors, but it had not been set aside as a separate fund when a receiver was appointed by the main contractor's (Brookmount's) bank. It was, consequently, held that Mac-Jordan were not entitled to payment in full of the retention moneys in priority to the receiver and the secured creditor. It was

common ground in that case that, prior to the appointment of the receivers, there were no identifiable assets of Brookmount impressed with the trust applicable to the retention fund. At best, there was merely a general bank account.

In reliance on that case Mr Hartman submits that no fiduciary relationship can attach to an unappropriated portion of a mixed fund. The only remedy is that of a floating charge. He refers to a passage in the judgment of Lord Greene MR in *Re Diplock's Estate, Diplock v Wintle* [1948] 2 All ER 318 at 346, [1948] Ch 465 at 519 where he said:

> 'The narrowness of the limits within which the common law operated may be linked with the limited nature of the remedies available to it . . . In particular, the device of a declaration of charge was unknown to the common law and it was the availability of that device which enabled equity to give effect to its wider conception of equitable rights.'

So Mr Hartman submits that the most that Mr Hunter could claim is to have an equitable charge on a blended fund . . . As I see it, however, we are not concerned in this case with a mere equitable charge over a mixed fund. Just as a person can give, by will, a specified number of his shares of a certain class in a certain company, so equally, in my judgment, he can declare himself trustee of 50 of his ordinary shares in MEL, or whatever the company may be, and that is effective to give a beneficial proprietary interest to the beneficiary under the trust. No question of a blended fund thereafter arises and we are not in the field of equitable charge.

Outcome

There was a valid trust in this case, and although precisely which 50 shares the claimant was to receive had not been identified, this was not a problem in a situation where the shares were all of equal value and were shares in the same company.

Hunter v Moss was then applied in *Re Harvard Securities* [1997] 2 BCLC 369, a case whose facts were broadly similar, namely a purported trust of shares forming part of a larger shareholding.

EXTRACT

Re Harvard Securities [1997] 2 BCLC 369

Neuberger J

On behalf of the liquidator, Mr Halpern, to whose argument I am much indebted, suggests that I should hold that the former clients of Harvard have no beneficial interest in the shares in English law, in the light of the decision and reasoning in *Re Wait, Re London Wine Co (Shippers) Ltd* and *Goldcorp*. So far as *Hunter* is concerned, he submits that I should either refuse to follow it or distinguish it.

Should I refuse to follow *Hunter*? In Underhill and Hayton *Law Relating to Trusts and Trustee* (15th edn, 1995) there is strong adverse criticism of the decision and reasoning in *Hunter*. It is said that Dillon LJ's reliance on the analogy of testamentary dispositions was inappropriate, because –

> 'On death a testator is totally divested of all his legal and beneficial title in all his assets in favour of his executor who becomes subject to equitable obligations to effect the testator's wishes so far as practicable . . . In his lifetime a settlor is only divested in his benefit or entitlement to his assets where one knows to which assets such divestments relates.'

In addition, as Mr Halpern points out, the reliance by Dillon LJ on the decision in *Re Rose* appears to overlook the fact that, in the relevant document, Mr Rose had specifically identified the shares which were intended to be the subject matter of the gift. Underhill and Hayton conclude their discussion as follows (at p 61):

> 'In view of the weak reasoning in *Hunter v Moss* and of the ringing endorsement in *Re London Wine Co (Shippers) Ltd* by the Privy Council in *Re Goldcorp Exchange Ltd* . . . it is respectfully submitted that *Hunter v Moss* should not be followed: there is no sound reasoning for distinguishing trusts of goods from trusts of intangibles.'

I see the force of these points. However, the decision in *Hunter* is binding on me, unless I am satisfied that it is *per incuriam* or that it has been overruled by a subsequent decision.

As to *Hunter* being *per incuriam*, Mr Halpern argues that it is inconsistent with the reasoning in *Re London Wine Co (Shippers) Ltd* and *Re Wait*. *Re London Wine Co (Shippers) Ltd* is a decision of a lower court, and in any event it was expressly considered and distinguished by the Court of Appeal in *Hunter*. On the other hand, *Re Wait* was also a decision of the Court of Appeal, and was not expressly referred to, let alone distinguished, by the Court of Appeal in *Hunter*. None the less, I do not think that it is properly open to me to hold that the decisions in *Re Wait* and *Hunter* are inconsistent and that I can choose between them or to conclude that, had the Court of Appeal in *Hunter* properly considered the decision in *Re Wait*, they would have reached a different conclusion. First, it is clear that the decision in *Re Wait* was cited to the Court of Appeal in *Hunter*: I must therefore presume that it was considered by them. Second, in view of the way in which Dillon LJ distinguished *Re London Wine Co (Shippers) Ltd*, it seems to me that he was impliedly distinguishing, or would have distinguished, *Re Wait* in the same way.

Equally, I do not consider that I can hold that *Hunter* is not binding on the basis that it has been effectively overruled by *Goldcorp*. First, it appears to me that while the decision in *Hunter* is undoubtedly binding on me in principle, the decision in *Goldcorp*, being that of the Privy Council and not of the House of Lords, is not binding on me, and would not have been binding on the Court of Appeal in *Hunter*. Second, I refer again to the way in which Dillon LJ distinguished *Re London Wine Co (Shippers) Ltd*: he said it was 'concerned with the appropriation of chattels and when the property in chattels passes', whereas in *Hunter* the Court of Appeal was concerned with shares and a declaration of trust. In my judgment, therefore, the ground upon which the Court of Appeal in *Hunter* distinguished *Re London Wine Co (Shippers) Ltd* is substantially the same ground upon which *Goldcorp* can be distinguished from *Hunter*.

Mr Halpern's alternative argument was that *Hunter* could be properly distinguished from *Re Wait, Re London Wine Co (Shippers) Ltd* and *Goldcorp* on a ground on which the present case could be properly distinguished from *Hunter*, namely that *Hunter* was concerned with an express declaration of trust, whereas the other cases (including the present one) are not. While it is true that this is a point mentioned by Dillon LJ when distinguishing *Re London Wine Co (Shippers) Ltd* (see [1994] 3 All ER 215 at 221, [1994] 1 WLR 452 at 458) I have come to the conclusion that it is not a proper ground for distinguishing *Hunter* from *Re Wait, Re London Wine Co (Shippers) Ltd* and, indeed, *Goldcorp* and the present case. First, it is clear from the reasoning in *Re Wait* and *Re London Wine Co (Shippers) Ltd* that this is not a valid ground for distinction. The point is well illustrated by Oliver J's inability to see how 'a farmer who declares himself to be trustee of two sheep (without identifying them) can be said to have created a perfect and complete trust of whatever rights he may confer by such declaration as a matter of contract' and from his disagreement with Sir John Romilly. Second, it appears to me that the suggested ground for distinguishing *Hunter* runs into difficulties in the light of the passage I have quoted from the judgment of Dillon LJ in that case ([1994] 3 All ER 215 at 220–221, [1994]

1 WLR 452 at 458): as part of the reasoning for rejecting the defendant's argument, he said in terms that the execution of a document, by way of gift, of some of the proposed donors shares (with no identification as to precisely which shares) would none the less be sufficient to create an enforceable trust. Third, in my view the suggested distinction between *Hunter*, on the one hand, and *Re Wait and Re London Wine Co (Shippers) Ltd* (and indeed *Goldcorp*) on the other hand is not logically defensible, a view clearly consistent with the general thrust of the observations to which I have referred in Underhill and Hayton, and in Meagher Gummow & Lehane, referred to below.

Furthermore, in *Hunter* itself, the judge did not decide that an express declaration of trust, in terms, was made. He merely concluded that 'the sense of what [the defendant] then said was that he would henceforth hold the shares on such a trust'. (Indeed in the present case, I have already quoted from correspondence from Harvard to its clients in which Harvard described the holding of Australian and US shares, sold to the relevant client, as being held 'on your behalf' and 'being your shares'.)

While I am not particularly convinced by the distinction, it appears to me that a more satisfactory way of distinguishing *Hunter* from the other cases is that it was concerned with shares, and not with chattels. First, that is a ground which is consistent with Dillon LJ's reliance on *Re Rose* (a case concerned with shares) and his ground for distinguishing *Re London Wine Co (Shippers) Ltd* (and, by implication, *Re Wait*) which, it will be remembered, he described as being 'concerned with the appropriation of chattels and when property in chattels passes'. Second, it is on this basis that the editors of Underhill and Hayton believe that *Hunter* is explained (although they regard it on an unsatisfactory basis). Third, the observations of Atkin LJ in *Re Wait* [1927] 1 Ch 606 at 630, [1926] All ER Rep 433 at 443 referring to the 'ordinary operations of buying and selling goods' could be said to provide a policy ground for there being one rule for chattels and another for shares.

Fourth, as the editors of Meagher Gummow & Lehane *Equity Doctrines & Remedies* (3rd edn) paras 679–682 point out, the need for appropriation before any equitable interest can exist in relation to chattels can be contrasted with the absence of any such need before there can be an effective equitable assignment of an unascertained part of a whole debt or fund. This distinction is described by the editors as 'very difficult to see'; none the less, they accept that, despite the criticism to which cases such as *Re Wait* have been subjected, it is unlikely that they will be overruled. The editors conclude:

'What must be appreciated, despite what has sometimes been said in reliance on the judgment of Atkin LJ . . . is the narrow scope of the principle for which those cases stand: it applies only to contracts for the sale of an unascertained part of a mass of goods. So limited, the principle may still be regarded as anomalous but, perhaps, commercially convenient: see *Re Wait* [1927] 1 Ch 606 at 636, 639, 640 per Atkin LJ.'

The description of the sub-contracted grain in *Re Wait*, the client's wine in *Re London Wine Co (Shippers) Ltd*, and the customer's bullion in *Goldcorp* as 'an unascertained part of a mass of goods' is quite apt. It would not, however, be a sensible description of the 50 shares in Hunter or, indeed, the shares in the present case. Mr Halpern pointed out that it is not really possible to identify, whether physically or by words, a proportion of a debt, whereas it is possible to identify chattels (by labelling or segregation) or shares (by reference to their number); he also pointed out that part of a debt or fund is fungible with the balance. For those two reasons, he submitted that the inconsistency suggested in Meagher Gummow & Lehane is not valid. There is obvious force in that point, but, in the end, it seems to me that, given that the distinction exists between an assignment of part of a holding of chattels and an assignment of part of a debt or fund, the effect of the decision in *Hunter* is that, in this context, shares fall to be treated in this context in the same way as a debt or fund rather than chattels.

In all the circumstances, therefore, it seems to me that the correct way for me, at first instance, to explain the difference between the result in *Hunter*, and that in *Re Wait, Re London Wine Co (Shippers) Ltd* and *Goldcorp*, is on the ground that Hunter was concerned with shares, as opposed to chattels.

To my mind, the provisions of cl 5 and the correspondence and other documentation to which I have referred show that, as between Harvard and its former clients, a particular number of unidentified shares of a particular class in a particular company were being treated as the beneficial property of the client. Had the correspondence and internal records of Harvard gone one stage further, and identified the share numbers the subject of this arrangement, Mr Halpern accepts (quite rightly in my judgment) that the beneficial interest in the relevant shares would have been vested in the client. The only reason for contending that this is not the case is that the precise shares were not identified. In the light of the decision and reasoning in Hunter, and the above discussion, I do not consider that it is open to me to hold that that aspect prevents Harvard's former clients having a beneficial interest in the shares, so far as English law is concerned.

At the time, many critics considered that *Hunter v Moss* and *Re Harvard Securities* were either incorrect,[8] or that they should be distinguished because an alternative outcome in *Hunter v Moss* would have allowed an employer to perpetrate a breach of contract. It was argued, as Eden explains in the extract provided below, that segregation is necessary, and that no distinction ought to be drawn between tangible and intangible goods.

EXTRACT

Eden, P. 'Beneficial ownership of shares: the implications of *Re Harvard Securities*' (2000) 16(5) *Insolvency Law and Practice* 175

In *Re Harvard Securities*, Neuberger J quoted the relevant passages from in *Re London Wine (Shippers) Ltd* and *Re Goldcorp Exchange Ltd* and then turned to the final authority on equitable assignment, *Hunter v Moss*. The facts of *Hunter v Moss* were that the defendant was the registered holder of 950 shares in a company with an issued share capital of 1,000 shares. In the course of conversation, the defendant agreed that he would hold 5 per cent of the issued shares (i.e. 50 shares) in trust for the plaintiff. Both at first instance and on appeal it was held that the failure to segregate the 50 shares did not render the trust void for uncertainty of subject-matter. The academic response to the Court of Appeal's decision in *Hunter v Moss* has been largely, but not universally, hostile. Much of the criticism of *Hunter v Moss* has sought to argue that the decision cannot be reconciled with the Privy Council's decision in *Re Goldcorp Exchange Ltd*.

In *Re Harvard Securities*, counsel for the liquidator submitted that, in the light of *Re Wait, Re London Wine (Shippers) Ltd* and *Re Goldcorp Exchange Ltd*, Neuberger J should either refuse to follow *Hunter v Moss* or distinguish it. Neuberger J quoted the strong adverse criticism of the decision and reasoning in *Hunter v Moss* contained in Underhill and Hayton: *Law Relating to Trusts and Trustees* Professor Hayton criticises the Court of Appeal's decision in *Hunter v Moss* on two grounds. Firstly, on the ground that Dillon LJ's judgment overlooks the crucial difference

[8] See for example the Australian case of *White v Shortall* [2006] NSWSC 1379.

between inter vivos and testamentary dispositions and, secondly, on the ground that there is no sound reason for distinguishing between trusts of goods and trusts of intangibles.

Professor Hayton's first criticism has been echoed by Sarah Worthington on the grounds that, if a donor intends to make a gift of specifically identified legal property, the decision in *Re Rose* is authority for the proposition that equity will only view the donee as obtaining equitable ownership once the donor has done everything in his or her power to transfer title in the property to the donee. In Worthington's view, this means that equity will never assist with the gift of part of an identified bulk unless the donor, either personally or via an agent, has physically segregated the portion to be given away. Although gifts of shares are not the norm in commercial transactions, given the practical difficulties involved in physically segregating intangible property in a bulk (such as shares), and the re-affirmation of the principle that equity operates on the conscience of the owner of the legal interest in *Westdeutsche Landesbank Girozentrale v Islington London Borough Council*, it is submitted that subsequent cases may well take the same pragmatic view to the perfect gift rule as Dillon LJ in *Hunter v Moss*. There is no need for appropriation for the equitable assignment of an unascertained part of a debt or fund and, in *Re Harvard Securities*, Neuberger J stated that the effect of the decision in *Hunter v Moss* was that, in this context, shares fall to be treated in the same way as a debt or a fund rather than chattels.

Professor Hayton's second criticism of the Court of Appeal's decision in *Hunter v Moss* is that there is no sound reason for distinguishing between trusts of goods and trusts of intangibles. It is submitted with respect that, in his original casenote, Professor Hayton rather overstated the support for this proposition contained in an article written by Professor Sir Goode in 1987. Professor Sir Goode has written subsequently that he regards the Court of Appeal's decision in *Hunter v Moss* as correct.

At the heart of Professor Hayton's second criticism is the proposition that the principle in *Re Wait* is of general application. The difficulties with this proposition are twofold. First, in *Re Wait* Atkin LJ was at pains to emphasise that his decision was based on his view the effect of the provisions of the Sale of Goods Act, an Act which does not apply to gifts or choses in action. Second, both Lord Harworth MR and Atkin LJ were explicit about their desire to reach a decision that would accord with the need of commercial practice even if this meant restricting the principles of equity to 'their own sphere'. This interpretation of the judgment of Atkin LJ in *Re Wait* was specifically endorsed by Neuberger J in *Re Harvard Securities*. Given the rapprochement between the rules of equity and commercial law and the fact that the decision in *Re Wait* no longer accords with the needs of modern commercial practice in relation to bulk shipments of commodities, there appears to be no sound basis for arguing that *Re Wait* is authority for a general principle that applies to trusts of goods governed by the Sale of Goods Act 1979 (prior to the coming into force of the Sale of Goods (Amendment) Act 1995) and trusts of intangibles not governed by the provisions of the Sale of Goods Act . . .

In 1987, Professor Sir Roy Goode concluded his much quoted article on 'Ownership and Obligation in Commercial Transactions' with the statement that, while for the most part the concepts of legal and equitable ownership work well enough to do justice, the concept of ownership expressed in the cases up to that date was too narrow in insisting on specific identification of fungible goods forming part of a bulk, or of securities forming part of a fund, when the smooth working of the market required fungibility.

The Court of Appeal's decision in *Hunter v Moss*, as applied in *Re Harvard Securities* and *Re CA Pacific Finance Ltd* [[2000] 1 BCLC 494], is a fair and sensible solution to the problem of beneficial ownership of shares, particularly in the light of the increasing dematerialisation and immobilisation of securities, and, notwithstanding the academic criticism of the decision, it should continue to be followed in subsequent cases.

What Eden demonstrates here is that despite the initial hostility, the absence of a need to segregate shares from a larger bulk does appear to be justified, especially in light of the judgment in the Hong Kong case of *Re CA Pacific Finance Ltd* [2000] 1 BCLC 494 where it is explained that shares are much more easily separated than tangible goods.

EXTRACT

Re CA Pacific Finance Ltd [2000] 1 BCLC 494

Case facts

This case concerned two companies – CA Pacific Securities Ltd and CA Pacific Finance Ltd. Both these companies were part of a larger company called the CA Pacific Group. CA Pacific Group decided to wind up CA Pacific Finance Ltd because it had failed to repay a loan issued to it. The following day CA Pacific Securities was also wound up. The issue for the court was whether CA Pacific Securities Ltd's clients had any proprietary interest in the securities they had instructed CA Pacific Securities to buy when the share certificates were in a central pool and had not been earmarked as being for particular customers. Having established that the securities broker was acting as the agent of his client, and therefore having a fiduciary duty is to account for the principal's property, thus establishing a trustee-beneficiary relationship, Yuen J went on to consider whether the subject matter of the trust was sufficiently certain.

Yuen J

Certainty of subject matter

Mr Hildyard's further submission was that there could be no trust because immobilised shares with unnumbered share certificates in CCASS [the Hong Kong Stock Exchange's Central Clearing and Settlement System] cannot be the subject matter of a trust for want of certainty.

It is the case that after a purchase of securities through CCASS, scrip deposited with Hong Kong Securities Co Ltd do not physically change hands unless and until a purchasing client requires delivery of the scrip. There is no earmarking of the scrip, by number or otherwise . . . However, it does not follow that there is no certainty of subject matter. There are strict recording requirements at each level to show what securities are held for whom. All transactions for sale and purchase through CCASS are recorded in detail . . . Thus in this system, each purchaser of securities would have his quantity of scrip available with HKSCC's depositary, even though he would not be able to point to any particular tranche of shares as his own. I would add that it is not suggested that there has been any shortfall of scrip in CCASS.

Consideration of the nature of the subject matter

Mr Hildyard submitted that there was no certainty of subject matter of the trust, because there has been no appropriation of securities to each client. He relied heavily on the decisions in *Re Wait* [1927] 1 Ch 606, [1926] All ER Rep 433, *Re London Wine Co (Shippers) Ltd* [1986] PCC 121 and *Re Goldcorp Exchange Ltd*.

It is correct of course that certainty of subject matter is essential to the creation of a trust. But in considering whether there is sufficient certainty of subject matter, one must have regard to what the subject matter is.

For certain types of goods, such as wheat in *Re Wait*, wine in *Re London Wine Co (Shippers) Ltd* and bullion in *Re Goldcorp Exchange Ltd*, segregation or appropriation is the means of identifying the goods which have been made the subject matter of the trust. But in my view, it does not follow that segregation or appropriation is necessary for all things.

What is required is not segregation for the sake of segregation. What is required is certainty of the property over which it is intended there should be a disposal of the beneficial interest. What is necessary is the means of identifying or distinguishing the subject matter of the trust.

How one identifies or distinguishes things must depend on the nature of the thing. For tangible goods, that is done by segregating one parcel from the rest of a bulk. Each parcel has its own characteristics and would be subject to its own risks (eg corking of the wine in *Re London Wine Co (Shippers) Ltd*). But for intangible things such as fungible shares ranking pari passu – which enjoy exactly the same rights, which have no separate characteristics and no inherent risks (as HKSCC takes responsibility for replacing any defective securities in CCASS: CCASS, r 815) – it is difficult to see why segregation is necessary, so long as one knows the quantity of the shares which are to form the subject matter of the trust.

Nature of tangible goods

In *Re Wait, London Wine* and *Goldcorp*, the persons who were asserting a trust were purchasers who had failed to obtain the passing of legal title to goods, due to a failure to appropriate goods to the contracts of sale. In *Re Wait*, there was a sale of goods ex-bulk, but even that feature was not present in *Goldcorp*, where it was held that there was only a sale of unascertained generic goods.

Even if there had been actual goods which could have been appropriated, however, a trust could not be validly created unless the beneficial interest has been properly 'hived off' from the legal and beneficial interests owned by the vendors before the transaction. It was in this 'hiving off' process that difficulties were faced by the purchasers in those cases.

I should add that I note that in *London Wine*, Oliver J dealt with an argument that the trust was of a proportion of a homogeneous mass and rejected it due to the absence of clear words, especially when the numerical whole was not known. I would however agree with respect with Rimer J's view in *Hunter v Moss* [1993] 1 WLR 934 that it is not really possible to have a homogeneous mass of tangible assets, because tangible assets are inherently physically separate, and so distinguishable one from the other.

Nature of shares

In our case, however, the subject matter is shares. It is well established that shares are simply bundles of intangible rights against the company which had issued them. Share certificates are not valuable property in themselves – they are just evidence of the true property, which are the proportionate interests of the shareholders in the ownership of the company.

One *pari passu* share is exactly the same as another. This was recognised in *Solloway v McLaughlin* [1937] 4 All ER 328, [1938] AC 247, where the Privy Council held that the broker need only have retained an equivalent quantity of stock in its possession, and in the more recent cases of *Hunter v Moss* [1993] 1 WLR 934 (in the Chancery Division), [1994] 3 All ER 215, [1994] 1 WLR 452 (in the Court of Appeal) and *Re Harvard Securities Ltd* (in liq), *Holland v Newbury* [1997] 2 BCLC 369. Therefore, each share certificate with HKSCC's depositary evidences the same bundle of rights, and each bundle of rights can satisfy the client's proprietary interest as any other.

Client's beneficial interest at inception of trade through CCASS

Mr Hildyard further submitted that in an insolvency situation, a court would not assist a party who had a contractual right to have a trust fund set up, but who had failed to enforce that right prior to insolvency (*Mac-Jordan Construction Ltd v Brookmount Erostin Ltd (in receivership)* [1992] BCLC 350). So if CAPS' clients are to enjoy a proprietary interest in the securities, they would have had to acquire it before CAPS collapsed.

There is no difficulty here, because the broker (CAPS) never had the beneficial interest in the securities. The beneficial interest starts and remains with the client, because the securities had been acquired by the broker as his agent with money provided by him. There is no need to set up a trust fund with money belonging originally to another (as in the *Mac-Jordan Construction Ltd* case), or to 'hive off' the beneficial interest from legal and beneficial interests originally vested in the same person (as in the failed sale of goods cases).

In *Goldcorp*, Lord Mustill remarked ([1994] 2 All ER 806 at 824, [1995] 1 AC 74 at 100–101):

> 'The facts of the present case are, however, inconsistent with any such trust. This is not a situation where the customer engaged the company as agent to purchase bullion on his or her behalf, with immediate payment to put the agent in funds, delivery being postponed to suit the customer's convenience. The agreement was for a sale by the company to, and not the purchase by the company for, the customer.'

What Lord Mustill said was not the situation in *Goldcorp* is exactly the situation in our case.

Since *Goldcorp* dealt with unascertained generic tangibles, and *Hunter v Moss* dealt with intangible shares, it is clear that different considerations applied to the question of certainty of subject matter. It is therefore not surprising that leave to appeal to the House of Lords was refused in *Hunter v Moss* [1994] 3 All ER 215, [1994] 1 WLR 452 after the report of the Privy Council decision in *Goldcorp* (see *Re Harvard Securities Ltd (in liq), Holland v Newbury* [1997] 2 BCLC 369 at 381).

Conclusion

In conclusion, therefore, I find that neither the client agreement nor the non-segregation of securities in CCASS effects any change. The fungibility of the securities in CCASS does not pose any challenge to the position that the proprietary interest in the securities belongs to the client; on the contrary, the fungible nature of such securities permits the client to retain a proprietary interest in them without the need for appropriation. Such a finding is also consistent with the trust of money referred to in s 84 Securities Ordinance.

ACTIVITY

Consider the following questions. There is no 'correct' answer. However you will need to give some consideration as to how you would convince someone that your point of view on these questions is correct. Why does an argument convince you/not convince you?

1. Do you consider the distinction between the need to separate chattels from a larger bulk and the absence of a need to separate shares from a larger bulk is justified or not?
2. What do you consider to be the primary justification for the court's refusal to acknowledge that there was a trust in existence in cases such as *Goldcorp* and *Re London Wine*? Do you agree with the view that these cases were decided on the basis that there were insufficient funds to satisfy all the claims or are there other justifications that are more convincing?
3. Do you agree with Neuberger J that *Hunter v Moss* was decided primarily on the basis of a distinction between chattels and shares or do you consider that the argument of Dillon LJ comparing the trust to a will to be more convincing?

In his article entitled 'Reconceptualising the express trust' (see below), Parkinson argues that the restrictions cause the law to be more problematic than is necessary. He argues therefore that some types of trust property need not be separated from the larger bulk provided that it is defined with sufficient certainty and clarity.

EXTRACT

Parkinson, P. (2002) 'Reconstituting the express trust' 61 *Cambridge Law Journal* 657

III. The requirement of trust property

While it is true that the trust obligation must attach to identifiable property, the distinction between ownership and obligation is not as clear cut. I will argue that there is strictly no need for there to be identifiable trust property. It is enough that there is identifiable subject-matter within which the trust property may be located, by computation or otherwise. Furthermore, the trust estate does not need to be segregated from the personal patrimony of the trustee. I will also show that it is not necessary that the amount of property to be held on trust within a larger mass be specifically quantified. It is enough that the trust obligation is defined with sufficient clarity that a court can decide, in the event of dispute, how much money or property is held on trust or should be devoted to the purposes of the trust. That is, the requirement of certainty of subject-matter is, on closer analysis, a requirement of certainty of obligation . . .

A. The need for identification of the trust property

The terms 'trust property' and 'the subject-matter of the trust' are often used interchangeably, but as Scott has argued, the two concepts need to be distinguished. The subject-matter of the trust is the property of which all or just a portion may be subject to a trust. The latter is the trust property. Thus where X's life estate in land is held on trust for Y and Z, the land is the subject-matter of the trust and the life estate is the trust property. The distinction may seem technical and in most cases unimportant, but the distinction is of considerable importance in analysing the nature of the res requirement.

The Texas case of *Wilkerson v. McClary* [647 SW 2d 79 (Texas Ct App 1983)] demonstrates the importance of being able to identify the subject-matter. A settlor declared an *inter vivos* trust of 'a checking/savings account located at Home Savings and Loan Association' on trust. At the date of her death, she had four such accounts, and she had not indicated to the bank that any of these accounts were held as a trustee. Since the court had no way of knowing which of the four accounts was meant to be held on trust, the trust failed for uncertainty.

A trust may also fail because the trust property is not sufficiently defined within the subject-matter. Many of the well-known examples where trusts have failed for uncertainty fall into this category. For example, in *Palmer* v. *Simmonds* the testator left 'the bulk of my estate' on trust. The estate was the subject-matter, but the trust property was not identified with sufficient certainty . . .

Thus for any trust to exist, the subject-matter must be identified specifically. The requirement that there must be identifiable subject-matter within which the trust property is located distinguishes the equitable obligation which arises under a trust from other forms of obligation which need not be satisfied out of any specific property. If I declare myself a trustee of $5,000 for my child, it is not enough that I have general assets in excess of that value. Nor is it sufficient that I happen to have $6,000 in a bank account. For I have not identified any specific money as

being held on trust, either by segregation or otherwise, and nor have I identified specific subject-matter as being the locus of the trust property.

What then, are the requirements for sufficient identification of the trust property? Is it sufficient that a trustee declares a specified quantity of property within a larger fungible mass to be held on trust, without segregating that property, or must there be segregation in order to satisfy the requirements of certainty? . . .

B. Is there a need for segregation?

Is it necessary that there be segregation out of the assets of the trustee in order for a trust to be created? It is important here to distinguish between failure of segregation which is relevant to the question of intention and failure of segregation which may lead to failure of the trust for uncertainty of subject-matter.

The segregation issue frequently arises in cases of insolvency where it is claimed that certain property which apparently forms part of the general assets of an individual or company, was in fact impressed with a trust so as to take it out of the pool of assets available to the general creditors. Typically in such cases, there is a lack of clarity about the exact form of legal arrangement which was intended by the parties . . .

In such cases, the purported trust will not fail for uncertainty of subject-matter per se. Rather, the lack of segregation helps to determine that a debtor-creditor relationship was intended rather than one of trusteeship . . . The position will however be different where the intention to create a trust is clear. Where there is an identifiable fund which is subject to trust obligations, there will be a trust even though the fund is not held separately from the general assets of the trustee . . . Prima facie trust moneys should be paid into a separate account, but if it is agreed between trustee and beneficiary that they may be paid into a general account, the trustee would be required to retain sufficient moneys in that account to cover his trust obligations . . . I see no reason why effect should not be given to such an agreement or why it should result in a destruction of the trust . . .

Of course segregation is desirable, even if it is not necessary for the validity of a trust. One consequence of a failure to segregate is that the trust moneys may be dissipated. A lack of segregation can also create difficulties in tracing the trust property in the mixed fund. This was the basis of a number of objections raised to the decision in *Hunter v. Moss*. Critics argued that without segregation, it is difficult to know which shares are owned by the beneficiary. What if some, but not all, of the shares are sold? In such circumstances, does the trustee sell the trust property or his or her own property? What if, after declaring the trust, the trustee transfers the shares by way of gift to two other persons? Against whom will the beneficiary be able to exercise the right of tracing? These are difficulties, and they point to the desirability of having a segregated fund as an administrative requirement. However, there are no great legal difficulties involved in answering these questions if the fund is not segregated. As Jill Martin has pointed out, these difficulties are readily resolved by application of tracing rules concerning the mixing of trust funds with the trustee's own property. Certainly, the High Court of Australia found no difficulty in tracing shares into a larger mass even when the shares subject to tracing were not specifically identifiable.

C. Principles for identifying the trust property within an undifferentiated mass

What then are the requirements for the existence of trust property within a larger mass? It is submitted that the requirement of certainty can be achieved in one of three ways. Firstly, where property within a mass is identified by subtraction or by identifying a proportion of the mass; secondly, where the trustee subsequently identifies the trust property by segregating that property out of the mass; thirdly, where property is impressed with a trust before it is mingled with a larger mass.

(i) Property identified by subtraction or proportion

The English authorities suggest two ways in which the trust property may be sufficiently identified within the subject-matter of the trust.

The first is by subtraction. This is illustrated by Megarry J.'s decision in *Re Kayford*. Megarry J. held that payment into a separate bank account was useful as an indication of the company's intention to create a trust but it was not essential. The money held on trust could be sufficiently identified within the bank account by subtracting the amount of money which was in the account before the funds which were subject to a trust obligation were added.

The second, for which *Hunter v. Moss* is the authority, is by identifying the proportion of the mass held on trust. In this case, the declaration that 5% of the share capital of a private company was held on trust was sufficient to make it certain. This equated to 50 shares.

How can this decision be reconciled with the cases concerned with the identification of chattels held in bulk, where no such trust was found? In discussing this issue, it is important to distinguish between trusts in relation to goods in bulk, and contracts for the purchase of goods stored in bulk. As Sarah Worthington has demonstrated, the legal principles are not the same. The creation of property rights in equity pursuant to a contract for purchase depends on the requirement of specific performance. No such requirement arises where a trustee declares himself or herself a trustee of an amount which is located within a larger mass. The only question is whether the trust property has been identified with sufficient specificity.

The case which has been most discussed on goods stored in bulk is *Re London Wine Company (Shippers) Ltd*. which was endorsed by the Privy Council in *Re Goldcorp Exchange Ltd. (in rec.)* . . . *Hunter* v. *Moss* has been distinguished from *London Wine* on the basis that shares are intangible and fungible assets. Bottles of wine are not fungibles. A bottle might, for example be corked or badly stored, and in the case of wine of a scarce vintage, it might be irreplaceable if broken or otherwise rendered imperfect. Each bottle of wine is a distinct entity. Therefore owning 20 bottles out of 100 in stock is not in itself a sufficient identification of the property.

However, a further ground for distinction is that in these cases also, there was a fluctuating mass, and so one could not identify the assets owned in equity by each customer by reference to proportions. In *London Wine*, for example, the mass of which the purchased bottles usually represented a portion was subject to fluctuation and change. It so happened that in some cases a customer or customers between them had purchased the entire company stock; but there was no reason why the company should not at some later stage purchase more wine of that vintage and also no reason why it should not satisfy the customers' contracts out of newly purchased stock. It was thus not possible to say either that certain bottles or cases were held on trust or that a particular customer owned a definite percentage of the company's entire stock. This might not matter perhaps if the bottles stored increased in number but it could matter very much if the numbers decreased. This is illustrated by *Re Goldcorp*. In this case, the levels of bullion held by the company varied from time to time. Thus not only was it impossible to say what bullion each customer owned but it was also impossible to know what fraction of the total bullion each customer owned especially since the amount purchased exceeded the gold bullion which was stored.

(ii) By subsequent identification or desegregation

Secondly, there may be certainty of subject-matter by subsequent identification or segregation. This emerges from the judgment of Scalia J. of the Supreme Court of the United States in *Begier v. Internal Revenue Service* [496 US 53 (1990)] . . . While the majority reached this view on the basis of an interpretation of the legislative history, Scalia J. delivered a concurring judgment which relied on fundamental trust principles. He held that Congress could not deem a trust to exist where the basic requirements for a trust were not met. In deciding whether a trust existed on general principles, he distinguished between collected and withheld taxes. He stated that

where the taxes subject to the trust-fund provision are collected taxes the statute plainly identified the res-the collected taxes. Where, however, the taxes are withheld, the statute provided no clear identification. He concurred in the result because by paying the amount due out of general funds, the company had thereby designated that amount of money to be the trust property to which the statute refers. He interpreted the intent of the statute to be that the trust property should be deemed to have existed from the time of the initial collection or withholding, and consequently it was not a voidable preference as a result of having been paid within 90 days of the bankruptcy.

Scalia J.'s reasoning is consistent with that of the Court of Appeal in *Re Diplock* [[1948] Ch 465], which indicated that property impressed with a trust, once mixed with the general assets of a trustee, may become unmixed if the trustee withdraws the property from the mixed fund for the purposes of identification as trust property.

(iii) Where property is impressed with a trust before mingling

There is sufficient certainty of trust property also if property is impressed with a trust before it forms part of a larger mass, for then the principles of tracing apply to its location . . .

D. Certainty of trust property and certainty of obligation

To summarise the argument so far then, cases of the highest authority stand for the proposition that an express trust may exist even though there is no corresponding equitable estate held individually or collectively by a group of beneficiaries. Furthermore, it is not necessary for the validity of the trust that there is a 'legal estate' which is held separate and apart from the property of the trustee. It is sufficient that there is certainty of subject-matter within which the trust property can be identified or from which it is subsequently segregated.

One might further observe that there are some kinds of trust where the requirement of certainty of trust property is best characterised as a requirement of certainty of obligation. An example of this phenomenon is where a person holds property subject to an obligation to make provision for someone else out of that property. So for example, a husband may leave property to his wife with an obligation to provide for the maintenance and education of the children. Such obligations are variously categorised as trusts, charges or other forms of obligation. Sometimes, the purpose is regarded simply as a motive in conferring unconditional beneficial interests. Invariably, where the obligation is characterised as a trust, the extent of the property which is to be used for the benefit of the beneficiaries is uncertain. In these circumstances, if uncertainty is fatal to the validity of a trust it will usually be because the uncertainty concerning the extent of the property to be devoted to the stipulated purpose provides an indication that the testator did not intend a trust at all . . .

It follows from analysis of the requirements of certainty in relation to trust property that at the heart of the doctrine, it is the obligation which must be described with sufficient certainty, not the trust property. It is enough that the subject-matter of the trust can be ascertained, that is the pool of property from which the trust fund must come, and that the trust obligation with respect to that property is defined with sufficient clarity. This is the thread which runs through all the cases concerning uncertainty of subject-matter which have been discussed . . . as in *Hunter v. Moss*, a trustee declares that 50 shares out of a parcel of 950 shares are held on trust, that is a sufficient definition of his obligation with respect to the parcel of 950 shares. If the trustee indicates that all the money in a particular bank account, less £50, is held on trust, that is a sufficient definition of the obligation. And if there is an obligation to collect sales taxes as a trustee or to account as a trustee for the proceeds of sale of airline tickets, then it is sufficiently certain if the obligation is defined clearly enough to provide a proper basis for computation of how much money which has been collected from customers is impressed with a trust.

Property is capable of forming the subject matter of a trust

In addition to the trust property being adequately identified, it is also necessary for it to be capable of forming the subject matter of a trust. A settlor cannot create a trust out of that which he or she does not own. Accordingly, it is not possible to create a trust from property one anticipates receiving in the future. Accordingly, in *Glegg v Bromley* [1912] 3 KB 474, the purported trust of damages that the putative settlor hoped to gain in successful litigation could not validly form the subject matter of the trust, and, by the same token in *Re Ellenborough* [1903] 1 Ch 697, the settlor's trust of an inheritance that she expected to acquire on the death of her brother and sister could not form a trust property. In both cases, the settlors had no guarantee that the subject matter of the trust would ever belong to them – the legal action might fail, and settlor's siblings might alter their wills. Accordingly, in both cases, there could be no trust because the settlor had no entitlement to the trust property.

Other examples of future property that cannot form the subject matter of a valid trust includes royalties from completed works (*Re Trytel, ex p Trustee of Property of Bankrupt v Performing Right Society Ltd and Soundtrac Film Co Ltd* [1952] 2 TLR 32), copyright in songs that have not yet been written (*Performing Right Society Ltd v London Theatre of Varieties Ltd* [1924] AC 1, HL) and the proceeds of sale of property that has not yet been sold (*Re Cook's Settlement Trusts, Royal Exchange Assurance v Cook* [1965] Ch 902). Even if the trust property does later materialise, the beneficiary cannot be entitled to it, because the trust never came into existence.

One exception to this is that if the settlor gives consideration for the property he or she expects to receive and then creates a trust, the beneficiaries will in this case acquire an entitlement – not from the date of creation of the trust, but on the date when the trust property is received by the settlor. This is justified on the basis that the giving of consideration by the settlor creates in him or her an actionable expectation of an entitlement to the trust property. The settlor's conscience is then bound, and therefore when he or she receives the trust property, it is not then possible for the settlor to retain it for him- or herself. Nevertheless, the settlor does not have to be the owner in law of the property; a trust may validly be created from an equitable interest. Therefore, where the settlor is him- or herself the beneficiary under a trust, a trust may be created from that beneficial interest.

The certainty of objects

The third of the three certainties is the need for a certainty of objects – namely certainty regarding the identity of the beneficiary or beneficiaries who will benefit from the trust. There is one exception to this principle, namely that trusts for the benefit of a charitable purpose do not need to identify the beneficiaries, or indeed any particular charitable purpose listed in s.3(1) of the Charities Act 2011.[9] Therefore although a charitable trust could be created for the benefit of a specific charity (Save the Children for example), a valid charitable trust could be created simply by specifying the charitable purpose that is intended to benefit from the trust (the prevention or relief of poverty for example) or simply by manifesting an intention to benefit charity generally. The leading case both on the need for certainty of objects in relation to private trusts, and the exception to this principle in the subject of charitable trusts, is the case of *Morice v Bishop of Durham* [1803–13] All ER Rep 451.

[9] (2011 c.25).

EXTRACT

Morice v The Bishop of Durham [1803–13] All ER Rep 451

Case facts

By her will the testatrix gave the residue of her estate to the executor of her will and directed that the funds should be given to 'such objects of benevolence and liberality' as the executor considered appropriate.

Sir William Grant MR

The only question is whether the trust upon which the residue of the personal estate is bequeathed be a trust for charitable purposes. That the residue is left on some trust and not for the personal benefit of the bishop is clear from the words of the will, and is admitted by his lordship who expressly disclaims any beneficial interest. That it is a trust, unless it be of a charitable nature, too indefinite to be executed by this court, has not been, and cannot be, denied. There can be no trust over the exercise of which this court will not assume a control, for an uncontrollable power of disposition would be ownership and not trust. If there be a clear trust, but for uncertain objects, the property that is the subject of the trust is undisposed of, and the benefit of such trust must result to those to whom the law gives the ownership in default of disposition by the former owner. But this doctrine does not hold good with regard to trusts for charity. Every other trust must have a definite object. There must be somebody in whose favour the court can decree performance. But. it is now settled upon authority which it is too late to controvert that, where a charitable purpose is expressed, however general, the bequest shall not fail on account of the uncertainty of the object . . . The only question could be whether the execution should be in this court, or by the King's sign manual, but clearly, if it can be brought up to a design of charity, the uncertainty of the particular object will not defeat the general purpose. It is not necessary to make use of the word 'charity,' or to point out some specific object, falling within the range of that word. Any other words enabling the court with a sufficient degree of certainty to collect the intention are equivalent. It is not necessary to name any individual legatee if he is distinctly pointed out in any way, and 'charity' is a legatee favoured more than any other. Therefore, a general description is sufficient.

Outcome

The court concluded that the testatrix had clearly intended to create a trust – there was no intention for the executor to take the residue for himself. The next issue was whether or not it was charitable. If the wording was sufficiently clear to demonstrate that the testatrix had intended the fund to be used for charitable purposes then it would succeed. However, if the trust was not intended to be charitable, then it would fail for uncertainty of objects. Both Sir William Grant MR in the Rolls Court, and Lord Eldon on Appeal to the Lord Chancellor's Court concluded that the trust was not for a charitable purpose.

For the purposes of this section however, what is significant is the words of Sir William Grant MR where he states: '*Every . . . trust must have a definite object. There must be somebody in whose favour the court can decree performance.*' In essence, if the beneficiaries are not defined with sufficient precision, then it is impossible to decide whether the trust fund has been applied in accordance with the settlor's intention. Where the trust is for a named beneficiary or named beneficiaries, there will not usually be any difficulty with certainty of objects. Therefore if a testator, Arthur Brown, writes a will leaving his estate divided equally between his children, Bridget Brown, Christopher Brown and Deborah Brown, the objects of the trust are sufficiently precisely defined.

The need for certainty of objects – fixed trusts and discretionary trusts

However, where the determination of certainty of objects becomes more problematic is where the trust is created for a group of beneficiaries. Trusts of this type take two forms, the first of these is a fixed trust, where the trustees must divide the trust fund equally between all members of the group. The second type of trust is a discretionary trust, where the trustees are given the discretion to select an individual beneficiary or a group of beneficiaries from a larger class. A trust of the latter type may be useful where a settlor wishes to confer the entirety of the trust fund, or the largest portion of the trust fund on the most deserving beneficiary. A discretionary trust may therefore be used to take account of circumstances not yet known, such as which of the settlor's children will end up in the greatest financial need. It may also be useful where a trust is created to confer a prize for educational or sporting achievement for example. In such situations, the trustees are able to select the eligible beneficiary or beneficiaries from a larger pool.

The need for linguistic certainty

Where a group of beneficiaries is identified, either for a fixed trust or a discretionary trust, it will be necessary for the group to be defined with sufficient precision in order for the trustees (and/or the courts) to be able to decide whether a particular individual is or is not within the group. This is known as linguistic certainty, or conceptual certainty, and essentially means that the concept of who the beneficiary is has been defined in a sufficiently precise way.

Accordingly, if a trust is created for one's children, then it will be possible to determine, through the use of birth certificates and other records, whether a person falls within the definition of being a child of the testator. However, other groups may be less capable of precise definition.

A trust for one's friends for example may be void for uncertainty as it will be impossible to decide whether 'friends' was intended to mean one's friends at the time of one's death, or all the friends one has ever had in one's lifetime. Also, different people may have different levels of friendship, ranging from some very close friends, to colleagues, to friends and acquaintances on social networking websites. Accordingly, if a trust fund is to be divided between members of a particular group, the group must be defined sufficiently precisely so that it is clear whether or not a particular person is or is not a member of that group, as Lord Upjohn explains in the case of *Wishaw v Stephens* [1970] AC 508:

> That class must be as defined as the individual; the court cannot guess at it. Suppose the donor directs that a fund be divided equally between 'my old friends,' then unless there is some admissible evidence that the donor has given some special 'dictionary' meaning to that phrase which enables the trustees to identify the class with sufficient certainty, it is plainly bad as being too uncertain. Suppose that there appeared before the trustees (or the court) two or three individuals who plainly satisfied the test of being among 'my old friends,' the trustees could not consistently with the donor's intentions accept them as claiming the whole or any defined part of the fund. They cannot claim the whole fund for they can show no title to it unless they prove they are the only members of the class, which of course they cannot do, and so, too, by parity of reasoning they cannot claim any defined part of the fund and there is no authority in the trustees or the court to make any distribution among a smaller class than that pointed out by the donor. The principle is, in my opinion, that the donor must make

his intentions sufficiently plain as to the objects of his trust and the court cannot give effect to it by misinterpreting his intentions by dividing the fund merely among those present. Secondly, and perhaps it is the more hallowed principle, the Court of Chancery, which acts in default of trustees, must know with sufficient certainty the objects of the beneficence of the donor so as to execute the trust. Then, suppose the donor does not direct an equal division of his property among the class but gives a power of selection to his trustees among the class; exactly the same principles must apply. The trustees have a duty to select the donees of the donor's bounty from among the class designated by the donor; he has not entrusted them with any power to select the donees merely from among known claimants who are within the class, for that is constituting a narrower class and the donor has given them no power to do this.

So if the class is insufficiently defined the donor's intentions must in such cases fail for uncertainty. Perhaps I should mention here that it is clear that the question of certainty must be determined as of the date of the document declaring the donor's intention (in the case of a will, his death). Normally the question of certainty will arise because of the ambiguity of definition of the class by reason of the language employed by the donor, but occasionally owing to some of the curious settlements executed in recent years it may be quite impossible to construct even with all the available evidence anything like a class capable of definition (*In re Sayer* [1957] Ch. 423), though difficulty in doing so will not defeat the donor's intentions (*In re Hain's Settlement* [1961] 1 W.L.R. 440). But I should add this: if the class is sufficiently defined by the donor the fact that it may be difficult to ascertain the whereabouts or continued existence of some of its members at the relevant time matters not.

If the group of beneficiaries is not defined with sufficient precision, the trust will fail because of the linguistic uncertainty with which the objects of the trust are defined.

ACTIVITY

Is it possible to define the following groups with sufficient linguistic certainty?

- Employees
- Family
- Neighbours
- Siblings
- Classmates
- Cousins
- Parents

Fixed trusts

Where the trust fund must be divided equally between the beneficiaries under what is known as a fixed trust, not only is it necessary to define the group of beneficiaries sufficiently precisely, it will also be necessary to decide whether all the members of the group have been identified. This is what Lord Upjohn goes on to explain in the quotation from *Wishaw v Stevens*, above. He explains that where a trust is created for the benefit of one's

friends, some people could prove that they are definitely within the group of intended beneficiaries. However, this would not mean that the objects of the trust have been defined with sufficient certainty because it would not permit the trustees to ensure that they have identified all the beneficiaries.

Accordingly, under a fixed trust, the objects of the trust will only be certain if the group is defined with sufficient linguistic certainty that it is possible to define whether or not an individual is part of the group, and whether it is possible to determine when all the beneficiaries within the group have been identified. This is called the fixed list test and derives from the case of *Inland Revenue Commissioners v Broadway Cottages Trust* [1955] Ch 20.

EXTRACT

Inland Revenue Commissioners v Broadway Cottages Trust [1955] Ch 20

Case facts

The settlor created a trust and directed that the income from the trust fund should be used to benefit all or any of those falling within the classes of beneficiaries listed in a schedule to the deed. It was not possible to list all the possible beneficiaries to this trust, but it was clear that two specific beneficiaries were within one of the named classes. Accordingly, they argued that the trust was sufficiently precisely defined, and should not fail for uncertainty of objects.

Jenkins LJ

It must, we think, follow from the appellants' concession to the effect that the class of 'beneficiaries' is incapable of ascertainment, and we understand them not to dispute, that the trust of the capital of the settled fund for all the beneficiaries living or existing at the termination of the appointed period, and if more than one in equal shares, must be void for uncertainty, inasmuch as there can be no division in equal shares amongst a class of persons unless all the members of the class are known . . . The trust of income during the appointed period as actually declared by clause 8 is not in those terms, but is a trust to apply such income for the benefit of all or such one or more of the settlor's wife and the beneficiaries as the trustees in their discretion think fit, and the question in the case is, in effect, whether the power of selection thus conferred on the trustees saves the trust from uncertainty having regard to the concession made by the Crown to the effect that, while the trustees can never discover all the beneficiaries, they can always tell whether a given individual is or is not one of the beneficiaries, and can therefore, with certainty, confine any payments they think fit to make to persons qualified as beneficiaries according to the terms of the schedule.

In approaching this question both sides accept the principle stated by Lord Eldon in *Morice v. Bishop of Durham*, where he said: 'As it is a maxim, that the execution of a trust shall be under the control of the court, it must be of such a nature, that it can be under that control; so that the administration of it can be reviewed by the court; or, if the trustee dies, the court itself can execute the trust: a trust therefore, which, in case of maladministration could be reformed; and a due administration directed; and then, unless the subject and the objects can be ascertained, upon principles, familiar in other cases, it must be decided, that the court can neither reform maladministration, nor direct a due administration.' The principle can be concisely stated by saying that, in order to be valid, a trust must be one which the court can control and execute. Mr. Pennycuick, for the appellants, contends that it is satisfied by the trust now before the court. Mr. Cross, for the Crown, contends that it is not. . . . The arguments in support of the Crown's claim that the trust is invalid are to this effect: First, the court could not compel the

trustees to make any distribution of income under clause 8 of the settlement, for that clause purports to confer on the trustees an uncontrolled discretion to determine the person or persons falling within the class of beneficiaries to whom any distribution is to be made, and the shares in which those persons, if more than one, are to take; and it would be beyond the power of the court to make or enforce an order upon the trustees to exercise that discretion. Nor could the court itself exercise the trustees' discretion in the event of their failing or refusing to do so, for the discretion is conferred on, and exercisable by, the trustees alone. Secondly, if the class of beneficiaries was an ascertainable class, it would or might be possible to imply a trust in default of distribution by the trustees for all the members of the class in equal shares, and that would be a trust which the court could control and execute. But, as the class is unascertainable, no such trust can be implied. Thirdly, again, if the class was ascertainable, it would or might be possible for all the beneficiaries to join in a demand for the execution of the trust by the distribution of the whole income amongst themselves in equal shares, and proper for the court to recognize and enforce that demand as made by all the persons beneficially interested in the subject-matter of the trust. But, as the class is unascertainable, no such demand is possible. Short of the whole class, no beneficiary or collection of beneficiaries can claim execution of the trust, for the trustees are under no duty to any particular beneficiary or beneficiaries, short of the whole class, to make any distribution to him or them of the whole or any part of the income; and such duty as the trust purports to impose on them towards the class as a whole is illusory, since the whole class can never be ascertained.

Fourthly, the validity of the trust must be tested by considering its terms and asking oneself whether the court would be able to control and execute the trust if called upon to do so. That question must be answered by reference to what might happen, and not merely by reference to what would be likely to happen. That is to say, the charge of invalidity cannot be met by making the assumption (in itself reasonable enough) that trustees undertaking a trust such as this would, in all probability, carry it out, by distributing the income amongst persons falling within the class of beneficiaries as defined by the settlement. On the contrary, it must be assumed that the trustees for some reason or other might fail or refuse to make any distribution, and see whether the court could execute the trust in that event. Consideration of the case on that assumption shows that the most the court could do would be to remove the inert or recalcitrant trustees and appoint others in their place. That, however, would not be execution of the trust by the court, but a mere substitution for one set of trustees invested with an uncontrollable discretion of another set of trustees similarly invested, who might be equally inert or recalcitrant.

It must be borne in mind that the question of whether the group of beneficiaries may be defined with certainty does not necessarily have to derive from the trust itself. Therefore, the trust may refer to some other document where the members of the group may be defined. Expert opinion could also be sought regarding whether the members of the group are defined with sufficient precision. The authority on this point is the case of *Re Tuck's Settlement Trusts* [1978] Ch 49, where it was held that the Chief Rabbi could provide an expert conclusive opinion as to whether the beneficiaries fulfilled the criteria of the trust which was for the benefit of people of Jewish blood and of the Jewish faith.

Alternatively, the trustees could refer to or collate a list of the beneficiaries themselves. Therefore, if a generous law lecturer were to create a trust of a fund to be divided equally between all the students studying the equity and trusts module at a particular university within a given year, then the university's list of students enrolled on that module would provide a sufficiently precise definition of the group of beneficiaries, and

identify all the members of that group. By the same principle, if the trust was worded so as to confer the benefit to be divided equally between all those equity and trusts students at a particular university within a given year who had attained a first class mark, then the trustees or the university could collate a list of all the beneficiaries.

ACTIVITY

1. Think of five examples of groups of beneficiaries (such as children) where it is possible to decide with certainty whether an individual is within the group or not, and whether it is possible to decide when all the members of the group have been identified.
2. Think of five examples of groups of beneficiaries (such as friends) where it is not possible to decide with certainty whether an individual is within the group or not, or where it is possible to identify some members of the group but it is not possible to decide when all the members of the group have been identified.

If you have difficulty with this exercise, the judgments in the following cases may be of assistance:

- *Re Barlow's Will Trusts* [1979] 1 All ER 296
- *McPhail v Doulton* [1971] AC 424
- *Whishaw v Stephens* [1970] AC 508 at 524
- *In re Gestetner's Settlements* [1953] Ch 672.

Discretionary trusts

Although a fixed trust requires all the beneficiaries within the group to be identified in order that the trustees may divide the trust fund equally between them, this is not required in relation to discretionary trusts. Discretionary trusts may allow the trustees to decide which members of a larger group of potential beneficiaries (known as postulants) should receive the trust fund. Discretionary trusts may allow the trust fund to be given to only one or to a number of selected persons within the larger class. Discretionary trusts may also permit an uneven distribution of the trust fund. Essentially, therefore, some beneficiaries may receive more than others. As with fixed trusts, linguistic certainty is necessary. Accordingly, it is necessary to determine whether the group has been defined sufficiently precisely so that the trustees are able to ascertain whether a beneficiary is or is not within the group.

However, in the case of *McPhail v Doulton* [1971] AC 424, the House of Lords decided that it was not necessary to be able to identify every potential beneficiary. Unlike fixed trusts, the intention here is not to confer a benefit on every beneficiary within the group. Accordingly, it is not necessary to be able to list all the beneficiaries. It is only necessary to be able to decide with certainty whether an individual upon whom the trustees wish to confer a benefit is definitely within the group or is definitely not within the group. Accordingly, the group must be defined sufficiently precisely in order that a judgement may be made upon this issue. However, the beneficiary must also adduce evidence of his or her entitlement. Therefore, where there is a trust for the benefit of the children of mine workers in a particular area, the applicant must be able to prove that his or her parent was a mine worker.

EXTRACT

McPhail v Doulton [1971] AC 424

Case facts

A fund was created for the benefit of the staff of a company and their relatives and dependants. The first matter for the House of Lords to decide was whether the instrument created a trust or a power. A trust confers an obligation upon the trustee. However, a power is merely that, something that the donee of the power can exercise or not. The lower courts favoured the relationship as being a power, because if it were a trust it would fail the test set out in *Inland Revenue Commissioners v Broadway Cottages Trust* in that it was impossible to ascertain who all the potential beneficiaries within the group were. However, the House of Lords was adamant that the compulsory nature of the obligation created a trust, and not a power – the trustees had no discretion as to whether or not they would administer the obligation. Accordingly, the issue to be considered was whether the trust was valid for reasons of certainty of objects.

Lord Wilberforce

This makes it necessary to consider whether, in so doing, the court should proceed on the basis that the relevant test is that laid down in *Inland Revenue Commissioners v. Broadway Cottages Trust* [1955] Ch. 20 or some other test.

That decision gave the authority of the Court of Appeal to the distinction between cases where trustees are given a power of selection and those where they are bound by a trust for selection. In the former case the position, as decided by this House, is that the power is valid if it can be said with certainty whether any given individual is or is not a member of the class and does not fail simply because it is impossible to ascertain every member of the class (*In re Gulbenkian's Settlements* [1970] A.C. 508). But in the latter case it is said to be necessary, for the trust to be valid, that the whole range of objects (I use the language of the Court of Appeal) should be ascertained or capable of ascertainment.

The respondents invited your Lordships to assimilate the validity test for trusts to that which applies to powers. Alternatively they contended that in any event the test laid down in the *Broadway Cottages* case [1955] Ch. 20 was too rigid, and that a trust should be upheld if there is sufficient practical certainty in its definition for it to be carried out, if necessary with the administrative assistance of the court, according to the expressed intention of the settlor. I would agree with this, but this does not dispense from examination of the wider argument. The basis for the *Broadway Cottages* principle is stated to be that a trust cannot be valid unless, if need be, it can be executed by the court, and (though it is not quite clear from the judgment where argument ends and decision begins) that the court can only execute it by ordering an equal distribution in which every beneficiary shares. So it is necessary to examine the authority and reason for this supposed rule as to the execution of trusts by the court.

Assuming, as I am prepared to do for present purposes, that the test of validity is whether the trust can be executed by the court, it does not follow that execution is impossible unless there can be equal division.

As a matter of reason, to hold that a principle of equal division applies to trusts such as the present is certainly paradoxical. Equal division is surely the last thing the settlor ever intended: equal division among all may, probably would, produce a result beneficial to none. Why suppose that the court would lend itself to a whimsical execution? And as regards authority, I do not find that the nature of the trust, and of the court's powers over trusts, calls for any such rigid rule. Equal division may be sensible and has been decreed, in cases of family trusts, for a

limited class, here there is life in the maxim 'equality is equity,' but the cases provide numerous examples where this has not been so, and a different type of execution has been ordered, appropriate to the circumstances . . .

So I come to *Inland Revenue Commissioners v. Broadway Cottages Trust* [1955] Ch. 20. This was certainly a case of trust, and it proceeded on the basis of an admission, in the words of the judgment, 'that the class of "beneficiaries" is incapable of ascertainment.' In addition to the discretionary trust of income, there was a trust of capital for all the beneficiaries living or existing at the terminal date. This necessarily involved equal division and it seems to have been accepted that it was void for uncertainty since there cannot be equal division among a class unless all the members of the class are known. The Court of Appeal applied this proposition to the discretionary trust of income, on the basis that execution by the court was only possible on the same basis of equal division. They rejected the argument that the trust could be executed by changing the trusteeship, and found the relations cases of no assistance as being in a class by themselves. The court could not create an arbitrarily restricted trust to take effect in default of distribution by the trustees. Finally they rejected the submission that the trust could take effect as a power: a valid power could not be spelt out of an invalid trust.

My Lords, it will have become apparent that there is much in this which I find out of line with principle and authority but before I come to a conclusion on it, I must examine the decision of this House in *In re Gulbenkian's Settlements* [1970] A.C. 508 on which the appellants placed much reliance as amounting to an endorsement of the *Broadway Cottages* case [1955] Ch. 20. But is this really so? That case was concerned with a power of appointment coupled with a gift over in default of appointment. The possible objects of the power were numerous and were defined in such wide terms that it could certainly be said that the class was unascertainable. The decision of this House was that the power was valid if it could be said with certainty whether any given individual was or was not a member of the class, and did not fail simply because it was impossible to ascertain every member of the class. In so deciding, their Lordships rejected an alternative submission, to which countenance had been given in the Court of Appeal, that it was enough that one person should certainly be within the class. So, as a matter of decision, the question now before us did not arise or nearly arise. However, the opinions given were relied on, and strongly, as amounting to an endorsement of the 'complete ascertainment' test as laid down in the *Broadway Cottages* case.

My Lords, I comment on this submission with diffidence, because three of those who were party to the decision are present here today, and will express their own views. But with their assistance, and with respect for their views, I must endeavour to appraise the appellants' argument. My noble and learned friend Lord Reid's opinion can hardly be read as an endorsement of the *Broadway Cottages* case. It is really the opinion of my noble and learned friend Lord Upjohn which has to be considered. Undoubtedly the main part of that opinion, as one would expect, was concerned to deal with the clause in question, which required careful construction, and with the law as to powers of appointment among a numerous and widely defined class. But having dealt with these matters the opinion continues with some general observations. I have considered these with great care and interest: I have also had the advantage of considering a detailed report of the argument of counsel on both sides who were eminent in this field. I do not find that it was contended on either side that the *Broadway Cottages Trust* case was open to criticism – neither had any need to do so. The only direct reliance upon it appears to have been to the extent of the fifth proposition appearing on p. 31 of the report, which was relevant as referring to powers, but does not touch this case. It is consequently not surprising that my noble and learned friend Lord Upjohn nowhere expresses his approval of this decision and indeed only cites it, in the earlier portion, in so far as it supports a proposition as to powers. Whatever dicta therefore the opinion was found to

contain, I could not, in a case where a direct and fully argued attack has been made on the *Broadway Cottages* case, regard them as an endorsement of it and I am sure that my noble and learned friend, had he been present here, would have regarded the case as at any rate open to review. In fact I doubt very much whether anything his Lordship said was really directed to the present problem. I read his remarks as dealing with the suggestion that trust powers ought to be entirely assimilated to conditions precedent and powers collateral. The key passage is where he says [1970] A.C. 508, 525:

> 'Again the basic difference between a mere power and a trust power is that in the first case trustees owe no duty to exercise it and the relevant fund or income falls to be dealt with in accordance with the trusts in default of its exercise, whereas in the second case the trustees must exercise the power and in default the court will. It is briefly summarised in *Halsbury's Laws of England,* 3rd ed., Vol. 30 (1959), p. 241, para. 445:
>
> > ". . . the court will not exercise or compel trustees to exercise a purely discretionary power given to them; but the court will restrain the trustees from exercising the power improperly, and, if it is coupled with a duty, the court can compel the trustees to perform their duty."
>
> 'It is a matter of construction whether the power is a mere power or a trust power and the use of inappropriate language is not decisive (*Wilson v. Turner* (1883) 22 Ch.D. 521, 525).
>
> 'So, with all respect to the contrary view, I cannot myself see how, consistently with principle, it is possible to apply to the execution of a trust power the principles applicable to the permissible exercise by the donees (even if trustees) of mere powers; that would defeat the intention of donors completely.
>
> 'But with respect to mere powers, while the court cannot compel the trustees to exercise their powers, yet those entitled to the fund in default must clearly be entitled to restrain the trustees from exercising it save among those within the power. So the trustees or the court must be able to say with certainty who is within and who is without the power. It is for this reason that I find myself unable to accept the broader proposition advanced by Lord Denning M.R. and Winn L.J., mentioned earlier, and agree with the proposition as enunciated in *In re Gestetner Settlement* [1953] Ch. 672 and the later cases.'

The reference to 'defeating the intention of donors completely' shows that what he is concerned with is to point to the contrast between powers and trusts which lies in the facultative nature of the one and the mandatory nature of the other, the conclusion being the rejection of the 'broader' proposition as to powers accepted by two members of the Court of Appeal. With this in mind it becomes clear that the sentence so much relied on by the appellants will not sustain the weight they put on it. This is:

> 'The trustees have a duty to select the donees of the donor's bounty from among the class designated by the donor; he has not entrusted them with any power to select the donees merely from among known claimants who are within the class, for that is constituting a narrower class and the donor has given them no power to do this' ([1970] A.C. 508, 524).

What this does say, and I respectfully agree, is that, in the case of a trust, the trustees must select from the class. What it does not say, as I read it, or imply, is that in order to carry out their duty of selection they must have before them, or be able to get, a complete list of all possible objects.

So I think that we are free to review the *Broadway Cottages* case [1955] Ch. 20. The conclusion which I would reach, implicit in the previous discussion, is that the wide distinction between the validity test for powers and that for trust powers is unfortunate and wrong, that the rule recently fastened upon the courts by *Inland Revenue Commissioners v. Broadway Cottages Trust* ought to be discarded, and that the test for the validity of trust powers ought to be similar to

that accepted by this House in *In re Gulbenkian's Settlements* [1970] A.C. 508 for powers, namely, that the trust is valid if it can be said with certainty that any given individual is or is not a member of the class . . .

Two final points: first, as to the question of certainty. I desire to emphasise the distinction clearly made and explained by Lord Upjohn ([1970] A.C. 508, 524) between linguistic or semantic uncertainty which, if unresolved by the court, renders the gift void, and the difficulty of ascertaining the existence or whereabouts of members of the class, a matter with which the court can appropriately deal on an application for directions. There may be a third case where the meaning of the words used is clear but the definition of beneficiaries is so hopelessly wide as not to form 'anything like a class' so that the trust is administratively unworkable or in Lord Eldon's words one that cannot be executed (*Morice* v. *Bishop of Durham*, 10 Ves.Jr. 522, 527). I hesitate to give examples for they may prejudice future cases, but perhaps 'all the residents of Greater London' will serve. I do not think that a discretionary trust for 'relatives' even of a living person falls within this category.

Outcome

Accordingly, the House of Lords acknowledged that a trust had been created, and concluded that it did not fail for uncertainty.

Ambiguity has arisen however since this case was decided, when in *Baden's Deed Trust (No 2)* [1973] Ch 9, the Court of Appeal concluded that evidential uncertainty, in other words the fact that an individual applicant could not prove their entitlement, should not be fatal to the validity of the trust. Accordingly, it was considered that as long as those who wished to be considered as beneficiaries could be identified with sufficient precision, it did not matter that there were others who could not prove that they fitted within the class of beneficiaries or not. The trust is concerned with a fund for the benefit of the relatives of a company's staff. Clearly close relatives (parents, children, siblings) could prove their entitlement through the use of birth and marriage certificates and other documents. Non-relatives could be discounted entirely. But, it was conceded that remoter relatives might fall within the class of beneficiaries, but that the twenty-fifth cousin would not be able to prove their status as a relative. However, the majority within the Court of Appeal concluded that this should not be detrimental to the validity of the trust.

EXTRACT

Re Baden's Deed Trust (No 2) [1973] Ch 9

Case facts

Once *McPhail v Doulton* had been decided as creating a discretionary trust in favour of the beneficiaries, litigation then recommenced on the basis that the trust was void for uncertainty, as relatives and dependants could not be defined with sufficient certainty. In the High Court, Brightman J concluded that dependants could be easily proved and that 'relatives' was sufficiently certain linguistically if it was defined as descendants from a common ancestor.

Sachs LJ

It is submitted on behalf of the executors that each of the words 'relatives' and 'dependants' imports such an uncertainty that the trusts as a whole are void.

The test to be applied to each of these words is: 'can it be said with certainty that any given individual is or is not a member of the class?' per Lord Wilberforce [1971] A.C. 424, 450, 454 and 456, words which reflect those of Lord Reid and Lord Upjohn in *In re Gulbenkian's Settlements* [1970] A.C. 508, 518, 521 and 525. Being in general agreement, as already indicated, with everything that Brightman J. has said as regards the two relevant words, it is sufficient first to make some observations as to the approach to be adopted to the questions raised before us and then in the light of those observations to deal comparatively compactly with the effect of the use of the two relevant words.

It is first to be noted that the deed must be looked at through the eyes of a businessman seeking to advance the welfare of the employees of his firm and those so connected with the employees that a benevolent employer would wish to help them. He would not necessarily be looking at the words he uses with the same eyes as those of a man making a will. Accordingly, whether a court is considering the concept implicit in relevant words, or whether it is exercising the function of a court of construction, it should adopt that same practical and common-sense approach which was enjoined by Upjohn J. in *In re Sayer* [1957] Ch. 423, 436, and by Lord Wilberforce in the *Baden* case [1971] A.C. 424, 452, and which would be used by an employer setting up such a fund.

The next point as regards approach that requires consideration is the contention, strongly pressed by Mr. Vinelott, that the court must always be able to say whether any given postulant is not within the relevant class as well as being able to say whether he is within it. In construing the words already cited from the speech of Lord Wilberforce in the *Baden* case (as well as those of Lord Reid and Lord Upjohn in the Gulbenkian case), it is essential to bear in mind the difference between conceptual uncertainty and evidential difficulties. That distinction is explicitly referred to by Lord Wilberforce in *In re Baden's Deed Trusts* [1971] A.C. 424, 457 when he said:

> '. . . as to the question of certainty. I desire to emphasise the distinction clearly made and explained by Lord Upjohn [1970] A.C. 508, 524 between linguistic or semantic uncertainty which, if unresolved by the court, renders the gift void, and the difficulty of ascertaining the existence or whereabouts of members of the class, a matter with which the court can appropriately deal on an application for directions.'

As Mr. Vinelott himself rightly observed, 'the court is never defeated by evidential uncertainty,' and it is in my judgment clear that it is conceptual certainty to which reference was made when the 'is or is not a member of the class' test was enunciated. (Conceptual uncertainty was in the course of argument conveniently exemplified, rightly or wrongly matters not, by the phrase 'someone under a moral obligation' and contrasted with the certainty of the words 'first cousins.') Once the class of persons to be benefited is conceptually certain it then becomes a question of fact to be determined on evidence whether any postulant has on inquiry been proved to be within it: if he is not so proved, then he is not in it. That position remains the same whether the class to be benefited happens to be small (such as 'first cousins') or large (such as 'members of the X Trade Union' or 'those who have served in the Royal Navy'). The suggestion that such trusts could be invalid because it might be impossible to prove of a given individual that he was not in the relevant class is wholly fallacious – and only Mr. Vinelott's persuasiveness has prevented me from saying that the contention is almost unarguable . . .

Turning now to the word 'dependants' – a word used over several generations in comparable trust deeds – I confess that the suggestion that it is uncertain seems no longer arguable. In *Simmons v. White Brothers* [1899] 1 Q.B. 1005, Collins L.J., albeit when considering that word when used in the Workmen's Compensation Act 1897, quoted with approval the following passage from the then current work [Minton-Senhouse and Emery, *Accidents to Workmen* (1898), p. 156] dealing with that subject, at p. 1007:

> 'It would be hopeless to attempt to lay down any rule of guidance, because every case would probably differ in some material circumstance from almost every other. Dependent probably means dependent for the ordinary necessaries of life for a person of that class and position in life. Thus the financial and social position of the recipient of compensation would have to be taken into account. That which would make one person dependent upon another would in another case merely cause the one to receive benefit from the other. Each case must stand on its own merits and be decided as a question of fact. . . .'

It is true that the court was then dealing with a specific Act, but the good sense of the above quotation has, in relation to the meaning of 'dependant,' a general application, and, has frequently been cited with approval. It demonstrates, incidentally, that such difficulties as may arise in determining whether an individual is a dependant are evidential and raise questions of fact and not of law. Indeed the whole stream of authority runs counter to the contentions put forward on behalf of the executors – save only the first-instance decision in *In re Ball, decd.* [1947] Ch. 228, a will case which would probably be decided differently today.

In agreement with the practical approach of Brightman J. [1972] Ch. 607, 625, I consider that the trustees, or if necessary the court, are quite capable of coming to a conclusion in any given case as to whether or not a particular candidate could properly be described as a dependant – a word that, as the judge said, 'conjures up a sufficiently distinct picture.' I agree, too, that any one wholly or partly dependent on the means of another is a "dependant." There is thus no conceptual uncertainty inherent in that word and the executors' contentions as to the effect of its use fail.

As regards 'relatives' Brightman J., after stating, at p. 625, 'It is not in dispute that a person is a relative of an . . . employee . . . , if both trace legal descent from a common ancestor:' a little later said: 'In practice, the use of the expression 'relatives' cannot cause the slightest difficulty.' With that view I agree for the reasons he gave when he correctly set out the evidential position.

As regards the suggested uncertain numerative range of that concept of the word 'relative' (a matter which strictly would only be relevant to the abandoned 'administratively unworkable' point) and also when considering the practical side of the functions of the trustees, it is germane to note that in *In re Scarisbrick* [1951] Ch. 622, Lord Evershed M.R. observed, with regard to a class of 'relations,' at p. 632: 'That class is, in theory, capable of almost infinite expansion, but proof of relationship soon becomes extremely difficult in fact.' That factor automatically narrows the field within which the trustees select. Further, a settlor using the word 'relatives' in the context of this deed (which is not the same context as that of a will) would assume that the trustees would, in the exercise of their discretion, make their selection in a sensible way from the field, however wide. Thus in practice they would presumably select those whom a reasonable and honest employee or ex-employee would introduce as 'relative,' rather than as a 'kinsman' or as a 'distant relative.' Indeed, on a construction summons some such definition might emerge for the word 'relative' – but that is not relevant to the present appeal, as the widest meaning that has been suggested for that word does not, in my judgment, produce uncertainty.

As a footnote to this conclusion it is interesting to observe that no case was cited to us in which a court has actually decided that a trust was invalid on account of the use of that word, whatever may have been said obiter. If this is due to a tendency to construe deeds and wills so as to give effect to them rather than to invalidate trusts, that is an approach which is certainly in accord with modern thought. I would accordingly dismiss this appeal.

Megaw LJ

If this trust were to be held void for uncertainty because of the inclusion of the 'dependants' in clause 9 (a), I think that few trusts would stand. I do not find any greater uncertainty in it than is inherent in, or can by ingenuity be conjured up in relation to, any ordinary, well understood

word. It would be odd indeed, and wholly regrettable, if a word which was regarded as sufficiently certain to be used, without further explanation or definition, for the purposes of an Act of Parliament (see, for example, section 46 (1) (vi) of the Administration of Estates Act 1925) had nevertheless to be condemned by the courts as being so uncertain as to involve the validity of a trust deed.

Then it is said that the deed is invalid because of the inclusion of the word 'relatives.' Brightman J. [1972] Ch. 607, 625, approached that question on the basis that: 'It is not in dispute that a person is a relative of an officer or employee or ex-officer or ex-employee, if both trace legal descent from a common ancestor.' He held that the executors' argument on this issue also failed. I agree, for the reasons given by the judge. But out of deference to the clear and forceful submission addressed to us by Mr. Vinelott for the executors, I shall state in my own words why, in my judgment, that submission is wrong.

First, lest there should be any suggestion that the inclusion of 'relatives' makes this trust so wide as to be administratively unworkable, I would respectfully agree with Lord Wilberforce's words – obiter dicta, it is true – when the present case was earlier considered by the House of Lords [1971] A.C. 424, 457: 'I do not think that a discretionary trust for "relatives" even of a living person falls within this category.' Lord Wilberforce's dictum was, I have no doubt, directed towards the terms of this particular trust deed. I do not think it was intended to be confined, or ought to be confined, to a provision specifying one single living person. It is apt as regards relatives of employees in the plural. Such a trust is not administratively unworkable.

The main argument of Mr. Vinelott was founded upon a strict and literal interpretation of the words in which the decision of the House of Lords in *In re Gulbenkian's Settlements* [1970] A.C. 508 was expressed. That decision laid down the test for the validity of powers of selection. It is relevant for the present case, because in the previous excursion of this case to the House of Lords [1971] A.C. 424 it was held that there is no relevant difference in the test of validity, whether the trustees are given a power of selection or, as was held by their Lordships to be the case in this trust deed, a trust for selection. The test in either case is what may be called the Gulbenkian test. The *Gulbenkian* test, as expressed by Lord Wilberforce at p. 450, and again in almost identical words at p. 454 is this:

> '. . . the power is valid if it can be said with certainty whether any given individual is or is not a member of the class and does not fail simply because it is impossible to ascertain every member of the class.'

The executors' argument concentrates on the words 'or is not' in the first of the two limbs of the sentence quoted above: 'if it can be said with certainty whether any given individual is or is not a member of the class.' It is said that those words have been used deliberately, and have only one possible meaning; and that, however startling or drastic or unsatisfactory the result may be – and Mr. Vinelott does not shrink from saying that the consequence is drastic – this court is bound to give effect to the words used in the House of Lords' definition of the test. It would be quite impracticable for the trustees to ascertain in many cases whether a particular person was not a relative of an employee. The most that could be said is: 'There is no proof that he is a relative.' But there would still be no 'certainty' that such a person was not a relative. Hence, so it is said, the test laid down by the House of Lords is not satisfied, and the trust is void. For it cannot be said with certainty, in relation to any individual, that he is not a relative.

I do not think it was contemplated that the words 'or is not' would produce that result. It would, as I see it, involve an inconsistency with the latter part of the same sentence: 'does not fail simply because it is impossible to ascertain every member of the class.' The executors' contention, in substance and reality, is that it does fail 'simply because it is impossible to ascertain every member of the class.'

The same verbal difficulty, as I see it, emerges also when one considers the words of the suggested test which the House of Lords expressly rejected. That is set out by Lord Wilberforce in a passage immediately following the sentence which I have already quoted. The rejected test was in these terms [1971] A.C. 424, 450: '. . . it is said to be necessary . . . that the whole range of objects . . . should be ascertained or capable of ascertainment.' Since that test was rejected, the resulting affirmative proposition, which by implication must have been accepted by their Lordships, is this: a trust for selection will not fail simply because the whole range of objects cannot be ascertained. In the present case, the trustees could ascertain, by investigation and evidence, many of the objects: as to many other theoretically possible claimants, they could not be certain. Is it to be said that the trust fails because it cannot be said with certainty that such persons are not members of the class? If so, is that not the application of the rejected test: the trust failing because 'the whole range of objects cannot be ascertained'?

In my judgment, much too great emphasis is placed in the executors' argument on the words 'or is not.' To my mind, the test is satisfied if, as regards at least a substantial number of objects, it can be said with certainty that they fall within the trust; even though, as regards a substantial number of other persons, if they ever for some fanciful reason fell to be considered, the answer would have to be, not 'they are outside the trust,' but 'it is not proven whether they are in or out.' What is a 'substantial number' may well be a question of common sense and of degree in relation to the particular trust: particularly where, as here, it would be fantasy, to use a mild word, to suggest that any practical difficulty would arise in the fair, proper and sensible administration of this trust in respect of relatives and dependants.

I do not think that this involves, as Mr. Vinelott suggested, a return by this court to its former view which was rejected by the House of Lords in the Gulbenkian case. If I did so think, I should, however reluctantly, accept Mr. Vinelott's argument and its consequences. But as I read it, the criticism in the House of Lords of the decision of this court in that case related to this court's acceptance of the view that it would be sufficient if it could be shown that one single person fell within the scope of the power or trust. The essence of the decision of the House of Lords in the *Gulbenkian* case, as I see it, is not that it must be possible to show with certainty that any given person is or is not within the trust; but that it is not, or may not be, sufficient to be able to show that one individual person is within it. If it does not mean that, I do not know where the line is supposed to be drawn, having regard to the clarity and emphasis with which the House of Lords has laid down that the trust does not fail because the whole range of objects cannot be ascertained. I would dismiss the appeal.

Stamp LJ

The House of Lords . . . were unanimously of the opinion that the effect of the clause in question was to constitute a mandatory trust for distribution. The House of Lords, declaring to that effect, remitted the case to the Chancery Division for determination whether on this basis clause 9 was valid or void for uncertainty.

Had the House of Lords gone no further than that, the judge of the Chancery Division before whom the matter came, Brightman J., as it turned out to be, would, if – and the 'if' is important – the word relatives 'extends to include all the descendants of a common ancestor, have been constrained by authority to hold that the trust was void for uncertainty. It had been held by this court in *Inland Revenue Commissioners v. Broadway Cottages Trust* [1955] Ch. 20 that a trust for such members of a given class of objects as the trustees shall select is void for uncertainty, unless the whole range of objects eligible for selection is ascertained or capable of ascertainment. Where the trustees had a duty to distribute the whole of the fund or its income, as opposed to a mere power of appointment over it coupled with a trust in default of appointment, it was thought that any of the beneficiaries could compel the execution of that

trust by the court if necessary and that the trust could not be executed by the court except by equal division and accordingly could not be executed unless all the beneficiaries could be ascertained. The law, as it was understood, was fully stated in the speeches of Lord Hodson and Lord Guest when the originating summons came before the House of Lords in the present case ([1971] A.C. 424), and it would be presumptuous of me to add anything to those statements. I may, however, perhaps be permitted to quote from the speech of Lord Upjohn in *In re Gulbenkian's Settlements* [1970] A.C. 508 a passage which was not part of his ratio decidendi and which was quoted or referred to by Lord Hodson, Lord Guest and Lord Wilberforce, in which he said, at p. 524:

> 'The trustees have a duty to select the donees of the donor's bounty from among the class designated by the donor; he has not entrusted them with any power to select the donees merely from among known claimants who are within the class, for that is constituting a narrower class and the donor has given them no power to do this.'

The trust contained in clause 9 (a) of the trust deed here in question is a trust to apply 'the net income of the fund in making at their absolute discretion grants to or for the benefit of any of the officers and employees or ex-officers or ex-employees of the company [viz. Matthew Hall & Co. Ltd.] or to any relatives or dependants of any such persons in such amounts at such times and on such conditions (if any) as they think fit.'

Upon the footing that a reference to the 'relatives' of a given person is prima facie a reference to all who are descended from a common ancestor, it must in my judgment follow that unless a gloss be put upon that word the trust here would if the law laid down in *Inland Revenue Commissioners v. Broadway Cottages Trust* [1955] Ch. 20 was still good law, be void for uncertainty . . .

You may say with certainty that any given individual is or is not an officer, employee, ex-officer or ex-employee. You may say with certainty that a very large number of given individuals are relatives of one of them; but, so the argument runs, you will never be able to say with certainty of many given individuals that they are not . . .

Validity or invalidity is to depend upon whether you can say of any individual – and the accent must be upon that word 'any,' for it is not simply the individual whose claim you are considering who is spoken of – 'is or is not a member of the class,' for only thus can you make a survey of the range of objects or possible beneficiaries.

If the matter rested there, it would in my judgment follow that, treating the word 'relatives' as meaning descendants from a common ancestor, a trust for distribution such as is here in question would not be valid. Any 'survey of the range of the objects or possible beneficiaries' would certainly be incomplete, and I am able to discern no principle upon which such a survey could be conducted or where it should start or finish. The most you could do, so far as regards relatives, would be to find individuals who are clearly members of the class – the test which was accepted in the Court of Appeal, but rejected in the House of Lords, in the *Gulbenkian* case.

The matter does not, however, rest there, and I must return to examine more closely Lord Wilberforce's reasons for rejecting the *Broadway Cottages* test. Lord Wilberforce in his speech [1971] A.C. 424, 451–452 referred to *Kemp v. Kemp* (1801) 5 Ves.Jr. 849, where Sir Richard Arden M.R. had held that the court disclaimed the right to execute a power (i.e. a trust power) and gave the fund equally. It was upon this basis that this court in the Broadway Cottages case held that a discretionary trust is not valid unless all the beneficiaries are ascertainable: for otherwise the court being called upon to execute the trust cannot divide the fund in equal shares. But, as I have already said, accepting that the test of validity is whether the trust can be executed by the court, Lord Wilberforce did not think it followed that execution is impossible

unless there can be equal division. He cited cases where, prior to the time of Sir Richard Arden, a discretionary trust had been executed otherwise than by equal division. *Harding v. Glyn* (1739) 1 Atk. 469, he said, was an early case where the court executed a discretionary trust for 'relations' – and it is a discretionary trust for relations that I am considering – by distributing to the next of kin in equal shares . . . I have referred to this part of Lord Wilberforce's speech because what he said regarding *Harding v. Glyn*, 1 Atk. 469, was, as I read the speech, part of the foundation upon which he built his conclusion, first, that the court can execute a discretionary trust otherwise than by directing an equal division, and secondly, and consequently, that the *ratio decidendi* of the *Broadway Cottages* case was wrong and that that case was wrongly decided. *Harding v. Glyn* accordingly cannot be regarded simply as a case where in default of appointment a gift to the next of kin is to be implied as a matter of construction, but as authority endorsed by the decision of the House of Lords [1971] A.C. 424 that a discretionary trust for 'relations' was a valid trust to be executed by the court by distribution to the next of kin. The class of beneficiaries thus becomes a clearly defined class and there is no difficulty in determining whether a given individual is within it or without it . . . The only other challenge to the validity of the trust is directed against the use of the word 'dependants' which it is said introduces a linguistic or semantic uncertainty. That in the context the word connotes financial dependence I do not doubt, and although in a given case there may be a doubt whether there be a sufficient degree of dependence to satisfy the qualification of being a 'dependant,' that is a question which can be determined by the court and does not introduce linguistic uncertainty . . .

Outcome

Sachs and Megaw LJJ accepted that relatives was a sufficiently certain term, and that it did not matter that not all relatives would be able to prove their entitlement. Stamp LJ disagreed with this point of view, but concluded that if relatives was synonymous with next of kin, then it would be possible to say whether a relative was or was not within the class of beneficiaries. Accordingly, the Appeal was dismissed, and the trustees could distribute the trust fund as they saw fit between the company staff and their relatives and dependants.

The precise law on this point is therefore a matter of debate. The earlier judgment of the House of Lords in *McPhail v Doulton* requires that it is necessary to say with certainty whether **or not** a given postulant is within the class of beneficiaries. However, the later authority of the Court of Appeal's interpretation of *McPhail v Doulton* in *Re Baden's Deed Trust* (an action that arose from the same trust as *McPhail v Doulton*) indicates that it is only necessary to be able to say with certainty whether a given postulant **is** within the class of beneficiaries, and there being no need to have regard to those who cannot prove this matter. The authoritative judgment is that of the House of Lords, although the Court of Appeal judgment is persuasive, but weakened by the fact that the judgment was the verdict of the majority. Much will therefore depend on how future cases decide this issue on similar facts and whether the Court of Appeal or particularly the Supreme Court follows the judgment in *Baden's Deed Trust* or whether it adheres to the judgment of *McPhail v Doulton*.

ACTIVITY

Which of the approaches do you consider to be most satisfactory – the strict *McPhail v Doulton* approach, or the broader approach adopted in *Re Baden*? What are the advantages and the disadvantages of the two approaches?

Administrative unworkability

By way of a postscript to his judgment in *McPhail v Doulton*, Lord Wilberforce commented that a trust would fail because of administrative unworkability:

> Two final points: first, as to the question of certainty. I desire to emphasise the distinction clearly made and explained by Lord Upjohn ([1970] A.C. 508, 524) between linguistic or semantic uncertainty which, if unresolved by the court, renders the gift void, and the difficulty of ascertaining the existence or whereabouts of members of the class, a matter with which the court can appropriately deal on an application for directions. There may be a third case where the meaning of the words used is clear but the definition of beneficiaries is so hopelessly wide as not to form 'anything like a class' so that the trust is administratively unworkable or in Lord Eldon's words one that cannot be executed (*Morice v. Bishop of Durham*, 10 Ves.Jr. 522, 527). I hesitate to give examples for they may prejudice future cases, but perhaps 'all the residents of Greater London' will serve. I do not think that a discretionary trust for 'relatives' even of a living person falls within this category.

In essence, the trust will fail if it is too broad for the trustees to be able to administer. The situation described by Lord Wilberforce illustrates this point admirably. A trust for the benefit of the residents of Greater London would not be workable, certainly as a fixed trust, because it would be impossible to determine who all the beneficiaries were. Even as a discretionary trust, it may be such a complicated trust to administer that the courts would be reluctant to view it as valid. Accordingly in the case of *R v District Auditor No 3 District of West Yorkshire Metropolitan County Council ex parte West Yorkshire Metropolitan County Council* [1986] RVR 24, a trust for the benefit of '*any or all or some of the inhabitants of the County of West Yorkshire*' because although '*the definition, it was said, is straightforward and clear cut. There is no uncertainty as to the concept. If anyone were to come forward and claim to be a beneficiary, it could be said of him at once whether he was within the class or not*', Lloyd LJ argued '*it seems to me, be open to argument what is meant by "an inhabitant" of the county of West Yorkshire*.' He went on to state:

> A trust with as many as 2 1/2 million potential beneficiaries is, in my judgment, quite simply unworkable. The class is far too large. In *In re Gulbenkian's Settlements* [1970] AC 508, [1968] 3 All ER 785 Lord Reid said at page 518: 'It may be that there is a class of case where, although the description of a class of beneficiaries is clear enough, any attempt to apply it to the facts would lead to such administrative difficulties that it would for that reason be held to be invalid.'

Conclusion

In this chapter, the certainties required in order for a valid trust to exist have been outlined, as well as some of the problems that have faced the courts in terms of identifying when these certainties have been manifested. Generally, the three certainties will need to be manifested in relation to each type of trust, whether the trust is an express trust or an implied trust, an *inter vivos* trust or a will trust.

Nevertheless, the three certainties are more readily discerned in relation to some types of trust than others. For example, as shall be demonstrated in Chapter 14, the certainty of intention is less immediately apparent in relation to a constructive trust than in relation to an express trust. This does not mean that the intention does not exist, but the intention is effectively implied on the basis that no other intention can be discerned. In essence the conduct of the defendant is such that a trust is regarded as having been the

defendant's intention (such as where he or she establishes an intention in common with the claimant to share the beneficial ownership of the cohabitational home) or no other intention (such as where a trust fails, and it must therefore have been the settlor's intention that the trust property will revert back to the settlor's estate).

As was touched upon previously, the precision with which the objects of a trust are defined is not needed in relation to a charitable trust – the precise beneficiaries need not be identified. Nevertheless, there must be certainty of the fact that a settlor's objectives are exclusively charitable, and a trust will fail if the charitable objects identified do not confer an exclusively charitable benefit.

Chapter summary

This chapter may be useful for assessments and assignments on:

- The validity requirements of a trust
- The definition of a trust
- The characteristics of a trust (especially compared with other relationships such as contracts, gifts and powers).

Further reading

Case Comment (1993) 'Contract – passing of property – retention of title – goods supplied to insolvent sub contractor' *Construction Law Journal* 337.

Hardcastle, I.M. (1990) 'Administrative unworkability – a reassessment of an abiding problem' *Conveyancer and Property Lawyer* 24.

Jones, A. (1993) 'Contract – passing of property – retention of title – goods supplied to insolvent sub contractor' *Conveyancer and Property Lawyer* 466.

Martin, J. (1996) 'Certainty of subject matter: a defence of *Hunter v. Moss*' *Conveyancer and Property Lawyer* 223.

Maxton, J.K. (1992) 'The nature of a beneficiary's interest pending the administration of an estate' *Conveyancer and Property Lawyer* 92.

Norris, W. (1995) 'Uncertainty and informality: *Hunter v Moss*' *Private Client Business* 43.

Ricketts, C.E.F. (1991) 'Different views on the scope of the Quistclose analysis: English and antipodean insights' *Law Quarterly Review* 608.

Worthington, S. (1999) 'Sorting out ownership interests in a bulk: gifts, sales and trusts' *Journal of Business Law* 1.

9

Formalities

Chapter outline

This chapter will cover:

- Capacity
- Writing
- Formal approval
- The rule against perpetuities, accumulations and the remoteness of vesting.

Introduction

This chapter will consider the formalities required for creating different types of trust. Many trusts may be created without any need to observe any specific formalities. Provided that the trust property is transferred to the trustee(s) and that an intention to confer a benefit on a specific beneficiary is identified, a valid trust may be created. After all, putting a coin into a charity collector's tin is an act of trust creation. Nevertheless, with certain types of trust, further formalities are required.

Capacity

Some types of trust have very limited requirements as to capacity. The aforementioned donation to a charity collector is an act of trust creation, but a child or a person with very limited understanding could create a valid trust in this way. However, more complex trusts have more complex requirements in terms of capacity, especially where the trust concerns valuable trust property. Accordingly, a person under the age of 18 can neither write a will[1] nor create a trust of land.[2] A valid trust will also not be created if the settlor lacks the understanding of what a trust means, or does not understand the implications of disposing of the trust property, or lacks the capacity to understand who the beneficiaries might be. Accordingly, the trust purportedly created in the case of *Re Beaney* [1978] 1 WLR 770 was not valid. Here the settlor had purportedly created a trust of her house in her daughter's favour. She was held to lack the required capacity for creating a valid trust because the house was the only significant asset the testatrix owned, and because, by giving the house to one daughter, she effectively disinherited her other children. Section 3(1) of the Mental Capacity Act 2005[3] gives some general indicators of a lack of capacity, namely that:

> A person is unable to make a decision for himself if he is unable
>
> (a) to understand the information relevant to the decision;
>
> (b) to retain that information;
>
> (c) to use or weigh that information as part of the process of making the decision; or
>
> (d) to communicate his decision (whether by talking, using sign language or any other means).

However, this is a fairly broad test in that understanding is decided according to one's circumstances, and therefore, the fact that someone may need to have the obligation explained in simple terms or through the use of visual aids does not preclude them from having the necessary understanding. Secondly, a person may have the necessary capacity even though they are only able to retain the information for a short period of time. While the ability to use the information requires the settlor to be aware of the likely consequences of making or not making a decision, it does not mean that one should have an oracle-like foresight of every possible outcome of a decision. It is sometimes alleged that a trust created by a person who lacks capacity is void. In reality it is voidable[4] because it is a matter

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[1] Wills Act 1837, s.7.
[2] Law of Property Act 1925, s.1(6).
[3] (2005 c.9.).
[4] *Sutton v Sutton* [2009] EWHC 2576 (Ch).

for the person alleging incapacity to prove it.[5] Once a prima facie case is made out, the settlor will then have to prove that he or she has the requisite capacity – or, if the settlor has died, or has become incapacitated since the making of the trust, it will then be a matter for those alleging that the trust is valid to prove that the settlor had the necessary capacity at the time of making the trust.[6]

Writing

Inter vivos trusts may be created without any written formalities. Thus it is seen in the case of *Paul v Constance* [1977] 1 WLR 527 where a trust was created simply because of the words spoken by the deceased. However, where the trust is complex or valuable in financial terms, the prudent solicitor would advise that the instrument be made in writing. Specific forms of trust however must be in writing. These are trusts of land, wills, and trusts of equitable interests. A person who is a beneficiary under one trust, may him- or herself create a trust out of his or her equitable interest, as this is a valuable asset, and therefore likely to be something that a person may wish to devolve under a trust. However, as shall be shown, such a trust would need to comply with the formality of writing if it is to be valid.

Trusts of land

Section 53(1)(b) of the Law of Property Act 1925 provides that all trusts of land and all dispositions of equitable interests over land must be manifested and proved by writing and signed by the settlor.

EXTRACT

Law of Property Act 1925, s.53(1)(b)

(b) a declaration of trust respecting any land or any interest therein must be manifested and proved by some writing signed by some person who is able to declare such trust or by his will;

This does not require the trust to be made in writing merely that evidence of its having been created is made in writing. This is explained by Judge Launcelot Henderson in the case of *Sleebush v Gordon* [2005] EWHC 3447 (Ch) where he explains the meaning of s.53(1)(b) Law of Property Act 1925:

> I have little hesitation in rejecting this argument. It is true that the only copy of the 1945 Conveyance in evidence seems not to have been signed by Rhys and Charlotte. Seals have been placed to the right of the space left for their signatures, but the space is blank, and there are no details of any attesting witness. The Conveyance was executed in the normal way by the vendor, a Mr George Booth. It follows that there is no declaration of trust signed by Rhys and Charlotte which would satisfy the requirements

[5] *Williams v Williams* [2003] EWHC 742 (Ch) at [44]–[45].
[6] Ibid.

of s 53(1)(b). However, the express declaration in cl 3 of the Conveyance that they were to hold the proceeds of sale in trust for themselves in equal shares as tenants in common remains strong contemporary evidence of their intentions, as it should not have been included unless they had discussed the question with the solicitors who were then acting for them and given instructions accordingly. There could be many reasons why they failed to execute the Conveyance. Possibly it was thought to be an unnecessary formality, once it had been executed by the vendor. Another possibility is that they executed a counterpart which was handed over to the vendor. What seems highly improbable, in the absence of any corroborating evidence, is that they deliberately refused to sign the Conveyance because they were unhappy about taking the Property as beneficial tenants in common. On the contrary, that would have been the natural thing for them to do, since the Claimant's evidence (based on what Rhys told her) is that the deposit of £225 on the purchase price of £900 was provided by Rhys and Charlotte in equal shares, while the balance of £675 was borrowed from the Woolwich Building Society under a mortgage in their joint names. It would be surprising if their intention had been to purchase as beneficial joint tenants, given the difference in their ages and the likelihood that Charlotte would be the first of them to die.

However, an oral declaration of a trust of land is not void, merely difficult to enforce. Accordingly, the trustee of land will not be permitted to keep the trust property for him- or herself, as this would contravene the equitable principle that a statute that is aimed at preventing fraud must not be used as an instrument of fraud. Accordingly, it is likely that where a trust of land has been made orally, the courts will seek to circumvent the impact of s.53(1)(b) either by construing the trust as a constructive trust, or by providing that the doctrine of estoppel prevents the trustee from denying the existence of the trust. Accordingly, in the case of *Rochefoucauld v Bousted* [1898] 1 Ch 550, the lack of writing did not prevent the trust from existing.

EXTRACT

Rochefoucauld v Bousted [1898] 1 Ch 550

Case facts

The defendant bought land as a trustee for the claimant, and then mortgaged this land without the claimant's consent. The issue for the Court of Appeal was whether the trust could be enforced in the absence of writing:

Lindley LJ

We come, therefore, to the conclusion that the plaintiff has proved that the estates in question were conveyed to the defendant on May 27, 1873, upon trust for her, but subject to a charge in his favour in respect of all sums advanced by him in order to obtain the estates from the Dutch company in the first instance, and of all sums advanced by him in order to work them as coffee plantations after he had acquired them.

This conclusion renders it necessary to consider whether the Statute of Frauds affords a defence to the plaintiff's claim. The section relied upon is s. 7, which has been judicially interpreted in *Forster v. Hale* and *Smith v. Matthews*. According to these authorities, it is necessary to prove by some writing or writings signed by the defendant, not only that the conveyance to him was

subject to some trust, but also what that trust was. But it is not necessary that the trust should have been declared by such a writing in the first instance; it is sufficient if the trust can be proved by some writing signed by the defendant, and the date of the writing is immaterial. It is further established by a series of cases, the propriety of which cannot now be questioned, that the Statute of Frauds does not prevent the proof of a fraud; and that it is a fraud on the part of a person to whom land is conveyed as a trustee, and who knows it was so conveyed, to deny the trust and claim the land himself. Consequently, notwithstanding the statute, it is competent for a person claiming land conveyed to another to prove by parol evidence that it was so conveyed upon trust for the claimant, and that the grantee, knowing the facts, is denying the trust and relying upon the form of conveyance and the statute, in order to keep the land himself. This doctrine was not established until some time after the statute was passed. In *Bartlett v. Pickersgill* the trust was proved, and the defendant, who denied it, was tried for perjury and convicted, and yet it was held that the statute prevented the Court from affording relief to the plaintiff. But this case cannot be regarded as law at the present day . . . The defence, based on the Statute of Frauds, is met by the plaintiff in two ways. First, she says that the documents signed by the defendant prove the existence of the trust alleged; secondly, she says that if those documents do not prove what the trust is with sufficient fullness and precision, the case is one of fraud which lets in other evidence, and that with the aid of other evidence the plaintiff's case is established. In our opinion the plaintiff is correct in this contention. We are by no means satisfied that the letters signed by the defendant do not contain enough to satisfy the Statute of Frauds. Whether this is so or not, the other evidence is admissible in order to prevent the statute from being used in order to commit a fraud; and such other evidence proves the plaintiff's case completely.

In order to ensure that the interests of the beneficiary are overreached for the purposes of s.2 of the Law of Property Act 1925 (i.e. the beneficiary's interest is transferred from being an interest in the land, and converted into an interest in the money paid by the buyer to the seller-trustee when the land is sold) when the land is sold, it will be necessary to put a restriction on the proprietorship register on the Land Register preventing the land from being sold unless it is sold by two trustees in accordance with the requirements of s.40 of the Land Registration Act 2002.

Necessarily however, a constructive trust of land will not need to be in writing, as is confirmed in s.53(2) Law of Property Act 1925.

Trusts of equitable interests

Creating a trust out of an equitable interest must be made in writing and signed in accordance with s.53(1)(c) Law of Property Act 1925. It is important to note that s.53(1)(c) applies to all types of property of which one may be the beneficial owner – in addition to being one of the main Acts of Parliament relied upon by students of land law, the Law of Property Act 1925 is also relevant to other types of property.

EXTRACT

Law of Property Act 1925, s.53(1)(c)

(c) a disposition of an equitable interest or trust subsisting at the time of the disposition, must be in writing signed by the person disposing of the same, or by his agent thereunto lawfully authorised in writing or by will.

This is a stricter requirement than is seen in relation to trusts of land, as there is a requirement for the trust to be made in writing. This is discussed by Michael Briggs QC in *Supperstone v Hurst* [2006] 1 FCR 352, where he states:

> The learned registrar held that Mr and Mrs Hurst's statements made for the purposes of his unsuccessful IVA [Individual Voluntary Arrangement] constituted written declarations of trust satisfying s 53(1)(b) of the Law of Property Act 1925, and binding upon Mr and Mrs Hurst as to their beneficial interest in the property. This was not a conclusion which had been contended for by Mr Fisher, and was inconsistent with the parties' common stance that the issue as to the respective size of their beneficial interests should be determined by reference to constructive trust principles. It was a conclusion that the learned registrar reached for the first time, tentatively, at the time of preparing his draft judgment and he maintained it after hearing submissions from the parties on that point following delivery to them of the draft judgment . . . In my judgment neither Mr nor Mrs Hurst's statements in connection with his unsuccessful IVA were declarations of trust in relation to the property. Neither of them purported to create a trust where either no trust or some different trust had existed before. They were merely statements made for the purpose of informing Mr Hurst's creditors as to the nature and extent of his assets and as to his wife's readiness to co-operate in the sale of the property and the realisation of his beneficial interest for the benefit of those creditors.

Therefore, even though the statements made by the Hursts were evidence of the trust, the trust itself (in the form of the Hursts' declarations as to their beneficial interests in their matrimonial home) was not made in writing, as it merely confirmed the earlier position of the parties. Accordingly, we see that s.53(1)(c) imposes stricter formalities on the settlor than s.53(1)(b). Again however, the requirement of writing will be disregarded in cases where it would be inequitable for the settlor to deny that a trust existed, whereupon a resulting or constructive trust will be found.

Why therefore does the law require stricter formalities regarding the trust of an equitable interest than for a trust of land? The answer lies in the fact that with *inter vivos* trusts of land, there will be a transfer of the land to the trustee, or a declaration of trust. Accordingly, there will be an element of conduct that reinforces the fact that a trust has been created, and therefore all that is needed is there to be evidence in writing of the existence of the trust, in order to give credence to the fact that the transfer of the trust property to the trustee was not in the form of a gift. It also ensures that a trust of land cannot be created through what might be termed loose talk – the requirement of written evidence ensures that land (a valuable commodity) is not made the subject of a trust either accidentally, or without giving sufficient thought to the implications that the transaction will have.

However, with a trust of an equitable interest, the trustees will be the legal owners of the property, and therefore the settlor cannot manifest his or her intention to create a trust with the same ease – the settlor cannot transfer the trust property because it is not within his or her control. Also, an oral declaration of trust may not be sufficient to ensure that the trustees of the main trust are sufficiently aware of their obligations. Accordingly, a trust of an equitable interest must be made in writing, rather than merely being evidenced in writing.

Wills

A trust contained in a will must comply with the formalities for creating a valid will trust. These are contained in s.9 Wills Act 1837.

EXTRACT

Wills Act 1837, s.9

Signing and attestation of wills

[No will shall be valid unless-

(a) it is in writing, and signed by the testator, or by some other person in his presence and by his direction; and

(b) it appears that the testator intended by his signature to give effect to the will; and

(c) the signature is made or acknowledged by the testator in the presence of two or more witnesses present at the same time; and

(d) each witness either-

(i) attests and signs the will; or

(ii) acknowledges his signature,

in the presence of the testator (but not necessarily in the presence of any other witness), but no form of attestation shall be necessary.]

Accordingly, a will needs to be made in writing. The reason for this is perhaps obvious. When a will comes into effect, the settlor will have died, and cannot therefore be called upon to explain or to clarify what his or her intentions were. Therefore in order to ensure that the settlor's intentions are recorded, a will must be in writing. In order to write a valid will, the testator must be aged over 18, as is provided by s.7 Wills Act 1837.[7]

Other formalities

Other types of trust property will depend on the fulfilment of other formalities. In *Milroy v Lord* (1862 4 De Gf & J 264) Turner LJ explains that:

> the settlor must have done everything . . . which was necessary to be done in order to transfer the property and render the settlement binding upon him.

Necessarily of course, this will vary depending on the nature of the trust. There will be the necessity of transferring the trust property to the trustees, or making an effective declaration of one's intention to be a trustee. However, what constitutes effective transfer may vary according to the nature of the property transferred. For example, where the trust consists of company shares, then it will be necessary to complete a share transfer form, and the transfer may have to be approved by the company's directors, as is seen in the case of *Re Rose* [1952] Ch 499. Once all the necessary formalities have been complied with the trust will be completely constituted.

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[7] One exception to this is that persons in the armed forces may write a valid will even if they are under the age of 18. There are also exceptions to the requirement of writing in relation to military wills. Further discussion of the law relating to military wills may be found in Halsbury's Laws of England *Wills and Intestacy* (Vol. 102 (2010) 5th ed., paras. 1–564; Vol. 103 (2010) 5th ed., paras. 565–1304) at para. 79.

The rule against perpetuities, accumulations and remoteness of vesting

The rule against perpetuities contains three elements. Firstly, it requires that the beneficiary or beneficiaries under a trust must become the outright owner of the trust property within a specific period. This is known as the rule against remoteness of vesting, although some texts and cases will use the phrase 'the rule against perpetuities' to describe only this specific aspect of the rule. For trusts created after 6 April 2010, the Perpetuities and Accumulations Act 2009[8] specifies this as a fixed period of 125 years from the date upon which the trust comes into effect – either from the date of the creation of the trust in the case of a trust created during the settlor's lifetime, or, in the case of a will, from the date of the settlor's death.

EXTRACT

Perpetuities and Accumulations Act 2009, s.5

5 Perpetuity period

(1) The perpetuity period is 125 years (and no other period).

(2) Subsection (1) applies whether or not the instrument referred to in section 1(2) to (6) specifies a perpetuity period; and a specification of a perpetuity period in that instrument is ineffective.

This simplifies the law considerably, as trusts created between 15 July 1964 and 6 April 2010 will have to be completed within either a fixed period of 80 years or a period of 21 years after the death of a named person.[9] In relation to trusts created before 15 July 1964, where the old common law still applies, the trust must be completed within 21 years of the death of a named person. As such trusts may still be in existence, it will be important for the trusts lawyer to know when the trust was created in order to advise on the date by which it must be completed. For all trusts created after 15 July 1964, including those operating under the Perpetuities and Accumulations Act 2009, a 'wait and see' provision applies. In essence, this means that a trust must be treated as being valid, until such time as it becomes apparent that it is invalid.

[8] (2009 c.18).

[9] Perpetuities and Accumulations Act 1964 (1964 c.55).

EXTRACT

Perpetuities and Accumulations Act 2009, s.7

7 Wait and see rule

(1) Subsection (2) applies if (apart from this section and section 8) an estate or interest would be void on the ground that it might not become vested until too remote a time.

(2) In such a case-

(a) until such time (if any) as it becomes established that the vesting must occur (if at all) after the end of the perpetuity period the estate or interest must be treated as if it were not subject to the rule against perpetuities, and

(b) if it becomes so established, that does not affect the validity of anything previously done (whether by way of advancement, application of intermediate income or otherwise) in relation to the estate or interest.

(3) Subsection (4) applies if (apart from this section) any of the following would be void on the ground that it might be exercised at too remote a time-

(a) a right of re-entry exercisable if a condition subsequent is broken;

(b) an equivalent right exercisable in the case of property other than land if a condition subsequent is broken;

(c) a special power of appointment.

(4) In such a case-

(a) the right or power must be treated as regards any exercise of it within the perpetuity period as if it were not subject to the rule against perpetuities, and

(b) the right or power must be treated as void for remoteness only if and so far as it is not fully exercised within the perpetuity period.

(5) Subsection (6) applies if (apart from this section) a general power of appointment would be void on the ground that it might not become exercisable until too remote a time.

(6) Until such time (if any) as it becomes established that the power will not be exercisable within the perpetuity period, it must be treated as if it were not subject to the rule against perpetuities.

The relevance and application of the rule against perpetuities is more readily explained with reference to concrete examples. Consider for example, a will worded in the following terms. Donna writes a will leaving money to be divided equally between the children of her brothers and sisters, with the issue of such children to take the share their parent would have received if they had not died. Let us say that Donna dies at the age of 20, leaving a brother. At the time of Donna's death, there is no-one who is eligible to inherit, but this does not mean that there can never be anyone who is eligible to inherit. Firstly, it is not known whether Donna's brother will have children, and therefore the trust could exist for many years before it is known to whom the estate should be distributed. Furthermore, it is still possible that Donna's parents would still be young enough to have other children, whose children would be eligible to inherit a portion of Donna's estate. However, although a trust can exist for many years it is undesirable to leave Donna's estate on trust on an indefinite basis – it creates that situation where ownership and control of property is fettered unduly.

Accordingly, the new perpetuity period allows for a period of 125 years from the date of Donna's death to determine who should inherit. It is probable that the trust will be completed within a much shorter period than this in that after Donna's parents die or are deemed too old to have more children (although this is problematic to determine) or medically unable to have children, and Donna's brother dies or becomes too old to have children or is medically unable to have children, then it is clear either that no-one is eligible to inherit or alternatively that there is a beneficiary, or a group of beneficiaries (known in law as a class of beneficiaries) who are entitled to inherit. It is impossible, at the time of Donna's death, to decide that the trust fails because there may yet be eligible beneficiaries. Accordingly, the wait and see provision of s.7 would be used in order to maintain the trust until it becomes clear either that there are no beneficiaries, or the 125-year period lapses.

On the other hand, lets us say that Tess writes a will on the same terms as Donna, namely leaving money to be divided equally between the children of her brothers and sisters, with the issue of such children to take the share their parent would have received if they had not died. However, Tess is 68 when she dies and her sister is 88, and has no children. It is clear in this instance that the trust fails because there is no-one who has been identified as a beneficiary, and it is not possible (or at least unlikely in the extreme) that there will be anyone alive in the future who is able to inherit. Accordingly the trust fails. The first principle of the rule against perpetuities and accumulations therefore prevents the trust from continuing in operation on an indefinite basis if it is not clear whether anyone would be eligible to inherit.

The second aspect of the principle is that the trust may not be invested on an indefinite basis. An example of this may arise with prizes for academic excellence. Consider the situation where an educational establishment awards prizes for academic excellence. The trustees may be under an obligation to award the prize every year and if so they must abide by the terms of their obligation. However, it may be that in some years, no entrant is eligible, and the prize is reinvested and distributed the following year. Again, while this may be desirable in the short term, the law is again eager to ensure that this does not fetter property on an indefinite basis, and so the perpetuity rule (and the time periods contained within statute or common law as applicable) applies in this instance as well. In other words, the trustees may be permitted to refrain from distributing the trust fund for a period of time, but they cannot do this on an indefinite basis. The longest period of time for which the trustees can defer distribution is the relevant perpetuity period in operation when the trust was made.

The third element of the rule against perpetuities is that a restriction on the alienation and enjoyment of the trust property must only apply for the duration of the perpetuity period. For example, Lord Wealthy of Goldpots owns Goldpots House, and decides to create a trust that will prevent any of his heirs from selling the Wealthy family seat. Such a restriction would be valid for the duration of the perpetuity period applicable at the time of Lord Wealthy's death. However, the restriction could not last beyond this time. Accordingly, 125 years after Lord Wealthy's death, his great-great-grandson could not be prevented from selling Goldpots House if he wished.

Chapter summary

This chapter may be useful for assessments and assignments on:

- The characteristics of a trust
- The formality required in order to create a trust.

Further reading

Fairbairn, P. and Wood, V. (2010) 'Hanging onto the family silver' 15(3) *Elderly Client Adviser* 12.

Goldsmith, J. (2010) 'The Perpetuities and Accumulations Act 2009' 1(1) *Elder Law Journal* 83.

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10

The trust property

Chapter outline

This chapter will cover:

- The variety of types of property that may be the subject of a trust
- Trust property need not be of particular monetary value
- The types of property that may not be the subject of a trust.

Introduction

It is important that you read this chapter in conjunction with the text on the certainty of subject matter (see Chapter 8).

Property that may be the subject of a trust

The property that forms the subject matter of the trust may, in most cases, consist of any property that may be owned and transferred. Therefore, trusts may comprise of land, money, company shares or chattels. A trust may even be created out of an equitable interest, therefore a beneficiary under a trust may create a trust out of that to which he or she is entitled.

A trust arising on death, either in the form of a will or in the form of intestacy, is probably the situation where the widest range of trust property is encountered. Trusts in other contexts are likely to consist of money, or specific types of property, such as land, or specific goods that are the subject of a contractual relationship. However, with a will a testator is likely to be disposing of everything that he or she owns, and therefore a will is likely to refer to a broader range of assets than other types of trusts. Below, as an example of a trust where the testator disposes of a broad range of assets, is a transcript of the will of William Shakespeare.

EXTRACT

The Will of William Shakespeare

Vicesimo Quinto die Januarii (struck through) Martii Anno Regni Domini nostri Jacobi nucn Regis Angliae etc decimo quarto & Scotie xlixo Annoque Domini 1616

Testamentum

Willemi Shackspeare

Registretur

In the name of god Amen I William Shackspeare of Stratford upon Avon in the countie of Warr' gent in perfect health & memorie god by praysed doe make & Ordayne this my last will & testam[en]t in manner & forme followeing That ys to saye first I Comend my Soule into the hands of god my Creator hoping & assuredlie beleeving through thonelie merittes of Jesus Christe my Saviour to be made partaker of lyfe everlastinge And my bodye to the Earthe whereof yt ys made.

I[te]m I Gyve and bequeath unto my sonne in L[aw] (struck through) Daughter Judyth One Hundred & ffyftie pounds **(1)** of lawfull English money to be paied unto her in manner and forme follewing That ys to saye One Hundred Poundes in discharge of her marriage porc[i]on within one yeare after my deceas w[i]th considerac[i]on after the Rate of twoe shillinges in the pound for soe long tyme as the same shalbe unpaid unto her after my deceas & the ffyftie pounds Residewe thereof upon her surrendering of or gyving of such sufficient securitie as the overseers of this my will shall like of to Surrender or graunte All her estate and Right that shall discend or come unto her after my deceas or that she nowe hath of in or to one Copiehold ten[emen]te with theappertenances lyeing & being in Stratford upon Avon aforesaied in the

saide countie of warr' being parcell or holden of the mannor of Rowington unto my daughter Susanna Hall & and her heiries for ever. **(2)**

Item I gyve and bequeath unto my saied Daughter Judyth One Hundred & ffyftie Poundes more if shee or Anie issue of her bodie Lyvinge att thend of three yeares next ensueing the daie of the date of this my will during which tyme my executors to paie her considerac[i]on from my deceas according to the Rate aforesaied. And if she dye within the saied terme without issue of her bodye then my will ys & and I doe gyve & bequeath One Hundred Poundes thereof to my Neece Elizabeth Hall & ffiftie Poundes to be sett fourth by my executors during the lief of my Sister Johane Harte & the use and proffitt thereof Cominge shalbe payed to my saied Sister Jone **(3)** & after her deceas the saied L li shall Remaine Amongst the children of my saied Sister Equallie to be devided Amongst them. But if my saied daughter Judith be lyving att thend of the saeid three yeares or anie issue of her bodye then my will ys & soe I devise & bequeath the saied Hundred & ffyftie poundes to be sett out by my executors and overseers for the best benefitt of her and her issue and the stock not to be paied unto her soe long as she shalbe marryed and Covert Baron by my executors & overseers (struck through) but my will ys that she shall have the considerac[i]on yearelie paied unto her during her lief & after her deceas the saied stock and condierac[i]on to bee paid to her children if she have Anie & if not to her executors or Assignes she lyving the saied terme after my deceas provided that if such husbond as she shall att thend of the saied three yeares by marryed unto or attain after doe sufficientlie Assure unto her & thissue of her bodie landes answereable to the porc[i]on by this my will gyven unto her & to be adjudged soe by my executors & overseers then my will ys that the saied CL li shalbe paied to such husbond as shall make such assurance to his owne use.

Item I gyve and bequeath unto my saied sister Jone XX li & all my wearing Apparrell to be paied and delivered within one yeare after my deceas **(4)**. And I doe will & devise unto her the house with thappurtenances in Stratford where in she dwelleth for her naturall lief under the yearelie Rent of xiid

Item I gyve and bequeath unto her three sonnes William Harte (name omitted) Hart and Michaell Harte ffyve pounds A peece to be payed within one yeare after my decease to be sett out for her within one yeare after my deceas by my executors with thadvise & direccons of my overseers for her best proffitt untill her marriage & then the same with the increase thereof to be paied unto her (struck through).

Item I gyve and bequeath unto her (struck through) the saied Elizabeth Hall All my Plate **(5)** (except my brod silver and gilt bole) that I now have att the date of this my will.

Item I gyve and bequeath unto the Poore of Stratford aforesaied tenn poundes; **(6)** to Mr Thomas Combe my Sword; **(7)** to Thomas Russell Esquier ffyve poundes & to ffrauncis Collins of the Borough of Warr' in the countie of Warr' gent. thirteene poundes Sixe shillinges & Eight pence to be paied within one yeare after my deceas.

Item I gyve and bequeath to mr Richard (struck through) Hamlett Sadler Tyler thelder (struck through) XXVIs VIIId to buy him A Ringe; to William Raynoldes **(8)** gent XXVIs VIIId to buy him a Ringe; to my godson William Walker XXs in gold; to Anthonye Nashe gent. XXVIs VIIId to mr. John Nash XXVIs VIIId in gold (struck through) & to my ffellowes John Hemynges, Richard Burbage & Heny Cundell XXVIs VIIId A peece to buy them Ringes.

Item I Gyve Will Bequeth and Devise unto my Daughter Susanna Hall for better enabling of her to performe this my will & towardes the performans thereof All that Capitall Messuage or tenemente with thappertenaces in Stratford aforesaid called the newe plase wherein I nowe Dwell & two messuags or ten[emen]tes with thappurtenances scituat lyeing and being in Henley Streete within the borough of Stratford aforesaied. And all my barnes, stables, Orchardes,

gardens, landes, ten[emen]tes and herediaments whatsoever scituat lyeing & being or to be had Receyved, perceyved or taken within the townes & Hamletts, villages, ffieldes & groundes of Stratford upon Avon, Oldstratford, Bushopton & Welcombe or in anie of them in the saied countie of warr And alsoe All that Messuage or ten[emen]te with thappurtenances wherein one John Robinson dwelleth, scituat, lyeing & being in the blackfriers in London nere the Wardrobe & all other my landes ten[emen]tes & hereditam[en]tes whatsoever. To Have and to hold All & sing[u]ler the saied premisses with their Appurtenances unto the saied Susanna Hall for & during the terme of her naturall lief & after her deceas to the first sonne of her bodie lawfullie yssueing & to the heiries Males of the bodie of the saied first Sonne lawfullie yssueinge & for defalt of such issue to the second Sonne of her bodie lawfullie issueinge & of [struck through] to the heires Males of the bodie of the saied Second Sonne lawfullie yssyeinge & for defalt of such heires to the third sonne of the bodie of the saied Susanna Lawfullie yssyeing & of the heires Males of the bodie of the saied third sonne lawfullie yssueing And for defalt of such issue the same soe to be Remaine to the ffourth, sonne (struck through) ffythe, sixte and seaventh sonnes of her bodie lawfullie issueing one after Another & and to the heires Males of the bodies of the saied ffourth, ffythe, Sixte and Seaventh sonnes of her bodie lawfullie yssueing one after Another & to the heires Males of the bodies of the saied ffourth, fifth, Sixte & Seaventh sonnes lawfullie yssueing in such mamer as yt ys before Lymitted to be & Remaine to the first, second & third Sonns of her bodie & to their heires males. And for default of such issue the saied premises to be & Remaine to my sayed Neece Hall & the heires Males of her bodie Lawfull yssueing for def[ault of] . . . [damaged] . . . such iss[u]e to my daughter Judith & the heires Males of her bodie lawfullie issueinge. And for defalt of such issue to the Right heires of me the saied Willm Shackspere for ever.

Item I gyve unto my wief my second best bed with the furniture; **(9)** (Item I gyve and bequeath to my saied daughter Judith my broad silver gilt bole **(10)**.

All the Rest of my goodes Chattel, Leases, plate, Jewels & household stuffe whatsoever after my dettes and Legasies paied & my funerall expences discharged, **(11)** I gyve devise & bequeath to my Sonne in Lawe John Hall gent. & my daughter Susanna his wief whom I ordaine & make executors of this my last will & testam[en]t. And I doe entreat & Appoint the saied Thomas Russell Esquier & ffraunci[s] Collins gent. To be overseers hereof And doe Revoke All former wills and publishe this to be my last will & testam[en]t. In Wit[n]es whereof I have hereunto put my hand the Daie & Yeare first above Written.

By me William Shakspeare (signed)

Witnes to the publishing Hereof (signed)

Fra: Collyns

Juliyus Shawe

John Robinson

Hamnet Sadler

Robert Whattcott

Probatum coram Mag[ist]ro Willi[a]mo Byrde legum d[o]c[t]ore Commissar[io] etc. xxiido die mensis Junii Anno d[omi]ni 1616 Juram[en]to Johannis Hall unius ex[ecutorum] etc. Cui etc. de bene etc. Jurat[i[Res

Source: **The National Archives (2012) Shakespeare's Will.** http://www.nationalarchives.gov.uk/museum/item.asp?item_id=21

This will provides an example of the variety of items that a person could leave in a will. The first substantive item to which attention may be drawn **(1)** is a trust of money to his daughter, Judith. Shakespeare then gives all the land he owns in Stratford-Upon-Avon to his elder daughter, Susanna **(2)**. The third item of interest is at **(3)**, where Shakespeare gives his sister Joan Hart a life interest in the sum of £50 – so that any income from the investment of the money is to be paid to her. **(4)** provides that Joan Hart is also to receive all Shakespeare's 'wearing apparrell' – his clothes. His plate items **(5)** (these would include items plated with gold or silver, such as tableware and cutlery) were given to his niece, Elizabeth Hall. The sixth item to which attention may be drawn is a legacy of £10 given to 'the poor of Stratford' **(6).** The seventh item is the gift of Shakespeare's sword **(7).** Eighth is a sum of money given to William Reynolds with the specific direction that it should be used to buy him a ring **(8).** Shakespeare leaves his second best bed to his wife along with his furniture **(9).** The final specific legacy is a broad gilt bowl which is given to his daghter Judith **(10)**. **(11)** is a residuary clause whereby everything that is not specified in the will is left to Shakespeare's son and daughter in law.

What this will shows therefore is that a will (or indeed any other type of trust) may be used to dispose of valuable items, such as money and land, but that it may also be used to dispose of less valuable items that may have personal significance to the testator and the beneficiary. For example, the fact that Shakespeare leaves most of his plate items to his niece may be indicative of her particular need for it compared with older members of Shakespeare's family, who may have already established their own households, and would not therefore need tableware.

However, there is one exception to this – the broad gilt bowl is not to go to Elizabeth Hall, but instead to his daughter, Judith. It is not known why this should be the case, but it is possible to conjecture that Judith may have been particularly fond of it, or that it had a particular significance for Judith that would not be shared by other relatives. A trust therefore may be used in order to create trusts of property that may not have any financial significance at all, as well as trusts involving assets worth several millions of pounds.

Intestacy also envisages a trust being created of the deceased's personal chattels as defined in s.55(1)(x) Administration of Estates Act 1925. Therefore where the deceased has died leaving a spouse or a civil partner, s.46 provides that the spouse or civil partner will inherit the personal chattels, which will include things that have nominal value as well as items that are more valuable. The jewellery referred to in s.46 may include items made of precious stones or gold and silver. It may however also include costume jewellery from a Christmas cracker. Therefore, although it is common to think of trusts as being an area of law that deals with valuable commodities – and indeed financial value may be a signficiant factor in the question of whether the claim is worth the cost and inconvenience of initiating litigation – trust property may also comprise of items that have very little value in financial terms.

EXTRACT

Administration of Estates Act 1925, s.55(1)(x)

(x) 'Personal chattels' mean carriages, horses, stable furniture and effects (not used for business purposes), motor cars and accessories (not used for business purposes), garden effects, domestic animals, plate, plated articles, linen, china, glass, books, pictures, prints, furniture, jewellery, articles of household or personal use or ornament, musical and scientific instruments and apparatus, wines, liquors and consumable stores, but do not include any chattels used at the death of the intestate for business purposes nor money or securities for money:

It is possible, though perhaps less probable, that *inter vivos* trusts created in a family context may be equally broad in terms of subject matter. However, it is less likely with *inter vivos* trusts that the settlor would wish to dispose of personal mementoes and items that are in frequent use – it is unlikely that an *inter vivos* trust would comprise of clothes or furniture for example. Accordingly, *inter vivos* trusts created intentionally are more likely to comprise of items that have more significant value, such as money or land.

Nevertheless, *inter vivos* trusts of goods that have been ordered from a seller may of course consist of a broad range of chattels, such as the gold bullion in the case of *Re Goldcorp Exchange* [1995] AC 74, or the Christmas gifts and foods that were the subject of the argument concerning the existence of a trust in *Re Farepak Food and Gifts Ltd* [2006] All ER (D) 265 (Dec). Similarly, donations of items to a charity shop are, in effect, a trust, and are likely to consist of a broad range of chattels.

More commonly however, trust property consists of money or choses in action, or land. Therefore, wills and trusts are most likely to be written where the settlor owns land or money that he or she wishes to bequeath. Professionally drawn wills are also likely to permit the trustees to sell any assets in order to enable them to invest the proceeds. Similarly, in the context of *inter vivos* family trusts, the trust will ordinarily be created in order to confer a financial benefit on the beneficiary, and will therefore be likely to consist of money, or things that have financial value.

In commercial trusts, the purpose of the trust is often to ringfence a particular fund or pool of money – as is encountered in the trusts in *Re Kayford* [1975] 1 All ER 604 and *Barclays Bank Ltd v Quistclose Investments Ltd* [1970] AC 567. Charitable trusts and unincorporated associations are also likely to be trusts where the trust property is most likely to comprise of money. In the context of charities, the money that forms the subject matter of the trust is likely to be money raised either through donations (even the simple act of putting fifty pence in a charity collection box is the act of creating a trust) and legacies, or through fundraising.

The other most common form of trust property is land. As has been shown, many aspects of land ownership make use of the trust, from the seller acting as trustee of the land for the benefit of the buyer from the point at which contracts for the sale and purchase of land are exchanged, to co-ownership's reliance on trusts in the form of s.34 and s.36 Law of Property Act 1925. Where a trust is implied from the parties' common intentions, the subject matter of the trust is also likely to be land, as the line of cases from *Pettit v Pettit* [1970] AC 777 to *Lloyds Bank v Rossett* [1990] 1 AC 107 to *Stack v Dowden* [2007] 2 AC 432 to *Jones v Kernott* [2012] AC 776 indicate. These cases will be discussed further in Part 3.

Property that may not be the subject of a trust

Although most forms of real and personal property – including an equitable interest – may be the subject of a trust, some types of property cannot be transferred. Section 21 of the National Trust Act 1907[1] prevents some land from being alienable (i.e. transferred), once it has been acquired by the National Trust. Therefore, although the National Trust holds the freehold title to the land as trustees, it cannot transfer ownership of that land. The rule exists in order to prevent any sale or gift of the land. However, as sale would necessarily involve an element of the law of trusts being invoked, the rule also effectively prevents the National Trust from creating a trust of the land it owns. The land that is subject to this rule is listed in Schedule 1 Part 1 of the Act.

[1] (1907 c.136).

EXTRACT

National Trust Act 1907, Schedule 1

Freehold

County	Parish	Name and Description of Property
Merionethshire..	Llanaber..	The cliff known as 'Dinas o leu,' Barmouth.
Sussex.....	Alfriston..	The Old Clergy House.
Cornwall....	Tintagel..	15 acres of cliff land at Barras Head.
Wiltshire....	Salisbury..	The Joiners' Hall.
Kent.....	Brasted..	Land on Toy's Hill.
Cambridgeshire....	Wicken....	About 4 acres of Wicken Fen.
Kent.....	Westerham..	15 acres of woodland on Ide Hill.
Derbyshire..	Duffield....	Duffield Castle.
Co Cork....	Kilmeen..	Kanturk Castle.
Buckinghamshire....	Long Crendon..	The Old Court House.
Surrey....	Godalming..	Eashing Bridges.
Cumberland..	Crosthwaite....	Brandlehow Park Derwentwater 108 acres.
Monmouthshire....	Dixton Hadnock....	9 acres of Kymin Hill.
Cornwall..	Tintagel..	Old 14th century house known as 'The Old Post Office.'
Kent....	Westerham..	3 1/2 acres on Crockham Hill.
Devonshire..	Rockbeare..	21 acres on Rockbeare Hill known as Prickly Pear Blossoms Park and Recreation Ground.
Derbyshire..	Winster....	Old Market House.
Berkshire....	Newtown....	Land at Newtown Common.
Surrey....	Thursley..	Hindhead Inval and Weydown Commons 750 acres.
Cumberland..	Greystoke..	Gowbarrow Deer Park and Aira Force 750 acres.
Berkshire..	Newbury..	Monument to Viscount Falkland.
Yorkshire..	Sharow....	Old Sanctuary Cross.
Gloucestershire....	Westbury-on-Trym....	Westbury College Gatehouse.
Cambridgeshire....	Burwell....	30 acres of Fenland.
Surrey....	Wimbledon..	Mill Pond at Merton.
Somerset....	Barrington..	Barrington Court and 34 acres of land adjoining.

Other than Freehold

County	Parish	Name and Description of Property	Nature of Interest
Dorset..	Portesham....	Monument to Vice-Admiral Sir Thomas Hardy.	Lease for 500 years.
Cumberland....	Keswick..	Monument to John Ruskin on Friars Crag, Derwentwater.	Tenancy at will.

Other property that may not be the subject of a trust includes property that the settlor does not own – as has been shown with cases such as *Glegg v Bromley* [1912] 3 KB 474, where damages that the putitive settlor hoped to gain in successful litigation could not validly form the subject matter of the trust, and *Re Ellenborough* [1903] 1 Ch 697, where it was held that no trust could be created out of an inheritance that the settlor expected to acquire on the death of siblings, where the purported settlor siblings were still alive and therefore having the freedom to change any wills they had made in the purported settlor's favour.

EXTRACT

Dilnot, A and Harris L. (2012) 'Ownership of a fund' 5 *Journal of International Banking and Financial Law* 272

Introduction

. . . the principles which determine when a trust will arise in a commercial context must be clear and understandable. However, the English law of intermediated securities is built almost entirely upon the dubious authority of the Court of Appeal's decision in *Hunter v Moss* [1994] 1 WLR 452. This case was the basis of the decision of Briggs J in *Pearson & Ors* as the Joint Administrators of *Lehman Brothers International (Europe) (In Administration) v Lehman Brothers Finance SA & Ors* [2010] EWHC 2914 (Ch) (otherwise known as 'RASCALS'), upheld on appeal, that investors had a proprietary interest in securities and other intangible assets held in an un-segregated house depot account rather than in a segregated securities account (although the final outcome of the case was that the investors had alienated their interest under the RASCALS process by way of repo transactions and stock loans).

The issue in question concerns the requirement that for a trust to exist there must be certainty as to both the subject matter of the trust and the extent of the beneficiary's interest. While this requirement is easy to state in principle, it is not so easy to apply where the alleged trust fund consists of property held by the insolvent institution in an un-segregated house account where it has been mixed with other property belonging to both the institution and other investors (or affiliates) and with which the institution may be at liberty to deal on its own account. The extent to which a trust of intangible property can arise in these circumstances depends upon the true import of *Hunter v Moss*, a case far removed from the complexities of modern-day banking practice.

. . . As *Hunter v Moss* remains the leading authority on certainty of subject matter and the foundation of the modern securities industry in England, it is important to identify precisely why the case was decided as it was. However, before considering the judgments in detail it is useful to begin with a few introductory points:

First, central to any analysis of the law in this field is the concept of "fungability" . . . Frequently given examples of fungibles are tangibles valued by number, measurement or weight, such as grain or bars of gold. However, strictly speaking, whether assets are fungible does not depend upon their physical characteristics but upon whether they are legally interchangeable for the purpose of satisfying the transfer obligation in question. Intangible assets (eg debts) are capable of being fungible just as much as chattels.

Secondly, the factual situation in *Hunter v Moss* (according to the conventional understanding of the case) concerned a declaration of trust in respect of a specified but unidentified number of shares which together formed a discrete fund in the hands of the defendant (ie 50 of the fund of 950 shares held by the defendant) . . . Any case where there is no comparable discrete fund of intangible assets is factually different from *Hunter v Moss* and any legal analysis of that alternative situation which depends upon *Hunter v Moss* must take full account of that vital difference.

Thirdly, under *Hunter v Moss* the creation of the (equitable) proprietary interest in the 50 shares in favour of the plaintiff arose under a declaration of trust. However, while a declaration of trust is one way in which ownership of assets comprised in a bulk might pass to another person, there are others: most notably under a gift at common law or under a contract of sale.

Fourthly, there is an important difference between a proportionate share in a bulk and a part of the bulk defined by a numeric quantity of the consistent assets. A proportionate share, say, 10% of a 100 identical bottles of wine gives the owner a 10% interest in each and every bottle. A percentage share is not capable of appropriation or identification because it is, by its very nature, an undivided interest. No issues of identification arise. Conversely, ownership of ten bottles out of the fund of 100 gives absolute ownership of the ten in question and no interest in the balance. Here, there is question of identification: precisely which ten bottles of the 100 are we talking about? Thus, problems of identification only arise where the subject matter of the transfer is expressed as numeric rather than proportionate terms. It is important to note that, in *Hunter v Moss* the deputy judge's finding was that there had been a declaration of trust in respect of 50 of the plaintiff's shares, not a percentage of his holding . . .

Returning to *Hunter v Moss*, the defendant's principal objection to the validly of the declaration of trust of the 50 shares was based upon an analogy with declarations of trust in respect of chattels and the decision in Re London Wine Co (Shippers) Ltd [1986] PCC 121 . . . That there was no segregation of the securities contained in the house account was the objection raised in RASCALS to the assertion of a proprietary interest in the fund (ie the assets held in the house account).

In *Hunter v Moss* the defendant suggested that the same principle must apply to shares ie that a proprietary interest was contingent upon segregation. However, the deputy judge rejected this argument. He held that the test should be whether, immediately after the declaration of trust, the court could, if asked, make an order for the execution of the trust, which it could only do if the subject-matter of the trust is identified with sufficient certainty . . .

The Court of Appeal upheld the trial judge's reasoning although on different grounds . . . There are profound difficulties with the Court of Appeal's reasoning.

First, the comparison with testamentary gifts is not at all convincing. As Professor Hayton has observed, where the testator dies the whole of his estate vests in his executors, who take the property legally and beneficially but subject to fiduciary duties to administer it in accordance with the law including carrying the testator's wishes into effect.

Second, although Dillon LJ distinguished Re London Wine Co (Shippers) Ltd factually, he did not say why the distinction made any legal difference. . . .

More importantly, in discarding the analogy with sale, Dillon LJ seemed to overlook that, in some circumstances, where there is a contract for the sale of property which imposes a specifically enforceable and unconditional obligation on the vendor to transfer the property, equity will impose a trust on the ground that equity treats as done that which ought to be done. Due to the general absence of specific performance as a remedy in contracts for the sale of goods this analysis is not available for such contracts, but what of a contract of sale of shares or other personalty? If the contract is unconditional and specifically enforceable, might it not give rise to an equitable interest in shares in favour of the purchaser?

Finally, a similar point can be made in relation to Mac-Jordan Construction. The decision in that case was sound because the developer's declaration of trust did not relate to any particular fund, but could only pertain to the developer's general assets. It is implicit that, by contrast, the Court of Appeal thought that the defendant's holding of 950 shares was a sufficiently specific fund, separate from the defendant's general assets, to resolve any issue as to certainty of subject matter, any further appropriation to the plaintiff's specific interest being unnecessary. However, this is not what Dillon LJ actually said.

An alternative analysis of fund ownership

It will be apparent from the forgoing that both the deputy judge and the Court of Appeal in *Hunter v Moss* approached the issue of subject matter certainty on the basis that the defendant's 950 shares was a discrete fund of fungible assets. It was essentially on this basis that the deputy judge distinguished Re London Wine Co (Shippers) Ltd. However, there is another analysis of the case which was proposed by Professor Goode in his article: 'Are Intangible Assets Fungible' [2003] LMCLQ 379 . . . Goode's argument is that shares are not fungible intangibles at all. A person who holds, say, 50 shares in a company which has issued 500 shares is simply a co-owner of the issued share capital to the extent of 10% . . .

Certainty of subject matter and fungible intangibles

In advancing his alternative explanation for Hunter v Moss, Goode does not seek to cast doubt on the suggestion that intangible property can be fungible . . . Thus, the question which remains is whether the test of certainty of subject matter is the same as for chattels: does it require the equivalent of segregation or something less rigid? In RASCALS, Briggs J, although preferring Goode's 'single asset theory', accepted that the case before him was authority for the proposition that:

> 'A trust of part of a fungible mass without the appropriation of any specific part of it for the beneficiary does not fail for uncertainty of subject matter, provided that the mass itself is sufficiently identified and provided also that the beneficiary's proportionate share of it is not itself uncertain.

. . . The view advanced here is that the approach adopted by Colin Rimer QC at first instance in *Hunter v Moss* was correct. In the first place it is arguable that, notwithstanding the Court of Appeal's weaknesses of reasoning, the case can in fact be supported as consistent with an old and impressive line of authority concerning declarations of trust in respect of shares. Secondly, what is of fundamental importance to the existence of any trust is not compliance with an abstract standard of certainty but, rather, whether practically, the court can enforce the trust which equity imposes upon the settlor.

The deputy judge in *Hunter v Moss* was therefore correct to say that the real test is whether the court could make an order carrying the trust into effect.

In order for the trust to remain relevant in the modern world of banking and securities, this must be the approach of the courts and indeed this was the approach of both Briggs J and the Court of Appeal in RASCALS, which has strengthened the juridical basis of property rights in funds, slightly.

What this chapter has demonstrated therefore is that most things that can be owned can be the subject of a trust. The restrictions therefore pertain more to the certainty with which the trust property is defined, rather than the type of property that comprises the subject matter of the trust.

Chapter summary

This chapter may be useful for assessments and assignments on:

- The subject matter of a trust
- The defining characteristics of a trust.

Further reading

Hargreaves, E. (2011) 'The nature of beneficiaries' rights under trusts' 4 *Trusts Law International* 163.

Parkinson, P. (2002) 'Reconceptualising the Express Trust' 61 *Cambridge Law Journal* 657.

11

The trustee

Chapter outline

This chapter will cover:

- Who may be a trustee?
- Specific types of trustee
- The appointment of trustees
- Accepting and declining the office of trustee
- The trustee's rights
- The trustee's duties under the Trustee Act 2000
- The trustee's duties when exercising specific powers
- The trustee's further duties.

Introduction

In the trust relationship, the most onerous obligation is imposed on the trustee. This chapter will therefore discuss the various aspects of the trustee's role and functions. This chapter will explain the role of the trustee in the three-party relationship of the trust, and what happens when the trustee acts in breach of his or her obligations.

Who may be a trustee?

Because the settlor transfers ownership of the trust property to the trustee, it is necessary that the trustee is capable of being the legal owner of the trust property. Accordingly, an individual or a company may act as a trustee. Nevertheless, although a child may be the legal owner of personal property, the appointment of a person under the age of 18 as a trustee is void according to s.20 Law of Property Act 1925.[1]

EXTRACT

Law of Property Act 1925, s.20

Infants not to be appointed trustees

The appointment of an infant to be a trustee in relation to any settlement or trust shall be void, but without prejudice to the power to appoint a new trustee to fill the vacancy.

Nevertheless, as will be shown in Chapter 14, it is possible for a trust to be recognised by a court because it would be unjust to deny the trustee's obligation. This is known as a resulting or a constructive trust (these are similar, but not identical concepts, as will be seen later in this book) and it appears that, with the exception of trusts of land, it is possible for a person who is under the age of 18 to be identified as a trustee of a resulting or constructive trust, as confirmed in the case of *Re Vinogradoff, Allen v Jackson* [1935] WN 68.

Another issue is of course the question of capacity in the sense of mental capability. Because the role of being a trustee is an onerous obligation, there is a need to ensure that the trustee has the required capacity to fulfil that obligation. However, this is problematic. The settlor appoints the trustee, and therefore, if the settlor appoints a trustee who lacks capacity, it would appear that the law cannot prevent the appointment. However, a trustee may resign voluntarily from the obligation in accordance with s.36 Trustee Act 1925.[2] Alternatively, the other trustees may replace the trustee who is incapable of performing his or her duties in accordance with s.36 (as amended). The beneficiaries may also apply for a court order to remove an incapacitated trustee if the other trustees do not do so.

One restriction on the ability of trustees and beneficiaries to remove incapacitated trustees is that the Court of Protection must give leave to do so in cases where the incapacitated trustee is also a beneficiary of the trust.[3] The removal of a trustee must be made in writing by the remaining trustees. It is also possible that the trust instrument may

[1] (1925 c.20).
[2] (1925 c.19).
[3] Trustee Act 1925, s.36(9).

determine how a trustee is to be replaced. If this is the case, then the removal and appointment of trustees will occur in accordance with that process, and may involve a specific person or group nominating or identifying a new trustee. For example, with a charitable trust, it may be the case that a person is appointed ex-officio to the trusteeship, or that the post is advertised publicly.

EXTRACT

Trustee Act 1925, s.36

(1) Where a trustee, either original or substituted, and whether appointed by a court or otherwise, is dead, or remains out of the United Kingdom for more than twelve months, or desires to be discharged from all or any of the trusts or powers reposed in or conferred on him, or refuses or is unfit to act therein, or is incapable of acting therein, or is an infant, then, subject to the restrictions imposed by this Act on the number of trustees, –

(a) the person or persons nominated for the purpose of appointing new trustees by the instrument, if any, creating the trust; or

(b) if there is no such person, or no such person able and willing to act, then the surviving or continuing trustees or trustee for the time being, or the personal representatives of the last surviving or continuing trustee;

may, by writing, appoint one or more other persons (whether or not being the persons exercising the power) to be a trustee or trustees in the place of the trustee so deceased remaining out of the United Kingdom, desiring to be discharged, refusing, or being unfit or being incapable, or being an infant, as aforesaid.

(2) Where a trustee has been removed under a power contained in the instrument creating the trust, a new trustee or new trustees may be appointed in the place of the trustee who is removed, as if he were dead, or, in the case of a corporation, as if the corporation desired to be discharged from the trust, and the provisions of this section shall apply accordingly, but subject to the restrictions imposed by this Act on the number of trustees.

(3) Where a corporation being a trustee is or has been dissolved, either before or after the commencement of this Act, then, for the purposes of this section and of any enactment replaced thereby, the corporation shall be deemed to be and to have been from the date of the dissolution incapable of acting in the trusts or powers reposed in or conferred on the corporation.

(4) The power of appointment given by subsection (1) of this section or any similar previous enactment to the personal representatives of a last surviving or continuing trustee shall be and shall be deemed always to have been exercisable by the executors for the time being (whether original or by representation) of such surviving or continuing trustee who have proved the will of their testator or by the administrators for the time being of such trustee without the concurrence of any executor who has renounced or has not proved.

(5) But a sole or last surviving executor intending to renounce, or all the executors where they all intend to renounce, shall have and shall be deemed always to have had power, at any time before renouncing probate, to exercise the power of appointment given by this section, or by any similar previous enactment, if willing to act for that purpose and without thereby accepting the office of executor.

[(6) Where, in the case of any trust, there are not more than three trustees –]

(a) the person or persons nominated for the purpose of appointing new trustees by the instrument, if any, creating the trust; or

(b) if there is no such person, or no such person able and willing to act, then the trustee or trustees for the time being;

may, by writing appoint another person or other persons to be an additional trustee or additional trustees, but it shall not be obligatory to appoint any additional trustee, unless the instrument, if any, creating the trust, or any statutory enactment provides to the contrary, nor shall the number of trustees be increased beyond four by virtue of any such appointment.

[(6A) A person who is either –

(a) both a trustee and attorney for the other trustee (if one other), or for both of the other trustees (if two others), under a registered power; or

(b) attorney under a registered power for the trustee (if one) or for both or each of the trustees (if two or three),

may, if subsection (6B) of this section is satisfied in relation to him, make an appointment under subsection (6)(b) of this section on behalf of the trustee or trustees.

(6B) This subsection is satisfied in relation to an attorney under a registered power for one or more trustees if (as attorney under the power) –

(a) he intends to exercise any function of the trustee or trustees by virtue of section 1(1) of the Trustee Delegation Act 1999; or

(b) he intends to exercise any function of the trustee or trustees in relation to any land, capital proceeds of a conveyance of land or income from land by virtue of its delegation to him under section 25 of this Act or the instrument (if any) creating the trust.

(6C) In subsections (6A) and (6B) of this section 'registered power' means [an enduring power of attorney or lasting power of attorney registered under the Mental Capacity Act 2005].

(6D) Subsection (6A) of this section –

(a) applies only if and so far as a contrary intention is not expressed in the instrument creating the power of attorney (or, where more than one, any of them) or the instrument (if any) creating the trust; and

(b) has effect subject to the terms of those instruments.]

(7) Every new trustee appointed under this section as well before as after all the trust property becomes by law, or by assurance, or otherwise, vested in him, shall have the same powers, authorities, and discretions, and may in all respects act as if he had been originally appointed a trustee by the instrument, if any, creating the trust.

(8) The provisions of this section relating to a trustee who is dead include the case of a person nominated trustee in a will but dying before the testator, and those relative to a continuing trustee include a refusing or retiring trustee, if willing to act in the execution of the provisions of this section.

[(9) Where a trustee [lacks capacity to exercise] his functions as trustee and is also entitled in possession to some beneficial interest in the trust property, no appointment of a new trustee in his place shall be made by virtue of paragraph (b) of subsection (1) of this section unless leave to make the appointment has been given by [the Court of Protection]

Specific types of trustees

Usually, the notion of a trustee is of one or more individual persons who are intentionally appointed as trustees – the three-party situation (discussed in Chapter 6) where the

settlor transfers property to the trustee for the benefit of the beneficiary. In a domestic context involving express trusts of family property, the trustee is likely to be a family member or possibly a solicitor. In commercial contexts and also in the context of charities and pensions, the trustee is likely to be a professional person who has applied for, and who has been appointed to the post.

However, there are also specific types of trustees for specific purposes. A trustee in bankruptcy for example is a person who is appointed to administer the assets of a person who has been declared bankrupt. The trustee in bankruptcy must be a qualified insolvency practitioner.[4]

Trusts of land are also subject to specific rules, and therefore a trustee of land is a particular type of trustee,[5] who has powers to convey the land to the beneficiaries once they have reached full age.[6] Furthermore, in relation to land, ss.30–32 of the Settled Land Act 1925[7] also create specific types of trustees to administer trusts of settled land, as they must have the power to sell the land that is the subject of the settlement.

EXTRACT

Settled Land Act 1925, ss.30–32

Who are trustees for purposes of Act

(1) Subject to the provisions of this Act, the following persons are trustees of a settlement for the purposes of this Act, and are in this Act referred to as the 'trustees of the settlement' or 'trustees of a settlement', namely –

(i) the persons, if any, who are for the time being under the settlement trustees with power of sale of the settled land (subject or not to the consent of any person), or with power of consent to or approval of the exercise of such a power of sale, or if there are no such persons; then

(ii) the persons, if any, for the time being, who are by the settlement declared to be trustees thereof for the purposes of the Settled Land Acts 1882 to 1890, or any of them, or this Act, or if there are no such persons; then

(iii) the persons, if any, who are for the time being under the settlement trustees with [a power or duty to sell] any other land comprised in the settlement and subject to the same limitations as the land to be sold or otherwise dealt with, or with power of consent to or approval of the exercise of such a power of sale, or, if there are no such persons; then

(iv) the persons, if any, who are for the time being under the settlement trustees with [a future power or duty to sell] the settled land, or with power of consent to or approval of the exercise of such a future power of sale, and whether the power [or duty] takes effect in all events or not, or, if there are no such persons; then

(v) the persons, if any, appointed by deed to be trustees of the settlement by all the persons who at the date of the deed were together able, by virtue of their beneficial interests or by the exercise of an equitable power, to dispose of the settled land in equity for the whole estate the subject of the settlement.

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[4] Insolvency Act 1986, s.292(2).
[5] Trusts of Land and Appointment of Trustees Act 1996, s.1(1)(b).
[6] Trusts of Land and Appointment of Trustees Act 1996, s.6(2).
[7] Settled Land Act 1925 (1925 c.18 15 & 16 Geo 5).

(2) Paragraphs (i) (iii) and (iv) of the last preceding subsection take effect in like manner as if the powers therein referred to had not by this Act been made exercisable by the tenant for life or statutory owner.

(3) Where a settlement is created by will, or a settlement has arisen by the effect of an intestacy, and apart from this subsection there would be no trustees for the purposes of this Act of such settlement, then the personal representatives of the deceased shall, until other trustees are appointed, be by virtue of this Act the trustees of the settlement, but where there is a sole personal representative, not being a trust corporation, it shall be obligatory on him to appoint an additional trustee to act with him for the purposes of this Act, and the provisions of the Trustee Act 1925, relating to the appointment of new trustees and the vesting of trust property shall apply accordingly.

31 As to trustees of compound settlements

(1) Persons who are for the time being trustees for the purposes of this Act of an instrument which is a settlement, or is deemed to be a subsisting settlement for the purposes of this Act, shall be the trustees for the purposes of this Act of any settlement constituted by that instrument and any instruments subsequent in date or operation.

[Where there are trustees for the purposes of this Act of the instrument under which there is a tenant for life or statutory owner but there are no trustees for those purposes of a prior instrument, being one of the instruments by which a compound settlement is constituted, those trustees shall, unless and until trustees are appointed of the prior instrument or of the compound settlement, be the trustees for the purposes of this Act of the compound settlement.]

(2) This section applies to instruments coming into operation before as well as after the commencement of this Act, but shall have effect without prejudice to any appointment made by the court before such commencement of trustees of a settlement constituted by more than one instrument, and to the power of the court in any case after such commencement to make any such appointment, and where any such appointment has been made before such commencement or is made thereafter this section shall not apply or shall cease to apply to the settlement consisting of the instruments to which the appointment relates.

32 As to trustees of referential settlements

(1) Where a settlement takes or has taken effect by reference to another settlement, the trustees for the time being of the settlement to which reference is made shall be the trustees of the settlement by reference, but this section does not apply if the settlement by reference contains an appointment of trustees thereof for the purposes of the Settled Land Acts 1882 to 1890, or any of them, or this Act.

(2) This section applies to instruments coming into operation before as well as after the commencement of this Act, but shall have effect without prejudice to any appointment made by the court before such commencement of trustees of a settlement by reference, or of the compound settlement consisting of a settlement and any other settlement or settlements made by reference thereto, and to the power of the court in any case after such commencement to make any such appointment, and where any such appointment has been made before such commencement or is made thereafter this section shall not apply or shall cease to apply.

(3) In this section 'a settlement by reference to another settlement' means a settlement of property upon the limitations and subject to the powers and provisions of an existing settlement, with or without variation.

The judicial trustee and the public trustee are also specific types of trustee. The judicial trustee is the term used to describe the situation where a settlor or a person acting on the settlor's behalf makes an application to the court and, as a result, the Chancery Division of the High Court appoints one or more persons to act as trustees to replace existing trustees.

EXTRACT

Judicial Trustees Act 1896, s.1

Power of court on application to appoint judicial trustee

(1) Where application is made to the court by or on behalf of the person creating or intending to create a trust, or by or on behalf of a trustee or beneficiary, the court may, in its discretion, appoint a person (in this Act called a judicial trustee) to be a trustee of that trust, either jointly with any other person or as sole trustee, and, if sufficient cause is shown, in place of all or any existing trustees.

(2) The administration of the property of a deceased person, whether a testator or intestate, shall be a trust, and the executor or administrator a trustee, within the meaning of this Act.

(3) Any fit and proper person nominated for the purpose in the application may be appointed a judicial trustee, and, in the absence of such nomination, or if the court is not satisfied of the fitness of a person so nominated, an official of the court may be appointed, and in any case a judicial trustee shall be subject to the control and supervision of the court as an officer thereof.

(4) The court may, either on request or without request, give to a judicial trustee any general or special directions in regard to the trust or the administration thereof.

(5) There may be paid to a judicial trustee out of the trust property such remuneration, not exceeding the prescribed limits, as the court may assign in each case, subject to any rules under this Act respecting the application of such remuneration where the judicial trustee is an official of the court, and the remuneration so assigned to any judicial trustee shall, save as the court may for special reasons otherwise order, cover all his work and personal outlay.

(6) . . . in any case where the court shall so direct, an inquiry into the administration by a judicial trustee of any trust, or into any dealing or transaction of a judicial trustee, shall be made in the prescribed manner.

[(7) Where an application relating to the estate of a deceased person is made to the court under this section, the court may, if it thinks fit, proceed as if the application were, or included, an application under section 50 of the Administration of Justice Act 1985 (power of High Court to appoint substitute for, or to remove, personal representative).]

The public trustee, appointed by the Lord Chancellor has the power to:

(a) act in the administration of estates of small value;

(b) act as custodian trustee;

(c) act as an ordinary trustee;

(d) be appointed to be a judicial trustee;

in accordance with s.2(1) of the Public Trustee Act 1906.[8] However, the significance of the public trustee has diminished significantly in recent years with the public trustee only being appointed where there is no one else who is capable of acting as a trustee.

[8] (1906 c.55. 6 Edw 7).

A personal representative, as defined in s.33 Administration of Estates Act 1925[9] is also a form of trustee in a loose sense of that term, in that the personal representative owes a duty not to allow his or her personal interests to conflict with those of the beneficiaries. In this sense the personal representative is in exactly the same situation as the trustee. However, the personal representative does not have the same range of powers of investment and delegation of powers as a trustee.

A seller of land may also be regarded as a form of trustee for the buyer once contracts have been exchanged. A further specific type of trustee is the bare trustee. The bare trustee is a person who acts as a trustee for the benefit of adult beneficiaries. The trustee has no discretion to select beneficiaries from a larger class and the trustee is not a beneficiary under the trust – in essence therefore, the bare trustee is a trustee of the simplest form of trust. The elements of bare trusteeship are discussed by Hall VC in *Christie v Ovington* (1875) 1 Ch D 279, where he explains that:

> It will probably be held to mean a trustee to whose office no duties were originally attached, or who, although such duties were originally attached to his office, would, on the requisition of his *cestuis que trust*, be compellable in equity to convey the estate to them, or by their direction, and has been requested by them so to convey it.

Appointment of trustees

Appointment by declaration

Ordinarily, the trustees will be appointed by the settlor. The simplest method of appointing a trustee naturally arises in the creation of an express trust, especially when this occurs in the form of a written document. In these situations, such as in the case of a will or a trust of land, where writing is essential,[10] the document will specifically identify the trustees, and it is common, although not essential, for the trustees to give their consent to the appointment.

Standard clauses in wills will usually include a clause identifying either an individual or individuals to act as trustees and, in such cases, the appointment of a trustee is usually not problematic. The example below provides a standard clause for appointing one's spouse to be the trustee of one's will.

EXTRACT

Williams on Wills, Form B.3.1: Appointment of wife as sole executrix and trustee with alternative appointment

I appoint my wife [*name*] sole executrix and trustee of this my will but if my wife shall die in my lifetime or shall refuse or be unable to act as such executrix and trustee[2] then I appoint [*name*] of [*address*] and [*name*] of [*address*] to be the executors and trustees of this my will and I declare that in this will the expression 'my trustee' shall where the context so admits include my personal representatives or personal representative for the time being and the trustees or trustee for the time being of this will.

Source: Sherrin, C.H. *et al.* (2002) *Williams on Wills*, 8th ed. Butterworth-Heinemann: Oxford.

[9] (1925 c.23).
[10] Law of Property Act 1925, s.53(1)(a).

However, the case of *Waidanis v Rivers* [1908] 1 Ch 123 indicates that the appointment of trustees by declaration does not always occur in the manner envisaged by the law. In this case, there was an express declaration of who the trustees were to be. However, this was not declared in the will that was the subject of the litigation. Instead, one of the trustees had appointed a trustee to administer his own estate, which implicitly also included administering the estate of the deceased.

EXTRACT

Waidanis v Rivers [1908] 1 Ch 123

Case facts

Elizabeth Waidanis wrote a will appointing the executors and trustees of her father's will to be the executors and trustees of her will also. The trustees originally appointed under Elizabeth Waidanis' father's will were all dead, as were the trustees appointed in their place. The last survivor of these trustees, Tom Lamonby had appointed the defendants to execute his own estate, and this included administering the will of Elizabeth Waidanis' father. The defendants argued that they had never been appointed as trustees of Elizabeth Waidanis' father's will, and were therefore under no obligation to act as trustees for the will of Elizabeth Waidanis.

Swinfen Eady J

I should be sorry to throw any doubt on the proposition that the executors of Tom Lamonby were the trustees of the will of his testator. By the will of Mrs. Waidanis's father his real estate was devised to trustees therein named, their heirs and assigns. Successive trustees were appointed in their places, and the last person to be appointed was Tom Lamonby. He survived his co-trustee and died in 1905, having appointed executors . . . Sect. 30 of the Conveyancing Act, 1881, after providing that a trust estate shall, on the death of the trustee, vest in his legal personal representatives, provides that 'the personal representatives, for the time being, of the deceased, shall be deemed in law his heirs and assigns, within the meaning of all trusts and powers.' So the executors of Tom Lamonby, who was the trustee of the father's will, are to be deemed the heirs and assigns of Tom Lamonby. His executors not only proved his will, but accepted the trusts of Nesfield Robison's will, and acted therein for more than twelve months before the testatrix's death. Then the testatrix appointed the person or persons who at her death should be trustees of her father's will. I hold, therefore, that the executors of Tom Lamonby, being at the testatrix's death trustees of her father's will, were duly appointed and are trustees of her will, and I cannot appoint new trustees in their place.

Although, in general terms, there is no restriction on how many or how few trustees the settlor may appoint, it is common in most cases to appoint more than one trustee – the justification for this being that a plurality of trustees means that, in principle at least, each trustee will act as a safeguard to prevent fraudulent or negligent conduct by the other. On the other hand, an unlimited number of trustees is also viewed as being undesirable. Because the trustees (with the exception of charitable trustees) must act unanimously,[11] it is likely that an excessively large number of trustees would make this unanimity unnecessarily difficult.

Accordingly, in relation to settlements and trusts of land, the Trustee Act 1925, s.34(2)(a) restricts the number of trustees to a maximum of four. There is no lower limit,

[11] *Luke v South Kensington Hotel Company* (1879) 11 ChD 121.

although a sole trustee cannot give a valid receipt for any money he or she receives under the trust such as, for example any money received from the buyer under a contract for the sale of the land (Trustee Act 1925, s.14(2)). This author suggests that these restrictions probably represent the optimum number of trustees for most types of trust as being between two and four, although there may be specific situations where a sole trustee or a larger number of trustees may be preferred. For example, a charitable trust may benefit from being administered by a board of trustees, all of whom may have different specialisms, whereas a simple will with a small number of beneficiaries, all or most of whom are closely related, may not require more than one trustee.

EXTRACT

Trustee Act 1925, s.34

34 Limitation of the number of trustees

(1) Where, at the commencement of this Act, there are more than four trustees of a settlement of land, or more than four trustees holding land on trust for sale, no new trustees shall (except where as a result of the appointment the number is reduced to four or less) be capable of being appointed until the number is reduced to less than four, and thereafter the number shall not be increased beyond four.

(2) In the case of settlements and dispositions [creating trusts of land] made or coming into operation after the commencement of this Act –

(a) the number of trustees thereof shall not in any case exceed four, and where more than four persons are named as such trustees, the four first named (who are able and willing to act) shall alone be the trustees, and the other persons named shall not be trustees unless appointed on the occurrence of a vacancy;

(b) the number of the trustees shall not be increased beyond four.

(3) This section only applies to settlements and dispositions of land, and the restrictions imposed on the number of trustees do not apply –

(a) in the case of land vested in trustees for charitable, ecclesiastical, or public purposes; or

(b) where the net proceeds of the sale of the land are held for like purposes; or

(c) to the trustees of a term of years absolute limited by a settlement on trusts for raising money, or of a like term created under the statutory remedies relating to annual sums charged on land.

Power of trustees to give receipts

(1) The receipt in writing of a trustee for any money, securities, [investments] or other personal property or effects payable, transferable, or deliverable to him under any trust or power shall be a sufficient discharge to the person paying, transferring, or delivering the same and shall effectually exonerate him from seeing to the application or being answerable for any loss or misapplication thereof.

(2) this section does not, except where the trustee is a trust corporation, enable a sole trustee to give a valid receipt for –

[(a) proceeds of sale or other capital money arising under a trust of land;]

(b) capital money arising under the Settled Land Act 1925.

(3) This section applies notwithstanding anything to the contrary in the instrument, if any, creating the trust.

Appointment by selection

Trustees may also be appointed, in the same way as a person is appointed to a post. A judicial trustee for example is appointed by the Chancery division of the High Court.[12] Charitable trusts and pension trusts will also have a deliberate policy of appointment, whereby specific persons are appointed to be trustees for the charity or for the pension fund, and it is likely, particularly in the case of the larger, nationwide charities, the trustees will be professionally qualified and remunerated for their services. Smaller charitable trusts however may rely on volunteers to act as trustees.

Appointment by transfer of the trust property

Where trusts are created by transferral of the trust property to the trustee, again it will be clear who the trustee is, and again, it is probable that the trustee's consent to the appointment will have been given before the transfer of the property. However, in this context, it is important to ensure that the settlor's intention is clearly manifested and that there is no uncertainty as to the fact that the property is transferred to the recipient qua trustee rather than as a donee of a gift.

Appointment by the operation of law

A person may become a trustee through the operation of law. In this situation, unless the statute requires that the trustee consents to the appointment, a person will become a trustee simply through operation of law. For example, where two people co-own land, they will automatically be trustees of that land for their own benefit and for the benefit of the other co-owner by virtue of s.36 Law of Property Act 1925.

EXTRACT

Law of Property Act 1925, s.36

Joint tenancies

(1) Where a legal estate (not being settled land) is beneficially limited to or held in trust for any persons as joint tenants, the same shall be held [in trust], in like manner as if the persons beneficially entitled were tenants in common, but not so as to sever their joint tenancy in equity.

A person may also become a trustee through the operation of law more generally. For example, where property is vested in a person because there is no legally constituted trustee, then they will acquire the status of a trustee. An example may arise where a person dies and their property vests in their personal representative under s.33 Administration of Estates Act 1925.

A person may also be construed as a trustee where he or she has acquired trust property in circumstances which require him or her to hold it upon the trust. Therefore, where a trust fails, such as where the beneficiary dies before the settlor, the trustee will be regarded as a trustee for the estate of the settlor, even though this has not been specifically explained in the trust.

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[12] Judicial Trustees Act 1896, s.2.

The concept of the trustee *de son tort* is also recognised as being a form of constituting a person as a trustee. In this situation, the trustee has either intermeddled with the trust property, or has acted as though he or she is the trustee, and is therefore treated as having entered into the relationship of trustee.

However, the court or the trustees may also appoint trustees. Section 41 of the Trustee Act 1925 permits the court to appoint a trustee where it considers it expedient to do so, such as where a trustee is vetoing proposed actions unreasonably. The trustees may also appoint additional or replacement trustees, in accordance with s.36 or s.37 Trustee Act 1925.

Accepting and declining the office of trustee

Despite the trustee being essential to the trust relationship in that if there is no separation between the legal and the equitable owner, there can be no trust, the trust will not fail for want of a trustee. This will not be an issue where the trust arises through the operation of law, but may be an issue in the situation where the trustee is appointed either by the court or by the settlor. One possibility is that the trustee declines to undertake the obligation, while another possibility is that the trustee either dies or becomes incapable of fulfilling the trust relationship.

In such a situation, the settlor may have specified the appropriate procedure for appointing replacement trustees. Under a will, for example, it is common to appoint partners within the firm of solicitors that was retained to draft the will to act as the trustees. However, standard will precedents will define this as being the partners of the firm at the time of the testator's death, or if the firm has been taken over or incorporated into another business, then the partners of that business will act as the trustees. Below is an example of a will precedent from *Williams on Wills* that explains this obligation:

EXTRACT

Williams on Wills: Form B3.9 Appointment of future partners in a solicitors' firm as executors and trustees

(a) As executors of this will I appoint the partners at the date of my death in the firm of [name of firm] of [address] or the firm which at that date has succeeded to and carries on its practice including a firm which has been incorporated or has formed a limited liability partnership [and I express the wish that no more than two of them shall prove the will and that [name] if then a partner [or an employee of the firm or any successor thereto] should be one of them].

(b) In this clause the expression 'partners' includes any [employees described or held out as partners] directors members or beneficial owners of the firm or any successor thereto.

(c) As trustees of this will I appoint the persons who take out a grant of probate [not being a grant limited to settled land] by virtue of the foregoing appointment of executors.

(d) The expression 'my trustees' in this my will means my personal representatives and the trustees of this will from time to time (whether original or substituted) but after there has been a grant of probate or letters of administration in respect of my estate [(other than a grant limited to settled land)] it shall not include, by virtue of the foregoing appointment of executors, any person appointed an executor who for the time being has not proved this will.

Source: Sherrin, C.H. *et al.* (2002) *Williams on Wills,* 8th ed. Butterworth-Heinemann: Oxford.

In the absence of such alternative arrangements being made however, the court will appoint a judicial trustee.

Nevertheless, what may appear to be a failure to appoint a trustee may in fact be a failure of intention or subject matter. For example if the settlor purports to create a trust by transferring the trust property to unnamed beneficiaries, this is not a case where a valid trust fails for want of a trustee. Instead, the transaction is a nullity – there can be no transfer of property if the trustees are not identified. Therefore whatever the settlor's intentions may have been, his or her conduct does not accord with that intention – the trust is not completely constituted. Similarly, under a secret trust (discussed further in Chapter 15), where the secret trustee dies before the settlor, the trust fails not through the absence of a trustee but because there has been no effective transfer of the trust property to the trustee – the failure is one of subject matter, not an absence of a trustee.

The trustee assumes the obligation of the trust from the moment of express or implied acceptance or designation as trustee. When the trustee accepts the obligation, the trust property vests in him or her (subject to the intervention of third parties, such as HM Land Registry effecting the transfer of land through the amendment of the Land Register) and the trustee then has the duties and the obligations associated with trusteeship from that point onwards.

Nevertheless, where the trustee is in the situation of being able to accept the obligation (as has been shown, this would not be an issue where the trust arises by operation of law), the trustee is equally in a situation of being able to disclaim the obligation. Strictly, there is no formal mechanism for disclaiming trusteeship, but the case of *Ladbroke v Bleaden* (1852) 16 Jur 630 indicates that a deed of disclaimer is advisable in order to ensure that the purported trustee is not assumed by others to have accepted the obligation. New trustees would then need to be appointed.

Trustees' rights

As is shown in this chapter, the role of the trustee is generally one that is associated with obligation rather than with rights. However, under a trust, some rights are afforded to the trustee. These are as follows:

Right to be reimbursed for expenses incurred

The trustee has the right to be reimbursed from the trust fund under s.31 Trustee Act 2000[13] for expenses that have been incurred. Note that this is different from remuneration for the work undertaken. Ordinarily, the trustee is not entitled to be remunerated for his or her work, unless this is authorised by either the trust instrument or by the beneficiary, or exceptionally by the court. It is therefore common for professionally drafted wills, where a solicitor is appointed as trustee, to include a remuneration clause. Nevertheless, s.28 Trustee Act 2000 does allow a professional trustee to be remunerated for his or her work, irrespective of what the trust states. However, even if the trustee is not entitled to receive remuneration for his or her work, the trustee may be reimbursed for expenses that have been incurred in the operation of the trust[14] (such as obtaining legal advice for example)[15] as well as the expenses incurred in effecting the trustee's appointment to trusteeship

[13] Trustee Act 2000 (2000 c.29).
[14] Trustee Act 2000, s.31.
[15] *Macnamara v Jones* (1784) 2 Dick 587.

(such as, for example the fee imposed by HM Land Registry for effecting a change to the proprietorship register so as to render the trustee the registered proprietor of trust land).[16]

Agents are also entitled to receive remuneration for the work they undertake on behalf of the trust.[17] It is also possible that the trustees may be entitled to be indemnified for losses incurred by an agent in relation to property abroad, provided that the agent was appointed prior to 1 February 2001, when the Trustee Act 2000 came into force. Agents appointed before this date continue to be governed by s.23 Trustee Act 1925, where this indemnity is contained. Furthermore, the trustee is entitled to an equitable lien (discussed further in Chapter 25) over trust property in respect of which the trustee has spent money either in insuring or repairing.[18]

Right to be protected from liability for rent or breach of covenant that arises after the trust estate has been distributed

Where the trust comprises of land, the trustee will not be liable for any rent arrears or any breach of covenant that arises after the estate has been distributed. This is contained in s.26 Trustee Act 1925. Ordinarily, a person is liable for a breach of a covenant or a lease even after he or she has transferred the lease,[19] but a trustee is able to avoid this liability.

Right to be protected from omitting a person from the list of beneficiaries

Where the trustees intend to distribute the trust property in circumstances where there are or may be beneficiaries of which the trustees are not aware, the trustees will not be liable if they distribute the fund and a beneficiary of whom they have had no notice later claims to be entitled to a portion of the fund. However, the trustees must place an advertisement in the *London Gazette*[20] and in the local newspaper for the area in which the trust property is situated. If no beneficiary has come forward within a period of two months from the date of the notice, the trust fund may be distributed, and the trustee will not be liable if a beneficiary later comes forward. This requirement is not likely to be necessary in cases involving express trusts. However, they may be useful in situations where, for example a trustee in bankruptcy is attempting to locate creditors, or where a person administering a deceased intestate's estate is trying to ascertain whether there are any eligible beneficiaries who have not been identified. This is contained in s.27 Trustee Act 1925.

Trustees' duties

The trustee has significant obligations under a trust. Accordingly, this section will explain the duties owed by the trustee to the trust. These originate from a combination of common law and statute.

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[16] *Harvey v Olliver* [1887] WN 149.
[17] Trustee Act 2000, s.32.
[18] *Clack v Holland* (1854) 19 Beav 262.
[19] See for example the provisions of the Landlord and Tenants (Covenants) Act 1995.
[20] The *London Gazette* is the official newspaper of record.

Common law

A trustee's primary duty is to use the diligence and prudence expected of an ordinary person of business in the conduct of trust affairs, as Lord Hardwicke LC confirms in *Charitable Corporation v Sutton* (1742) 2 Atk 400 at 406. A trust corporation or an individual who holds him- or herself out as having a specialism in the operation of trusts will be held to a higher standard than the layperson. As is shown from the fact that the decision in *Charitable Corporation v Sutton* dates from 1742, the character of the trustee's duty has a long history. However, in *Bartlett v Barclays Bank* [1980] Ch 515, an outline of the trustee's duties under the contemporary common law is provided.

EXTRACT

Bartlett v Barclays Bank [1980] Ch 515

Case facts

A trust company was set up. The banking department of Barclays Bank was identified as the trustee. However, no representative of the trustee was a member of the board of directors. Neither did the board of directors include a representative of the beneficiaries of the trust. The board of directors invested the trust company's assets in a scheme that proved to be unsuccessful. The claimant beneficiaries therefore sued the trustee company for the loss they had sustained by the fact that the trustees had permitted the company to invest the trust fund in this way.

Brightman LJ

What, then, was the duty of the bank and did the bank fail in its duty? It does not follow that because a trustee could have prevented a loss it is therefore liable for the loss. The questions which I must ask myself are (1) What was the duty of the bank as the holder of 99.8 per cent of the shares in BTL and BTH? (2) Was the bank in breach of duty in any and if so what respect? (3) If so, did that breach of duty cause the loss which was suffered by the trust estate? (4) If so, to what extent is the bank liable to make good that loss? In approaching these questions, I bear in mind that the attack on the bank is based, not on wrongful acts, but on wrongful omissions, that is to say, non-feasance not misfeasance.

The cases establish that it is the duty of a trustee to conduct the business of the trust with the same care as an ordinary prudent man of business would extend towards his own affairs: *In re Speight* (1883) 22 Ch.D. 727, per Sir George Jessel M.R. at p. 739 and Bowen L.J. at p. 762; affirmed on appeal, *Speight v. Gaunt* (1883) 9 App.Cas. 1, and see Lord Blackburn at p. 19. In applying this principle, Lindley L.J. (who was the third member of the court in the *Speight* case) added in *In re Whiteley* (1886) 33 Ch.D. 347, 355:

> 'care must be taken not to lose sight of the fact that the business of the trustee, and the business which the ordinary prudent man is supposed to be conducting for himself, is the business of investing money for the benefit of persons who are to enjoy it at some future time, and not for the sole benefit of the person entitled to the present income. The duty of a trustee is not to take such care only as a prudent man would take if he had only himself to consider; the duty rather is to take such care as an ordinary prudent man would take if he were minded to make an investment for the benefit of other people for whom he felt morally bound to provide. That is the kind of business the ordinary prudent man is supposed to be engaged in; and unless this is borne in mind the standard of a trustee's duty will be fixed too low; lower than it has ever yet been fixed, and lower certainly than the House of Lords or this Court endeavoured to fix it in *Speight v. Gaunt*.'

See on appeal *Learoyd v. Whiteley* (1887) 12 App.Cas. 727, where Lord Watson added, at p. 733:

> 'Business men of ordinary prudence may, and frequently do, select investments which are more or less of a speculative character; but it is the duty of a trustee to confine himself to the class of investments which are permitted by the trust, and likewise to avoid all investments of that class which are attended with hazard.'

That does not mean that the trustee is bound to avoid all risk and in effect act as an insurer of the trust fund: see Bacon V.-C. in *In re Godfrey* (1883) 23 Ch.D. 483, 493:

> 'No doubt it is the duty of a trustee, in administering the trusts of a will, to deal with property intrusted into his care exactly as any prudent man would deal with his own property. But the words in which the rule is expressed must not be strained beyond their meaning. Prudent businessmen in their dealings incur risk. That may and must happen in almost all human affairs.'

The distinction is between a prudent degree of risk on the one hand, and hazard on the other. Nor must the court be astute to fix liability upon a trustee who has committed no more than an error of judgment, from which no business man, however prudent, can expect to be immune: see Lopes L.J. in *In re Chapman* [1896] 2 Ch. 763, 778:

> 'A trustee who is honest and reasonably competent is not to be held responsible for a mere error in judgment when the question which he has to consider is whether a security of a class authorized, but depreciated in value, should be retained or realized, provided he acts with reasonable care, prudence, and circumspection.'

If the trust had existed without the incorporation of BTL, so that the bank held the freehold and leasehold properties and other assets of BTL directly upon the trusts of the settlement, it would in my opinion have been a clear breach of trust for the bank to have hazarded trust money upon the Old Bailey development project in partnership with Stock Conversion. The Old Bailey project was a gamble, because it involved buying into the site at prices in excess of the investment values of the properties, with no certainty or probability, with no more than a chance, that planning permission could be obtained for a financially viable redevelopment, that the numerous proprietors would agree to sell out or join in the scheme, that finance would be available upon acceptable terms, and that the development would be completed, or at least become a marketable asset, before the time came to start winding up the trust. However one looks at it, the project was a hazardous speculation upon which no trustee could properly have ventured without explicit authority in the trust instrument. I therefore hold that the entire expenditure in the Old Bailey project would have been incurred in breach of trust, had the money been spent by the bank itself. The fact that it was a risk acceptable to the board of a wealthy company like Stock Conversion has little relevance.

I turn to the question, what was the duty of the bank as the holder of shares in BTL and BTH? I will first answer this question without regard to the position of the bank as a specialist trustee, to which I will advert later. The bank, as trustee, was bound to act in relation to the shares and to the controlling position which they conferred, in the same manner as a prudent man of business. The prudent man of business will act in such manner as is necessary to safeguard his investment. He will do this in two ways. If facts come to his knowledge which tell him that the company's affairs are not being conducted as they should be, or which put him on inquiry, he will take appropriate action. Appropriate action will no doubt consist in the first instance of inquiry of and consultation with the directors, and in the last but most unlikely resort, the convening of a general meeting to replace one or more directors. What the prudent man of business will not do is to content himself with the receipt of such information on the affairs of the company as a shareholder ordinarily receives at annual general meetings. Since he has the

power to do so, he will go further and see that he has sufficient information to enable him to make a responsible decision from time to time either to let matters proceed as they are proceeding, or to intervene if he is dissatisfied . . . So far, I have applied the test of the ordinary prudent man of business. Although I am not aware that the point has previously been considered, except briefly in *In re Waterman's Will Trusts* [1952] 2 All E.R. 1054, I am of opinion that a higher duty of care is plainly due from someone like a trust corporation which carries on a specialised business of trust management. A trust corporation holds itself out in its advertising literature as being above ordinary mortals. With a specialist staff of trained trust officers and managers, with ready access to financial information and professional advice, dealing with and solving trust problems day after day, the trust corporation holds itself out, and rightly, as capable of providing an expertise which it would be unrealistic to expect and unjust to demand from the ordinary prudent man or woman who accepts, probably unpaid and sometimes reluctantly from a sense of family duty, the burdens of a trusteeship. Just as, under the law of contract, a professional person possessed of a particular skill is liable for breach of contract if he neglects to use the skill and experience which he professes, so I think that a professional corporate trustee is liable for breach of trust if loss is caused to the trust fund because it neglects to exercise the special care and skill which it professes to have.

Outcome

Accordingly, Barclays Bank was found to have acted in breach of trust.

The judgment in *Bartlett v Barclays Bank* demonstrates the expectations surrounding the duties of the trustee. For example, it is important to note that Brightman LJ emphasises that not all loss occasioned by the trust is actionable, and that an ordinary prudent person of business will sometimes sustain a loss despite the prudence of his or her conduct. In such cases, the loss will be said to lie where it falls – the beneficiaries cannot sue where the loss has been sustained despite the trustee having acted as diligently as the law expects of him or her.

Brightman LJ proceeds to explain that the trustee's duty however is an onerous one – a greater duty is owed than merely accepting the information that is provided. Brightman LJ therefore explains that there is a duty to take an interest in the affairs of the trust, and to investigate the activities undertaken. The trustee cannot therefore be passive in the administration of the trust. Nevertheless, Brightman LJ concedes that the family trustee will often undertake the obligation of the trust out of a sense of familial duty, and will not necessarily have an in-depth commercial expertise. This was not the case with the defendants in this case. The trustee was a bank – an organisation whose entire *raison d'être* is investments. The investment of assets was its specialism. The trustee's failure therefore to investigate the board of directors' investment activities was especially culpable – more so than it would have been if the trustee had been a layperson who had no specialist knowledge regarding the law of trusts. *Bartlett v Barclays Bank* therefore provides an indication of why a higher standard is expected of professional trustees.

A trustee has a duty to act in good conscience.[21] There is a sense in this of needing to act honestly and diligently, and not allowing conflicts of interest to arise between the trustee and the trust. The duty of good conscience generally means acting honestly, and acknowledging the importance of service in the interests of the trust – a trust should not be used as a means of promoting or facilitating self-interest.

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[21] *Re Cockburn's Will Trust* [1957] 3 WLR 212.

The trustees are expected to act jointly.[22] Accordingly, responsibility cannot be imposed on one trustee for what should have been the action of all the trustees acting collectively. This is advantageous for the beneficiary in that they can take action against the trustees collectively for any breach of the trust. This means that if one trustee is unable to compensate the beneficiaries for the losses sustained by the trust, the loss may be recovered from the other trustees.

The Trustee Act 2000

While the case of *Bartlett v Barclays Bank* explains the general nature of the trustee's obligation to the trust, in relation to certain of the trustee's functions (namely investments, the acquisition of land, the appointment and supervision of agents, the compounding of liabilities, insurance, reversionary interests, and valuations and audit of the trust property), this common law duty has however been redefined under s.1 Trustee Act 2000. The Trustee Act 2000 duty will not apply if it appears from the trust instrument that the settlor did not intend for the statutory duty to apply. The statutory duty does not therefore supersede the common law duty, but instead operates alongside and in addition to the common law duty. The common law provides the foundational benchmark, and the Act overlaps this in relation to specific aspects of the trust's administration.

EXTRACT

Trustee Act 2000, s.1

1 The duty of care

(1) Whenever the duty under this subsection applies to a trustee, he must exercise such care and skill as is reasonable in the circumstances, having regard in particular –

(a) to any special knowledge or experience that he has or holds himself out as having, and

(b) if he acts as trustee in the course of a business or profession, to any special knowledge or experience that it is reasonable to expect of a person acting in the course of that kind of business or profession.

(2) In this Act the duty under subsection (1) is called 'the duty of care'.

EXTRACT

Trustee Act 2000, Schedule 1 Application of duty of care

Investment

1

The duty of care applies to a trustee –

(a) when exercising the general power of investment or any other power of investment, however conferred;

[22] *Luke v South Kensington Hotel Co* (1879) 11 Ch D 121.

(b) when carrying out a duty to which he is subject under section 4 or 5 (duties relating to the exercise of a power of investment or to the review of investments).

Acquisition of land

2

The duty of care applies to a trustee-

(a) when exercising the power under section 8 to acquire land;

(b) when exercising any other power to acquire land, however conferred;

(c) when exercising any power in relation to land acquired under a power mentioned in sub-paragraph (a) or (b).

Agents, nominees and custodians

3

(1) The duty of care applies to a trustee-

(a) when entering into arrangements under which a person is authorised under section 11 to exercise functions as an agent;

(b) when entering into arrangements under which a person is appointed under section 16 to act as a nominee;

(c) when entering into arrangements under which a person is appointed under section 17 or 18 to act as a custodian;

(d) when entering into arrangements under which, under any other power, however conferred, a person is authorised to exercise functions as an agent or is appointed to act as a nominee or custodian;

(e) when carrying out his duties under section 22 (review of agent, nominee or custodian, etc.).

(2) For the purposes of sub-paragraph (1), entering into arrangements under which a person is authorised to exercise functions or is appointed to act as a nominee or custodian includes, in particular-

(a) selecting the person who is to act,

(b) determining any terms on which he is to act, and

(c) if the person is being authorised to exercise asset management functions, the preparation of a policy statement under section 15.

Compounding of liabilities

4

The duty of care applies to a trustee-

(a) when exercising the power under section 15 of the Trustee Act 1925 to do any of the things referred to in that section;

(b) when exercising any corresponding power, however conferred.

Insurance

5

The duty of care applies to a trustee-

(a) when exercising the power under section 19 of the Trustee Act 1925 to insure property;

(b) when exercising any corresponding power, however conferred.

Reversionary interests, valuations and audit

6

The duty of care applies to a trustee-

(a) when exercising the power under section 22(1) or (3) of the Trustee Act 1925 to do any of the things referred to there;

(b) when exercising any corresponding power, however conferred.

Exclusion of duty of care

7

The duty of care does not apply if or in so far as it appears from the trust instrument that the duty is not meant to apply.

The statutory duty of care requires the trustee to exercise '*such skill and care as is reasonable in the circumstances*' – essentially adopting the standards that have been adopted and refined in the law of torts. The Act specifies that regard will be given to '*any special knowledge or experience that he has or holds himself out as having*' and also to the fact that if a person is acting in the course of a business or a profession, then the trustee is deemed to have '*any special knowledge or experience that it is reasonable to expect of a person acting in the course of that kind of business or profession*.' This means that the self-confident law student who professes to have a greater expertise than members of his or her family will be held to a higher standard of care than the person who has received no education in law. Notice that not only is the person who actually possesses special knowledge or experience held to a higher standard of care, but that the person who holds him- or herself out as having special knowledge or experience is also expected to meet a higher standard of care. Professional trustees are also expected to owe a higher standard of care.

Therefore trustees who work in professions such as banking or law will be held to a higher standard of care than those in professions where the office of trusteeship does not feature. Therefore, the solicitor will owe a higher standard of care than the school-teacher, even if the solicitor does not specialise in the law of trusts.

The duty of care applies in relation to investments; the acquisition of land; the appointment and supervision of agents, nominees and custodians; the compounding of liabilities insurance; as well as to the reversionary interests and to the valuation and auditing of trust assets.

Trustee investments

The statutory duty of care described above is owed either when the trustee is exercising the general power of investment, or when the trustee is exercising a duty to which s.4 or s.5 Trustee Act 2000 applies. The general power of investment is the term used in s.3 Trustee Act 2000 to allow the trustee to invest trust property in the same way as the absolute owner would. Prior to the 2000 Act, a trustee could only invest in a fairly narrow range of investments, and a proportion of the fund had to be invested in schemes where the original sum at least was guaranteed, such as bank or building society savings accounts (Trustee Investments Act 1961 (1961 c.62)). The difficulty with such an approach was that although the trust fund was secure, there was very little scope for the fund to make significant gains. Accordingly, the Trustee Act 2000 permits trustees to invest in anything in which the owner could invest in. However, the duty of care exists in order to

ensure that the trustee does not act capriciously or foolishly in the way one could with one's own money. Therefore, while one could use £1 million to buy 100 million penny sweets with one's own money, such an 'investment' as a trustee would be in breach of the duty of care, because he or she is unlikely to be exercising 'reasonable skill or care' by using the trust fund to purchase a wasting asset that has very little by way of resale value. Not all trust property is capable of being invested. Chattels for example cannot sensibly be the subject of investment, and the trustee's role in this respect would be to safeguard the property as opposed to investing it.

EXTRACT

Trustee Act 2000, s.3

3 General power of investment

(1) Subject to the provisions of this Part, a trustee may make any kind of investment that he could make if he were absolutely entitled to the assets of the trust.

(2) In this Act the power under subsection (1) is called 'the general power of investment'.

(3) The general power of investment does not permit a trustee to make investments in land other than in loans secured on land (but see also section 8).

(4) A person invests in a loan secured on land if he has rights under any contract under which-

(a) one person provides another with credit, and

(b) the obligation of the borrower to repay is secured on land.

(5) 'Credit' includes any cash loan or other financial accommodation.

(6) 'Cash' includes money in any form.

If the trustee does invest the trust fund, he or she must have regard to what is termed the standard investment criteria. The standard investment criteria as defined by s.4 relates to the considerations that the trustee must apply when deciding how to invest the trust fund.

EXTRACT

Trustee Act 2000, s.4

4 Standard investment criteria

(1) In exercising any power of investment, whether arising under this Part or otherwise, a trustee must have regard to the standard investment criteria.

(2) A trustee must from time to time review the investments of the trust and consider whether, having regard to the standard investment criteria, they should be varied.

(3) The standard investment criteria, in relation to a trust, are–

(a) the suitability to the trust of investments of the same kind as any particular investment proposed to be made or retained and of that particular investment as an investment of that kind, and

(b) the need for diversification of investments of the trust, in so far as is appropriate to the circumstances of the trust.

The first aspect to consider is the duty to review the investments. Therefore, the trustee cannot simply invest the trust fund in a savings account and forget about it. Instead, the trustee must consider whether the investments continue to be the most appropriate for the fund. For example, share prices may vary over time, and therefore investments that are considered appropriate when the trust is established may become less suitable over time. Similarly, bank and building society accounts may offer introductory rates with high rates of interest, but once the introductory period has lapsed, the bank or building society may simply transfer the funds to an account that earns very little or no interest. Therefore, part of the trustee's duty is to review the investments.

A further issue to consider according to s.4 is the suitability of the investment, or of investments of that kind for the trust. This encompasses many issues. Firstly, it is necessary to consider the nature of the trust. At one end of the spectrum, the trust in question may be the short-term administration of a will before the trust is distributed to adult beneficiaries. In this situation, where the trust may only last for a matter of weeks between the date of the deceased's death and the distribution of the estate, long-term investments would not be suitable. At the other end of the spectrum, there are charitable trusts, or trusts for the benefit of infant beneficiaries, which may need to be invested over lengthy periods. Here, short-term investment schemes, such as an instant access savings account would not be suitable investments for the trust.

A related issue is the nature of the beneficiaries. If there are beneficiaries who are entitled to receive the income of the trust fund (such as those who have a life interest) then it is necessary to ensure that the investment is of a type that will generate an income. For example, some types of investment scheme may offer long-term gain, but only if the fund is invested over a long period of time. This will not therefore benefit the beneficiary under a life interest, and therefore the trustee would need to consider whether such an investment is necessarily suitable for trusts where there are life interests as well as beneficiaries who are entitled to the capital.

The second aspect of the standard investment criteria is to consider the suitability of the particular proposed investment. It is likely to be imprudent to invest in several investments that are similar in character, such as only investing in certain types of asset, such as internet service companies. A further consideration that may apply in relation to charities is whether the investment is suitable for the trust. Although the case of *Cowan v Scargill* [1985] Ch 270 confirms that the trustees' primary consideration should be financial gain, rather than the trustees' own ethical standpoint, in *Harries v Church Commissioners for England* [1993] 2 All ER 300 it was conceded that the trustees should not invest in schemes that are completely contrary to the trust's objectives. This is likely to be particularly relevant in relation to charities, where for example investing in a tobacco company would be entirely unsuitable where the trustees are acting for a lung cancer charity. Accordingly, it is important to diversify the type of commodity in which the trustees invest.

EXTRACT

Cowan v Scargill [1985] Ch 270

Case facts

The National Coal Board set up a mineworkers' pension fund with extensive investment powers. However, five of the trustees objected to some of the proposed investments on ethical grounds. They argued that investing in oil was contrary to the objectives of a coalworkers' pension fund, and that foreign investments were also contrary to the policy of the trade union they represented.

Megarry VC

The starting point is the duty of trustees to exercise their powers in the best interests of the present and future beneficiaries of the trust, holding the scales impartially between different classes of beneficiaries. This duty of the trustees towards their beneficiaries is paramount. They must, of course, obey the law; but subject to that, they must put the interests of their beneficiaries first. When the purpose of the trust is to provide financial benefits for the beneficiaries, as is usually the case, the best interests of the beneficiaries are normally their best financial interests. In the case of a power of investment, as in the present case, the power must be exercised so as to yield the best return for the beneficiaries, judged in relation to the risks of the investments in question; and the prospects of the yield of income and capital appreciation both have to be considered in judging the return from the investment.

The legal memorandum that the union obtained from their solicitors is generally in accord with these views. In considering the possibility of investment for 'socially beneficial reasons which may result in lower returns to the fund,' the memorandum states that 'the trustees' only concern is to ensure that the return is the maximum possible consistent with security'; and then it refers to the need for diversification. However, it continues by saying:

> 'Trustees cannot be criticised for failing to make a particular investment for social or political reasons, such as in South African stock for example, but may be held liable for investing in assets which yield a poor return or for disinvesting in stock at inappropriate times for non-financial criteria.'

This last sentence must be considered in the light of subsequent passages in the memorandum which indicate that the sale of South African securities by trustees might be justified on the ground of doubts about political stability in South Africa and the long-term financial soundness of its economy, whereas trustees could not properly support motions at a company meeting dealing with pay levels in South Africa, work accidents, pollution control, employment conditions for minorities, military contracting and consumer protection. The assertion that trustees could not be criticised for failing to make a particular investment for social or political reasons is one that I would not accept in its full width. If the investment in fact made is equally beneficial to the beneficiaries, then criticism would be difficult to sustain in practice, whatever the position in theory. But if the investment in fact made is less beneficial, then both in theory and in practice the trustees would normally be open to criticism.

This leads me to the second point, which is a corollary of the first. In considering what investments to make trustees must put on one side their own personal interests and views. Trustees may have strongly held social or political views. They may be firmly opposed to any investment in South Africa or other countries, or they may object to any form of investment in companies concerned with alcohol, tobacco, armaments or many other things. In the conduct of their own affairs, of course, they are free to abstain from making any such investments. Yet under a trust, if investments of this type would be more beneficial to the beneficiaries than other investments, the trustees must not refrain from making the investments by reason of the views that they hold.

Trustees may even have to act dishonourably (though not illegally) if the interests of their beneficiaries require it. Thus where trustees for sale had struck a bargain for the sale of trust property but had not bound themselves by a legally enforceable contract, they were held to be under a duty to consider and explore a better offer that they received, and not to carry through the bargain to which they felt in honour bound: *Buttle* v. *Saunders* [1950] 2 All E.R. 193. In other words, the duty of trustees to their beneficiaries may include a duty to 'gazump,' however honourable the trustees. As Wynn-Parry J. said at p. 195, trustees 'have an overriding duty to obtain the best price which they can for their beneficiaries.' In applying this to an official

receiver in *In re Wyvern Developments Ltd.* [1974] 1 W.L.R. 1097, 1106, Templeman J. said that he 'must do his best by his creditors and contributories. He is in a fiduciary capacity and cannot make moral gestures, nor can the court authorise him to do so.' . . .

Third, by way of caveat I should say that I am not asserting that the benefit of the beneficiaries which a trustee must make his paramount concern inevitably and solely means their financial benefit, even if the only object of the trust is to provide financial benefits. Thus if the only actual or potential beneficiaries of a trust are all adults with very strict views on moral and social matters, condemning all forms of alcohol, tobacco and popular entertainment, as well as armaments, I can well understand that it might not be for the 'benefit' of such beneficiaries to know that they are obtaining rather larger financial returns under the trust by reason of investments in those activities than they would have received if the trustees had invested the trust funds in other investments. The beneficiaries might well consider that it was far better to receive less than to receive more money from what they consider to be evil and tainted sources. 'Benefit' is a word with a very wide meaning, and there a circumstances in which arrangements which work to the financial disadvantage of a beneficiary may yet be for his benefit: see, for example, *In re T.'s Settlement Trusts* [1964] Ch. 158 and *In re C.L.* [1969] 1 Ch. 587. But I would emphasise that such cases are likely to be very rare, and in any case I think that under a trust for the provision of financial benefits the burden would rest, and rest heavy, on him who asserts that it is for the benefit of the beneficiaries as a whole to receive less by reason of the exclusion of some of the possibly more profitable forms of investment. Plainly the present case is not one of this rare type of cases. Subject to such matters, under a trust for the provision of financial benefits, the paramount duty of the trustees is to provide the greatest financial benefits for the present and future beneficiaries . . .

In the case before me, it is not in issue that there ought to be diversification of the investments held by the fund. The contention of the defendants, put very shortly, is that there can be a sufficient degree of diversification without any investment overseas or in oil, and that in any case there is no need to increase the level of overseas investments beyond the existing level . . .

I can see no escape from the conclusion that the N.U.M. trustees were attempting to impose the prohibitions in order to carry out union policy; and mere assertions that their sole consideration was the benefit of the beneficiaries do not alter that conclusion . . .

Outcome

Accordingly, the investment scheme had to be put into operation, notwithstanding the trustees' objections.

EXTRACT

Harries v Church Commissioners for England [1993] 2 All ER 300

Case facts

The Church Commissioners for England is a charity, which is required to maintain a fund for paying stipends and housing costs to the clergy. The assets committee had the power to invest the money in the fund, but was permitted to take account of social and ethical issues. Accordingly, it could refrain from investing in matters such as armaments, gambling, alcohol, tobacco or newspapers. The claimants argued however, that the overriding consideration should be the promotion of the Christian faith, and that the trustees should not invest the fund in a way that was incompatible with the Church of England's objectives.

Nicholls VC

. . . prima facie the purposes of the trust will be best served by the trustees seeking to obtain therefrom the maximum return, whether by way of income or capital growth, which is consistent with commercial prudence. That is the starting point for all charity trustees when considering the exercise of their investment powers. Most charities need money; and the more of it there is available, the more the trustees can seek to accomplish.

In most cases this prima facie position will govern the trustees' conduct. In most cases the best interests of the charity require that the trustees' choice of investments should be made solely on the basis of well-established investment criteria, having taken expert advice where appropriate and having due regard to such matters as the need to diversify, the need to balance income against capital growth, and the need to balance risk against return.

In a minority of cases the position will not be so straightforward. There will be some cases, I suspect comparatively rare, when the objects of the charity are such that investments of a particular type would conflict with the aims of the charity. Much-cited examples are those of cancer research charities and tobacco shares, trustees of temperance charities and brewery and distillery shares, and trustees of charities of the Society of Friends and shares in companies engaged in production of armaments. If, as would be likely in those examples, trustees were satisfied that investing in a company engaged in a particular type of business would conflict with the very objects their charity is seeking to achieve, they should not so invest. Carried to its logical conclusion the trustees should take this course even if it would be likely to result in significant financial detriment to the charity. The logical conclusion, whilst sound as a matter of legal analysis, is unlikely to arise in practice. It is not easy to think of an instance where in practice the exclusion for this reason of one or more companies or sectors from the whole range of investments open to trustees would be likely to leave them without an adequately wide range of investments from which to choose a properly diversified portfolio.

There will also be some cases, again I suspect comparatively rare, when trustees' holdings of particular investments might hamper a charity's work either by making potential recipients of aid unwilling to be helped because of the source of the charity's money, or by alienating some of those who support the charity financially. In these cases the trustees will need to balance the difficulties they would encounter, or likely financial loss they would sustain, if they were to hold the investments against the risk of financial detriment if those investments were excluded from their portfolio. The greater the risk of financial detriment, the more certain the trustees should be of countervailing disadvantages to the charity before they incur that risk.

Another circumstance where trustees would be entitled, or even required, to take into account non-financial criteria would be where the trust deed so provides.

No doubt there will be other cases where trustees are justified in departing from what should always be their starting point. The instances I have given are not comprehensive. But I must emphasise that of their very nature, and by definition, investments are held by trustees to aid the work of the charity in a particular way: by generating money. That is the purpose for which they are held. That is their raison d'être. Trustees cannot properly use assets held as an investment for other, viz non-investment, purposes. To the extent that they do they are not properly exercising their powers of investment. This is not to say that trustees who own land may not act as responsible landlords or those who own shares may not act as responsible shareholders. They may. The law is not so cynical as to require trustees to behave in a fashion which would bring them or their charity into disrepute . . . On the other hand, trustees must act prudently. They must not use property held by them for investment purposes as a means for making moral statements at the expense of the charity of which they are trustees. Those who wish may do so with their own property, but that is not a proper function of trustees with trust assets held as an investment.

I should mention one other particular situation. There will be instances today when those who support or benefit from a charity take widely different views on a particular type of investment, some saying that on moral grounds it conflicts with the aims of the charity, others saying the opposite. One example is the holding of arms industry shares by a religious charity. There is a real difficulty here. To many questions raising moral issues there are no certain answers. On moral questions widely differing views are held by well-meaning, responsible people. This is not always so. But frequently, when questions of the morality of conduct are being canvassed, there is no identifiable yardstick which can be applied to a set of facts so as to yield one answer which can be seen to be 'right' and the other 'wrong'. If that situation confronts trustees of a charity, the law does not require them to find an answer to the unanswerable. Trustees may, if they wish, accommodate the views of those who consider that on moral grounds a particular investment would be in conflict with the objects of the charity, so long as the trustees are satisfied that course would not involve a risk of significant financial detriment. But when they are not so satisfied trustees should not make investment decisions on the basis of preferring one view of whether on moral grounds an investment conflicts with the objects of the charity over another. This is so even when one view is more widely supported than the other . . .

It will be seen, therefore, that the commissioners do have an 'ethical' investment policy. They have followed such a policy for many years. Indeed, they have done so ever since they were constituted in 1948. Let me say at once that I can see nothing in this statement of policy which is inconsistent with the general principles I have sought to expound above.

The statement of policy records that the commissioners do not invest in companies whose main business is in armaments, gambling, alcohol, tobacco or newspapers . . . As I understand the position, the commissioners have felt able to exclude these items from their investments despite the conflicting views on the morality of holding these items as investments because there has remained open to the commissioners an adequate width of alternative investments.

I have already indicated that at the heart of the plaintiffs' case is a contention that the commissioners' policy is erroneous in law in that the commissioners are only prepared to take non-financial considerations into account to the extent that such considerations do not significantly jeopardise or interfere with accepted investment principles. I think it is implicit, if not explicit, in the commissioners' evidence that they do regard themselves as constrained in this way. So far as I have been able to see, this is the only issue identifiable as an issue of law raised in these proceedings. In my view this self-constraint applied by the commissioners is not one which in practice has led to any error of law on their part, nor is it likely to do so. I have already indicated that the circumstances in which charity trustees are bound or entitled to make a financially disadvantageous investment decision for ethical reasons are extremely limited. I have noted that it is not easy to think of a practical example of such a circumstance. There is no evidence before me to suggest that any such circumstance exists here . . .

The third aspect to consider is the value of the trust fund. Investment schemes aimed at very wealthy trusts are unlikely to be suitable where the trust property is comparatively small. It must be borne in mind that the law of trusts applies both to small trusts of a deceased individual where the trust property may amount to a few hundred pounds, and to vast charitable trusts whose wealth runs to many millions of pounds. Therefore, the trustees, when applying the standard investment criteria, must consider whether the investment is suitable for the trust property.

Related to this of course is the need to consider what the trust property consists of. Money may of course be invested, but the value of tangible items, such as land or jewellery are not likely to be invested but are likely to be safeguarded in other ways, such as

ensuring that buildings do not fall into disrepair, insuring against loss or damage, and making prudent decisions regarding when to sell the asset.

Section 4(3)(b) of the Trustee Act 2000 contains the next aspect of the standard investment criteria, namely the need for diversification of the fund. Again, this will depend on the value of the trust property, and the duration for which it will last. Therefore, a large trust fund should be invested in a portfolio of different types of investments. There will be a need to consider investing in different companies and different types of commodities, but also to consider investing in some relatively safe schemes, where the original capital will not be lost.

Diversification of investments is also important in relation to trusts where there are beneficiaries with a life interest and beneficiaries with an interest in remainder. The trustee has a duty to ensure that there is no disbenefit to one group of beneficiaries against the other. Therefore, diversification of investments may be a way of ensuring that some investments generate a regular income that will fulfil the trustee's obligation to the beneficiary of the life interest, while other investments may ensure the growth of the capital fund over a longer period, thus benefitting the beneficiary with the interest in remainder.

Despite these requirements, it may nevertheless be the case that the trust fund does not increase in value. However, unless the loss is attributable to the trustees' responsibility, the trustees would not be liable to account for the loss sustained. In the case of *Nestle v National Westminster Bank plc* [1994] 1 All ER 118 for example, Staughton LJ confirms that:

> Of course it is not a breach of trust to invest the trust fund in such a manner that its real value is not maintained. At times that will be impossible, and at others it will require extraordinary skill or luck.

In this case, the trustees had not invested the trust fund in a way that maximised the gains that could have been made. Although the importance of doing so was emphasised, it was also held that it was necessary to prove that the claimant had actually sustained a loss as a result of the trustees' investment policy. The appeal was dismissed because the beneficiary was unable to show that the trust would have made a larger gain if other investments had been undertaken; she was merely able to demonstrate that they could have made a gain. However, in the hearing before the High Court, Hoffmann J explained very saliently the modern rationale behind trustee investments, indicating that there has been a move away from a philosophy of adopting a 'prudent' approach to trust investments to a more modern approach that favours a portfolio theory. Accordingly, although the Victorian approach in *Re Whiteley* (1886) 33 Ch D 347 emphasised the need to act as a prudent person of business would act in the investment of trust assets, Hoffmann J explains in *Nestle v National Westminster Bank PLC* that the modern approach takes into consideration what is called a portfolio theory. What this means is that the trustees should invest a trust fund, especially a large one, in diverse ways, so that one investment that may be viewed as 'risky' (i.e. having significant opportunity for gain despite a significant risk of loss) does not make the whole trust fund risky, because the risk is balanced against safer investments. He explains:

> Modern trustees acting within their investment powers are entitled to be judged by the standards of current portfolio theory, which emphasises the risk level of the entire portfolio rather than the risk attaching to each investment taken in isolation. (This is not to say that losses on investments made in breach of trust can be set off against gains in the rest of the portfolio but only that an investment which in isolation is too risky and therefore in breach of trust may be justified when held in conjunction with other investments.)

In recent years, the individuals and organisations that have made the greatest gains have been those that have taken significant risks. Accordingly, when they were being established, investing in untried ventures (for example a system that allowed you to text messages that the whole world could read, or a system that allowed you to update your friends about what you were doing) may have been regarded as risky. It is likely however that the early investors in what the reader will recognise as Twitter and Facebook may make significant gains from having trusted their assets to a venture that may or may not have succeeded.

Acquisition of land

The statutory duty of care applies when the trustee is acquiring land or when the trustee is exercising any of its powers in relation to land. Section 8 of the Trustee Act 2000 permits the trustee to acquire freehold or leasehold land either as an investment, or in order for a beneficiary to occupy it or, according to s.8(1)(c) for any other reason.

EXTRACT

Trustee Act 2000, s.8

8 Power to acquire freehold and leasehold land

(1) A trustee may acquire freehold or leasehold land in the United Kingdom –

  (a) as an investment,

  (b) for occupation by a beneficiary, or

  (c) for any other reason.

(2) 'Freehold or leasehold land' means –

  (a) in relation to England and Wales, a legal estate in land,

  (b) in relation to Scotland –

    (i) the estate or interest of the proprietor of the dominium utile or, in the case of land not held on feudal tenure, the estate or interest of the owner, or

    (ii) a tenancy, and

  (c) in relation to Northern Ireland, a legal estate in land, including land held under a fee farm grant.

(3) For the purpose of exercising his functions as a trustee, a trustee who acquires land under this section has all the powers of an absolute owner in relation to the land.

When acquiring land and dealing with land, the trustee has the same rights an absolute owner, and can therefore lease the land or use the land as security for a mortgage loan. Of course, just as the owner may sell the land, so too may the trustee sell the land. However, whereas the owner is able to give the land as a gift if he or she chooses, the trustee cannot do this because it would breach the obligation owed by the trustee to the beneficiary, as the trustee's obligation is to safeguard the property for the beneficiary, or to invest the trust fund so as to ensure that the benefit accrues to the beneficiary. Clearly, giving the trust property away as a gift would not fulfil either of these obligations. Included in the trustee's powers regarding land is the power to convey the land to the adult beneficiaries of the trust, even if the trust instrument does not provide for this. This is contained in s.6 Trusts of Land and Appointment of Trustees Act 1996.[23]

[23] (1996 c.47).

EXTRACT

Trusts of Land and Appointment of Trustees Act 1996, s.6

6 General powers of trustees

(1) For the purpose of exercising their functions as trustees, the trustees of land have in relation to the land subject to the trust all the powers of an absolute owner.

(2) Where in the case of any land subject to a trust of land each of the beneficiaries interested in the land is a person of full age and capacity who is absolutely entitled to the land, the powers conferred on the trustees by subsection (1) include the power to convey the land to the beneficiaries even though they have not required the trustees to do so; and where land is conveyed by virtue of this subsection –

(a) the beneficiaries shall do whatever is necessary to secure that it vests in them, and

(b) if they fail to do so, the court may make an order requiring them to do so.

(3) The trustees of land have power to [acquire land under the power conferred by section 8 of the Trustee Act 2000].

(4) . . .

(5) In exercising the powers conferred by this section trustees shall have regard to the rights of the beneficiaries.

(6) The powers conferred by this section shall not be exercised in contravention of, or of any order made in pursuance of, any other enactment or any rule of law or equity.

(7) The reference in subsection (6) to an order includes an order of any court or of the [Charity Commission].

(8) Where any enactment other than this section confers on trustees authority to act subject to any restriction, limitation or condition, trustees of land may not exercise the powers conferred by this section to do any act which they are prevented from doing under the other enactment by reason of the restriction, limitation or condition.

[(9) The duty of care under section 1 of the Trustee Act 2000 applies to trustees of land when exercising the powers conferred by this section.]

The appointment and supervision of agents, nominees and custodians

The trustees have the power to delegate certain functions of the trust. This may be done under a power of attorney whereby the trustee delegates the entire role of trusteeship to an attorney (it should be noted here that an attorney in this sense means a person to whom the decision-making and executive powers are delegated, rather than in the American sense meaning a lawyer). However, the trustee may also appoint agents (s.11), nominees (s.16) and custodians (s.17) to carry out certain functions. One or more of the trustees may fulfil these functions, but the beneficiary cannot act as an agent, nominee or custodian – this is prohibited under s.12(3) Trustee Act 2000.

An agent's role is to enter into contractual relations between the principal, who, in the context of trusts, will be the trustee. Commonly therefore, an agent might be a solicitor, a banker or a stockbroker who is given the authority to buy or sell assets on behalf of the trust. A nominee is a person who has been authorised to submit a report on a proposal for a voluntary arrangement. A custodian is a person who is authorised to keep a document. The most extensive role is that of the agent therefore, who may be authorised to

carry out a wide range of functions on behalf of the principal/trustee. Accordingly, the rest of this section will focus principally on the trustee and the agent.

Where the trust is not a charitable trust, s.11 Trustee Act 2000 provides that an agent may be appointed to carry out any function except functions relating to the distribution of assets, decisions regarding whether the payment of fees should come from income of capital, and the appointment of trustees nominees or custodians. Any other function may be devolved to an agent. However, if asset management functions are delegated, the agreement must be either made or evidenced in writing in accordance with s.15(1) of the Trustee Act 2000, and the trustees must prepare what is termed a policy statement when the agency relationship is created, which sets out the manner in which the trustee must carry out his or her functions (s.15(2)(a)). In essence therefore, the trustee cannot absolve responsibility by placing the administration of the trust in the hands of the agent. Instead, the trustee has an obligation to direct and guide the agent's actions.

However, the delegation of a trustee's functions where the trust is charitable are far more limited, and is restricted to carrying out the trustees decisions, investing assets, raising funds and functions prescribed by an order made by the Secretary of State.

The trustee owes the statutory duty of care when appointing an agent, nominee or custodian, but no duty is owed by the agent, nominee or custodian to the beneficiary, although a duty will be owed to the trustee under the contractual principles governing the law of agency, which are beyond the scope of this book.

The statutory duty of care will apply when the trustee appoints the agent, nominee or custodian, or when reviewing their work, as is provided in s.23 Trustee Act 2000. Accordingly, if the trustee has breached the statutory duty of care in relation to these activities, he or she will be in breach of the trust. A further ground of liability arises where asset management functions have been delegated in that there is a duty to ensure that the policy statement that must be prepared is being complied with, as well as to consider whether it is necessary to revise the policy statement, and in light of that decision, to make the necessary changes if required. Otherwise however, the trustee is not liable for the acts or omissions of the agent, nominee or custodian.

EXTRACT

Trustee Act 2000, s.11

11 Power to employ agents

(1) Subject to the provisions of this Part, the trustees of a trust may authorise any person to exercise any or all of their delegable functions as their agent.

(2) In the case of a trust other than a charitable trust, the trustees' delegable functions consist of any function other than –

(a) any function relating to whether or in what way any assets of the trust should be distributed,

(b) any power to decide whether any fees or other payment due to be made out of the trust funds should be made out of income or capital,

(c) any power to appoint a person to be a trustee of the trust, or

(d) any power conferred by any other enactment or the trust instrument which permits the trustees to delegate any of their functions or to appoint a person to act as a nominee or custodian.

(3) In the case of a charitable trust, the trustees' delegable functions are-

(a) any function consisting of carrying out a decision that the trustees have taken;

(b) any function relating to the investment of assets subject to the trust (including, in the case of land held as an investment, managing the land and creating or disposing of an interest in the land);

(c) any function relating to the raising of funds for the trust otherwise than by means of profits of a trade which is an integral part of carrying out the trust's charitable purpose;

(d) any other function prescribed by an order made by the Secretary of State.

(4) For the purposes of subsection (3)(c) a trade is an integral part of carrying out a trust's charitable purpose if, whether carried on in the United Kingdom or elsewhere, the profits are applied solely to the purposes of the trust and either-

(a) the trade is exercised in the course of the actual carrying out of a primary purpose of the trust, or

(b) the work in connection with the trade is mainly carried out by beneficiaries of the trust.

(5) The power to make an order under subsection (3)(d) is exercisable by statutory instrument which shall be subject to annulment in pursuance of a resolution of either House of Parliament.

EXTRACT

Trustee Act 2000, s.15

15 Asset management: special restrictions

(1) The trustees may not authorise a person to exercise any of their asset management functions as their agent except by an agreement which is in or evidenced in writing.

(2) The trustees may not authorise a person to exercise any of their asset management functions as their agent unless-

(a) they have prepared a statement that gives guidance as to how the functions should be exercised ('a policy statement'), and

(b) the agreement under which the agent is to act includes a term to the effect that he will secure compliance with-

(i) the policy statement, or

(ii) if the policy statement is revised or replaced under section 22, the revised or replacement policy statement.

(3) The trustees must formulate any guidance given in the policy statement with a view to ensuring that the functions will be exercised in the best interests of the trust.

(4) The policy statement must be in or evidenced in writing.

(5) The asset management functions of trustees are their functions relating to-

(a) the investment of assets subject to the trust,

(b) the acquisition of property which is to be subject to the trust, and

(c) managing property which is subject to the trust and disposing of, or creating or disposing of an interest in, such property.

EXTRACT

Trustee Act 2000, s.23

Liability for agents, nominees and custodians etc.

(1) A trustee is not liable for any act or default of the agent, nominee or custodian unless he has failed to comply with the duty of care applicable to him, under paragraph 3 of Schedule 1 –

(a) when entering into the arrangements under which the person acts as agent, nominee or custodian, or

(b) when carrying out his duties under section 22.

(2) If a trustee has agreed a term under which the agent, nominee or custodian is permitted to appoint a substitute, the trustee is not liable for any act or default of the substitute unless he has failed to comply with the duty of care applicable to him, under paragraph 3 of Schedule 1 –

(a) when agreeing that term, or

(b) when carrying out his duties under section 22 in so far as they relate to the use of the substitute.

Compounding liabilities

Compounding liabilities is defined generally in section 15 of the Trustee Act 1925 as meaning the power to:

(a) accept any property, real or personal, before the time at which it is made transferable or payable; or

(b) sever and apportion any blended trust funds or property; or

(c) pay or allow any debt or claim on any evidence that he or they think sufficient; or

(d) accept any composition or any security, real or personal, for any debt or for any property, real or personal, claimed; or

(e) allow any time of payment of any debt; or

(f) compromise, compound, abandon, submit to arbitration, or otherwise settle any debt, account, claim, or thing whatever relating to the testator's or intestate's estate or to the trust;

and for any of these purposes may enter into, give, execute, and do such agreements, instruments of composition or arrangement, releases, and other things as to him or them seem expedient, without being responsible for any loss occasioned by any act or thing so done by him or them.

However, all of these activities will require the trustee to exercise the duty of care. The power to compound liabilities may also arise by other means, for example where this is provided in the trust instrument. Again the duty of care will apply, in accordance with Paragraph 4(b) of Schedule 1 to the Trustee Act 2000.

Safeguarding the trust property

Finally, the statutory duty of care will apply in relation to the trustee's power to insure the trust property under s.19 Trustee Act 1925. As the insurance premiums may be paid out of the trust fund, the trustee is required to exercise the duty of care both in relation

to deciding whether the trust fund should be insured, and in decisions such as valuing the property for insurance purposes. This relates to the trustees' duty to safeguard the trust property. Clearly, the interests of the trust are not best served if the trust property is left to fall into disrepair, or if the trust property is not adequately insured against risk. Accordingly, the trustees have a duty to ensure that the trust property is dealt with in a way that maximises its value.

Fiduciary duty

In addition to the duty of care, the trustee owes a number of other duties in relation to the trust. The first of these is the fiduciary nature of the trustee's duty. The trustee must act in good faith, by acting honestly and diligently, and by not deliberately acting in a way that would cause any breach of trust or any loss to the trust. The trustee must not put him- or herself in a position where personal interest conflicts with those of the beneficiaries, and must not profit from the trust. Accordingly, in the case of *Bristol and West Building Society v Mothew* [1996] 4 All ER 698 the defendant solicitor was found not to have acted in breach of trust, because his misconduct had been entirely inadvertent. Nevertheless, the Court of Appeal did explain what the nature of a trustee's duty to a trust should be. Although the extract reproduced below is lengthy, it provides an excellent outline of the key principles of the fiduciary duty owed by the trustee.

EXTRACT

Bristol and West Building Society v Mothew [1996] 4 All ER 698

Case facts

The defendant in this case was a solicitor, who had acted for the buyers of a house in a conveyancing transaction. However, as the house was bought with a mortgage loan from the claimants, he also acted for the claimants in terms of ensuring that the loan was registered as a charge on the Land Register. This is a perfectly acceptable course of action, and occurs on a routine basis in situations where a house is bought with the aid of a mortgage loan. The mortgage loan was granted on two conditions: namely that the buyers paid the deposit from their own money (rather than obtaining a loan from another lender) and that no other mortgage loans were granted in relation to the land without the claimants first being notified. However, the buyers wished to secure a second mortgage loan on the house, and this was done without the claimant's permission. Accordingly, when the buyers failed to repay the loan, the claimants discovered the second mortgage, and therefore sued the defendant solicitor for breach of contract and negligence (in which respect they succeeded) and also in breach of trust. Although it was held that the solicitor had acted in breach of contract, and that he had been negligent, no breach of trust was found, as Millett LJ explains.

Millett LJ

The claims in equity

The judge's reasoning

The judge found that, in the events which happened, the defendant committed a breach of trust by applying the mortgage advance in the purchase of the property; that he was accordingly liable to restore the trust property, viz the £59,000 with interest less receipts; that no question of damages at common law or of compensation for loss arose; and that it was irrelevant whether, had it been told of the position, the society might still have chosen to make the advance notwithstanding the arrangements which had been made with the bank.

Accordingly, the judge concluded that there was no question or issue to be tried in the action and gave summary judgment for the whole of the society's claim.

The judge's conclusion that the defendant had committed a breach of trust in applying the mortgage advance in the purchase of the property was based on the fact that he had obtained payment of the mortgage advance by misrepresentation . . .

In the judge's opinion it necessarily followed that the defendant's subsequent application of the mortgage money in the purchase of the property constituted a breach of trust . . .

The judge dismissed the submission that the society had to establish that it would not have made the advance if it had known the facts . . .

The judge did not explain why the consequence of the defendant's misrepresentation was that he held the mortgage advance on a constructive trust for the society, or why the defendant's authority to apply the money in accordance with the society's instructions was determined, but he took the opportunity to do so when he revisited these questions a few months later in *Bristol and West Building Society v May, May & Merrimans (a firm)* [1996] 2 All ER 801 after two county court judges had declined to follow his decision in the present case. The later case involved a number of transactions in which the same society had made mortgage advances and suffered loss when the borrowers defaulted which it sought to recover from the solicitors who had acted for both parties to the lending transactions. In some cases the solicitor knew nothing, prior to the receipt of the cheque for the mortgage advance, which ought to have led him to qualify his report, though he discovered the facts afterwards and before he disbursed the money on completion. In other cases the solicitor's breach of his instructions preceded his receipt of the mortgage advance, as it did in the present case.

The judge distinguished between the two groups of cases. In relation to the first group he reluctantly felt compelled by the decision in *Target Holdings Ltd v Redferns (a firm)* [1995] 3 All ER 785, [1996] AC 421 to conclude that, at least for the purpose of an application for summary judgment, it was necessary for the society to show that it would not have proceeded with the transaction if it had known the facts. In relation to the second group, however, where the society paid the cheque for the mortgage advance to the solicitor in response to a request based upon a warranty or representation which (as the judge put it) the solicitor 'knew or must be taken to have known' to be misleading, he confirmed his previous decision in the present case. He held that the society was entitled to succeed in such cases whether or not it would have still made the advance if it had known the facts.

In the course of his judgment the judge explained how the constructive trust in question arose. It was, he said, because the solicitor had given misleading information to his client. This constituted a breach of fiduciary duty which enabled the court to impose a constructive trust on the property acquired as a result of the breach of duty. He said:

> '. . . where moneys have been received by the solicitor from the society following a request based upon a warranty or representation which he knew, or must be taken to have known, to be misleading in some material respect, equity will give a remedy in respect of any loss which the society may suffer as a result of its payment in reliance upon that request. That will be a remedy based upon breach of fiduciary duty and may, where necessary, take the form of the imposition of a constructive trust on those moneys to enforce the solicitor's obligation to return them to the society forthwith. The constructive trust imposed by equity to enforce the obligation to make immediate restitution overrides any express or implied trust which might otherwise arise out of any instructions given by [the society] when the money is paid to the solicitor. No reliance can be placed on those instructions, because they are vitiated by the breach of duty by which they were obtained . . . In the absence of some

fresh instructions, given by the society after full disclosure of the matters in respect of which it has been misled, the only course properly open to the solicitor is to repay the moneys to the society with interest.'

The judge evidently considered himself to be imposing a remedial constructive trust as the appropriate remedy for a prior breach of fiduciary duty.

The judge's references to the solicitor having made a representation which 'he knew, or must be taken as having known' to be misleading is not an accurate description of the facts of the present case. It is not alleged that the defendant 'knew or must be taken to have known' the facts, but only that he 'knew or ought to have known' them, which is a very different matter. In explaining his decision in the present case the judge said that the defendant's misrepresentation could not be described as innocent because he 'clearly had the knowledge which made the representation false'. That confuses knowledge with the means of knowledge. On the society's pleaded case the defendant must be taken to have known the facts at one time but to have forgotten or overlooked them so that they were not present to his mind when he came to complete his report to the society.

It is not alleged that the defendant deliberately concealed the arrangements which the purchasers had made with their bank from the society or that he consciously intended to mislead it. Nothing in this judgment is intended to apply to such a case. My observations are confined to the case like the present where the provision of incorrect information by a solicitor to his client must be taken to have been due to an oversight. In such a case his breach of duty is unconscious; he will *ex hypothesi* be unaware of the fact that he has committed a breach of his instructions; and if this means that his subsequent application of the mortgage money constitutes a breach of trust then it will be a breach of a trust of which he is unaware. I would not willingly treat such conduct as involving a breach of trust or misapplication of trust money unless compelled by authority to do so, and in my judgment neither principle nor authority compels such a conclusion.

Before us the defendant submits that, while he was guilty of negligence and breach of contract, he was not guilty of a breach of trust or fiduciary duty. It is convenient to take first the question of fiduciary duty, and then to consider the question of breach of trust.

Breach of fiduciary duty

Despite the warning given by Fletcher Moulton LJ in *Re Coomber, Coomber v Coomber* [1911] 1 Ch 723 at 728 this branch of the law has been bedevilled by unthinking resort to verbal formulae. It is therefore necessary to begin by defining one's terms. The expression 'fiduciary duty' is properly confined to those duties which are peculiar to fiduciaries and the breach of which attracts legal consequences differing from those consequent upon the breach of other duties. Unless the expression is so limited it is lacking in practical utility. In this sense it is obvious that not every breach of duty by a fiduciary is a breach of fiduciary duty. I would indorse the observations of Southin J in *Girardet v Crease & Co* (1987) 11 BCLR (2d) 361 where she said:

'The word 'fiduciary' is flung around now as if it applied to all breaches of duty by solicitors, directors of companies and so forth . . . That a lawyer can commit a breach of the special duty [of a fiduciary] . . . by entering into a contract with the client without full disclosure . . . and so forth is clear. But to say that simple carelessness in giving advice is such a breach is a perversion of words.'

These remarks were approved by La Forest J in *Lac Minerals Ltd v International Corona Resources Ltd* (1989) 61 DLR (4th) 14 at 28, where he said:

'. . . not every legal claim arising out of a relationship with fiduciary incidents will give rise to a claim for a breach of fiduciary duty.'

It is similarly inappropriate to apply the expression to the obligation of a trustee or other fiduciary to use proper skill and care in the discharge of his duties. If it is confined to cases where the fiduciary nature of the duty has special legal consequences, then the fact that the source of the duty is to be found in equity rather than the common law does not make it a fiduciary duty. The common law and equity each developed the duty of care, but they did so independently of each other and the standard of care required is not always the same. But they influenced each other, and today the substance of the resulting obligations is more significant than their particular historic origin. In *Henderson v Merrett Syndicates Ltd, Hallam-Eames v Merrett Syndicates Ltd, Hughes v Merrett Syndicates Ltd, Arbuthnott v Feltrim Underwriting Agencies Ltd, Deeny v Gooda Walker Ltd (in liq)* [1994] 3 All ER 506 at 543, [1995] 2 AC 145 at 205 Lord Browne-Wilkinson said:

> 'The liability of a fiduciary for the negligent transaction of his duties is not a separate head of liability but the paradigm of the general duty to act with care imposed by law on those who take it upon themselves to act or advise others. Although the historical development of the rules of law and equity have, in the past, caused different labels to be stuck on different manifestations of the duty, in truth the duty of care on bailees carriers, trustees, directors, agents and others is the same duty: it arises from the circumstances in which the defendants were acting, not from their status or description. It is the fact that they have all assumed responsibility for the property or affairs of others which renders them liable for the careless performance of what they have undertaken to do, not the description of the trade or position which they hold.'

I respectfully agree, and indorse the comment of Ipp J in *Permanent Building Society (in liq) v Wheeler* (1994) 14 ACSR 109 at 157 where he said:

> 'It is essential to bear in mind that the existence of a fiduciary relationship does not mean that every duty owed by a fiduciary to the beneficiary is a fiduciary duty. In particular, a trustee's duty to exercise reasonable care, though equitable, is not specifically a fiduciary duty . . .'

Ipp J explained this (at 158):

> 'The director's duty to exercise care and skill has nothing to do with any position of disadvantage or vulnerability on the part of the company. It is not a duty that stems from the requirements of trust and confidence imposed on a fiduciary. In my opinion, that duty is not a fiduciary duty, although it is a duty actionable in the equitable jurisdiction of this court . . . I consider that Hamilton owed PBS a duty, both in law and in equity, to exercise reasonable care and skill, and PBS was able to mount a claim against him for breach of the legal duty, and, in the alternative, breach of the equitable duty. For the reasons I have expressed, in my view the equitable duty is not to be equated with or termed a "fiduciary" duty.'

I agree. Historical support for this analysis may be found in the passage in Viscount Haldane LC's speech in *Nocton v Lord Ashburton* [1914] AC 932 at 956, [1914–15] All ER Rep 45 at 54. Discussing the old bill in Chancery for equitable compensation for breach of fiduciary duty, he said that he thought it probable that a demurrer for want of equity would always have lain to a bill which did no more than seek to enforce a claim for damages for negligence against a solicitor.

In my judgment this is not just a question of semantics. It goes to the very heart of the concept of breach of fiduciary duty and the availability of equitable remedies.

Although the remedy which equity makes available for breach of the equitable duty of skill and care is equitable compensation rather than damages, this is merely the product of history and

in this context is in my opinion a distinction without a difference. Equitable compensation for breach of the duty of skill and care resembles common law damages in that it is awarded by way of compensation to the plaintiff for his loss. There is no reason in principle why the common law rules of causation, remoteness of damage and measure of damages should not be applied by analogy in such a case. It should not be confused with equitable compensation for breach of fiduciary duty, which may be awarded in lieu of rescission or specific restitution.

This leaves those duties which are special to fiduciaries and which attract those remedies which are peculiar to the equitable jurisdiction and are primarily restitutionary or restorative rather than compensatory. A fiduciary is someone who has undertaken to act for or on behalf of another in a particular matter in circumstances which give rise to a relationship of trust and confidence. The distinguishing obligation of a fiduciary is the obligation of loyalty. The principal is entitled to the single-minded loyalty of his fiduciary. This core liability has several facets. A fiduciary must act in good faith; he must not make a profit out of his trust; he must not place himself in a position where his duty and his interest may conflict; he may not act for his own benefit or the benefit of a third person without the informed consent of his principal. This is not intended to be an exhaustive list, but it is sufficient to indicate the nature of fiduciary obligations. They are the defining characteristics of the fiduciary. As Dr Finn pointed out in his classic work *Fiduciary Obligations* (1977) p 2, he is not subject to fiduciary obligations because he is a fiduciary; it is because he is subject to them that he is a fiduciary.

(In this survey I have left out of account the situation where the fiduciary deals with his principal. In such a case he must prove affirmatively that the transaction is fair and that in the course of the negotiations he made full disclosure of all facts material to the transaction. Even inadvertent failure to disclose will entitle the principal to rescind the transaction. The rule is the same whether the fiduciary is acting on his own behalf or on behalf of another. The principle need not be further considered because it is does arise in the present case. The mortgage advance was negotiated directly between the society and the purchasers. The defendant had nothing to do with the negotiations. He was instructed by the society to carry out on its behalf a transaction which had already been agreed.)

The nature of the obligation determines the nature of the breach. The various obligations of a fiduciary merely reflect different aspects of his core duties of loyalty and fidelity. Breach of fiduciary obligation, therefore, connotes disloyalty or infidelity. Mere incompetence is not enough. A servant who loyally does his incompetent best for his master is not unfaithful and is not guilty of a breach of fiduciary duty.

In the present case it is clear that, if the defendant had been acting for the society alone, his admitted negligence would not have exposed him to a charge of breach of fiduciary duty. Before us counsel for the society accepted as much, but insisted that the fact that he also acted for the purchasers made all the difference. So it is necessary to ask: why did the fact that the defendant was acting for the purchasers as well as for the society convert the defendant's admitted breach of his duty of skill and care into a breach of fiduciary duty? To answer this question it is necessary to identify the fiduciary obligation of which he is alleged to have been in breach.

It is at this point, in my judgment, that the society's argument runs into difficulty. A fiduciary who acts for two principals with potentially conflicting interests without the informed consent of both is in breach of the obligation of undivided loyalty; he puts himself in a position where his duty to one principal may conflict with his duty to the other: see *Clark Boyce v Mouat* [1993] 4 All ER 268, [1994] 1 AC 428 and the cases there cited. This is sometimes described as 'the double employment rule'. Breach of the rule automatically constitutes a breach of fiduciary duty. But this is not something of which the society can complain. It knew that the defendant was acting for the purchasers when it instructed him. Indeed, that was the very reason why it

chose the defendant to act for it. The potential conflict was of the society's own making (see Finn p 254 and *Kelly v Cooper* [1993] AC 205, [1993] 3 LRC 476).

It was submitted on behalf of the society that this is irrelevant because the defendant misled the society. It did not know of the arrangements which the purchasers had made with their bank, and so could not be said to be 'fully informed' for the purpose of absolving the defendant from the operation of the double employment rule. The submission is misconceived. The society knew all the facts relevant to its choice of solicitor. Its decision to forward the cheque for the mortgage advance to the defendant and to instruct him to proceed was based on false information, but its earlier decision to employ the defendant despite the potentially conflicting interest of his other clients was a fully informed decision.

That, of course, is not the end of the matter. Even if a fiduciary is properly acting for two principals with potentially conflicting interests he must act in good faith in the interests of each and must not act with the intention of furthering the interests of one principal to the prejudice of those of the other (see Finn p 48). I shall call this 'the duty of good faith'. But it goes further than this. He must not allow the performance of his obligations to one principal to be influenced by his relationship with the other. He must serve each as faithfully and loyally as if he were his only principal. Conduct which is in breach of this duty need not be dishonest but it must be intentional. An unconscious omission which happens to benefit one principal at the expense of the other does not constitute a breach of fiduciary duty, though it may constitute a breach of the duty of skill and care. This is because the principle which is in play is that the fiduciary must not be inhibited by the existence of his other employment from serving the interests of his principal as faithfully and effectively as if he were the only employer. I shall call this 'the no inhibition principle'. Unless the fiduciary is inhibited or believes (whether rightly or wrongly) that he is inhibited in the performance of his duties to one principal by reason of his employment by the other, his failure to act is not attributable to the double employment.

Finally, the fiduciary must take care not to find himself in a position where there is an actual conflict of duty so that he cannot fulfil his obligations to one principal without failing in his obligations to the other: see *Moody v Cox* [1917] 2 Ch 71, [1916–17] All ER Rep 548 and *Commonwealth Bank of Australia v Smith* (1991) 102 ALR 453. If he does, he may have no alternative but to cease to act for at least one and preferably both. The fact that he cannot fulfil his obligations to one principal without being in breach of his obligations to the other will not absolve him from liability. I shall call this 'the actual conflict rule'.

In the present case the judge evidently thought that the defendant was in breach of both the duty of good faith and the actual conflict rule. In *Bristol and West Building Society v May, May & Merrimans (a firm)* [1996] 2 All ER 801 at 817–818 he said:

> '. . . there can be no doubt that the requirement of unconscionable conduct is present where a solicitor who is acting for both borrower and lender misrepresents to the lender some fact which he knows, or must be taken to know, will or may affect the lender's decision to proceed with the loan. In those circumstances the solicitor is abusing his fiduciary relationship with one client, the lender, to obtain an advantage for his other client, the borrower. It is as much "against the dictates of conscience" for a solicitor knowingly to prefer the interests of one client over those of another client as it is for him to prefer his own interests over those of his client.' (My emphasis.)

I respectfully agree; but no such allegation is made in the present case.

As to the actual conflict rule, the judge said (at 832):

> 'First, in Mothew, the "agent" was a fiduciary who had put himself in a position in which his duty to the lender was in conflict with the interests of his other client, the borrower.' (My emphasis.)

I do not accept this. By instructing him to act for them, the purchasers must be taken to have authorised the defendant to complete the report without which the mortgage advance would not have been forthcoming; and to complete it truthfully. The defendant was required by the society to report on the purchasers' title as well as to confirm the absence of any further borrowing. The two stood in exactly the same case. The defendant would not have been in breach of his duty to the purchasers if he had disclosed the facts to the society any more than if he had reported a defect in their title.

This proposition can be tested by considering what the defendant's position would have been if he had acted for the purchasers and another solicitor had been instructed to act for the society. He would have been required to deduce the purchasers' title to the satisfaction of the society's solicitor, and to confirm to him that no further borrowing or second charge was in contemplation. His duty to the purchasers would have required him to ascertain the facts from them and to report them to the society. Unless they told him the facts and instructed him to lie to the society, instructions which he would be bound to refuse, his duty to the purchasers would not inhibit him in providing full and truthful information to the solicitor acting for the society.

In my judgment, the defendant was never in breach of the actual conflict rule. It is not alleged that he acted in bad faith or that he deliberately withheld information because he wrongly believed that his duty to the purchasers required him to do so. He was not guilty of a breach of fiduciary duty.

The judge relied on *Nocton v Lord Ashburton* [1914] AC 932, [1914–15] All ER Rep 45 and *Commonwealth Bank of Australia v Smith* (1991) 102 ALR 453 to hold that a party who pays money to his solicitor in reliance on a representation known by the solicitor to be false has a remedy in breach of fiduciary duty. Neither case is authority for the proposition (though its correctness is not in issue); certainly neither is authority for the proposition that a party who pays money to a solicitor in reliance on a representation which the solicitor ought to have known to be false has such a remedy.

In *Nocton v Lord Ashburton* a solicitor had an undisclosed personal interest in a transaction on which he gave his client advice which was to his own advantage and the disadvantage of his client. The plaintiff pleaded breach of the duty of good faith. In fact this was unnecessary; the existence of the defendant's undisclosed interest was enough: see *Lewis v Hillman* (1852) 3 HL Cas 607, 10 ER 239. The plaintiff was entitled to receive, and thought that he was receiving, the disinterested advice of a solicitor with no other interest in the transaction. *Commonwealth Bank of Australia v Smith* involved a breach of the actual conflict rule. The defendant, who was acting for both parties to a proposed transaction, placed himself in an impossible position by undertaking to advise one of them on the merits of the transaction.

In *Moody v Cox* [1917] 2 Ch 71, [1916–17] All ER Rep 548 a solicitor, who was acting for both vendor and purchaser, was in possession of valuations which showed that the property was not worth the price which the purchaser had agreed to pay. He did not disclose them to the purchaser, and claimed that his duty to the vendor precluded him from doing so. The purchaser was allowed to rescind. The case bears a superficial resemblance to the present but there are two crucial differences: (i) the vendor was under no obligation to disclose the valuations to the purchaser and did not wish his solicitor do so; and (ii) the vendor and the solicitor tacitly agreed to conceal the valuations from the purchaser. The solicitor was in breach of both the duty of good faith and the actual conflict rule; his defence fell foul of the no inhibition principle.

That was a case of deliberate concealment. Non-disclosure and concealment are two very different things. This has been a truism of the law from the time of Cicero, citing Diogenes of Babylon (see De Officiis, lib 3, c 12, 13). It is even enshrined, like other such truisms, in a Latin tag: *aliud est celare, aliud tacere.*

The society placed much reliance on a dictum by Lord Jauncey in *Clark Boyce v Mouat* [1993] 4 All ER 268 at 275, [1994] 1 AC 428 at 437, where he said:

> 'Another case of breach [of fiduciary duty] is where a solicitor acts for both parties without disclosing this to one of them or where having disclosed it he fails, unbeknown to one party, to disclose to that party material facts relative to the other party of which he is aware.' (My emphasis.)

But I do not think that Lord Jauncey meant to include an inadvertent failure which owes nothing to the double employment. Where such failure is to the advantage of the other party, the court will jealously scrutinise the facts to ensure that there has been nothing more than inadvertence, but there can be no justification for treating an unconscious failure as demonstrating a want of fidelity.

In my judgment the distinction drawn by Ipp J in *Permanent Building Society (in liq) v Wheeler* (1994) 14 ACSR 109 is sound in principle and is decisive of the present case. On the society's pleaded case the fact that the defendant was acting for the purchasers played no part in his failure to report the true state of affairs to the society. It did not inhibit him from fulfilling his obligations to the society. It is consistent with its pleaded case that the defendant would have done so but for a negligent oversight. It would have been exactly the same if he had failed to notice and report the existence of a defect in the purchasers' title. To characterise either such failure as a breach of fiduciary duty because he was acting for both parties in a situation where that fact did not contribute to his failure is, in my opinion, to substitute a verbal formula for principle.

In my judgment the judge's conclusion that the defendant was in breach of fiduciary duty cannot be supported. It follows that it cannot be sustained as a ground for holding the defendant to be in breach of a constructive trust of the mortgage money.

Breach of trust

It is not disputed that from the time of its receipt by the defendant the mortgage money was trust money. It was client's money which belonged to the society and was properly paid into a client account. The defendant never claimed any beneficial interest in the money which remained throughout the property of the society in equity. The defendant held it in trust for the society but with the society's authority (and instructions) to apply it in the completion of the transaction of purchase and mortgage of the property. Those instructions were revocable but, unless previously revoked, the defendant was entitled and bound to act in accordance with them.

The society's instructions were not revoked before the defendant acted on them, and in my judgment there was no ground upon which the judge could properly conclude that his authority to apply the money in completing the transaction had determined.

If his judgment in the present case is considered without the benefit of his later explanation in *Bristol and West Building Society v May, May & Merrimans (a firm)* [1996] 2 All ER 801, it would appear that the judge was of opinion that the defendant's authority to deal with the money was automatically vitiated by the fact that it (and the cheque itself) was obtained by misrepresentation. But that is contrary to principle. Misrepresentation makes a transaction voidable not void. It gives the representee the right to elect whether to rescind or affirm the transaction. The representor cannot anticipate his decision. Unless and until the representee elects to rescind the representor remains fully bound. The defendant's misrepresentations merely gave the society the right to elect to withdraw from the transaction on discovering the truth. Since its instructions to the defendant were revocable in any case, this did not materially alter the position so far as he was concerned, though it may have strengthened the society's position in relation to the purchasers.

The right to rescind for misrepresentation is an equity. Until it is exercised the beneficial interest in any property transferred in reliance on the representation remains vested in the transferee. In *El Ajou v Dollar Land Holdings plc* [1993] 3 All ER 717 at 734 I suggested that on rescission the equitable title might revest in the representee retrospectively at least to the extent necessary to support an equitable tracing claim. I was concerned to circumvent the supposed rule that there must be a fiduciary relationship or retained beneficial interest before resort may be had to the equitable tracing rules. The rule would have been productive of the most extraordinary anomalies in that case, and its existence continually threatens to frustrate attempts to develop a coherent law of restitution. Until the equitable tracing rules are made available in support of the ordinary common law claim for money had and received some problems will remain incapable of sensible resolution.

But all that is by the way. Whether or not there is a retrospective vesting for tracing purposes it is clear that on rescission the equitable title does not revest retrospectively so as to cause an application of trust money which was properly authorised when made to be afterwards treated as a breach of trust. In *Lipkin Gorman (a firm) v Karpnale Ltd* [1992] 4 All ER 512 at 528, [1991] 2 AC 548 at 573 Lord Goff said:

> 'Of course, "tracing" or "following" property into its product involves a decision by the owner of the original property to assert his title to the product in place of his original property. This is sometimes referred to as ratification. I myself would not so describe it; but it has, in my opinion, at least one feature in common with ratification, that it cannot be relied upon so as to render an innocent recipient a wrongdoer (cf *Bolton Partners v Lambert* (1889) 41 Ch D 295 at 307 per Cotton LJ: ". . . an act lawful at the time of its performance [cannot] be rendered unlawful, by the application of the doctrine of ratification.").'

In *Westdeutsche Landesbank Girozentrale v Islington London BC* [1996] 2 All ER 961 at 988, [1996] 2 WLR 802 at 828 Lord Browne-Wilkinson expressly rejected the possibility that a recipient of trust money could be personally liable, regardless of fault, for any subsequent payment away of the moneys to third parties even though, at the date of such payment, he was ignorant of the existence of any trust. He said:

> 'Since the equitable jurisdiction to enforce trusts depends upon the conscience of the holder of the legal interest being affected, he cannot be a trustee of the property if and so long as he is ignorant of the facts alleged to affect his conscience, ie until he is aware that he is intended to hold the property for the benefit of others in the case of an express or implied trust, or, in the case of a constructive trust, of the facts which are alleged to affect his conscience.'

Mutatis mutandis that passage is directly applicable in the present case. The defendant knew that he was a trustee of the money for the society; but he did not realise that he had misled the society and could not know that his authority to complete had determined (if indeed it had). He could not be bound to repay the money to the society so long as he was ignorant of the facts which had brought his authority to an end, for those are the facts which are alleged to affect his conscience and subject him to an obligation to return the money to the society.

Before us the society put forward a more sophisticated argument. The defendant's instructions, it pointed out, expressly required him to report the arrangements in question 'to the Society prior to completion'. This, it was submitted, made it a condition of the defendant's authority to complete that he had complied with his obligation. Whether he knew it or not, he had no authority to complete. It was not necessary for the society to revoke his authority or withdraw from the transaction.

I do not accept this. The society's standing instructions did not clearly make the defendant's authority to complete conditional on having complied with his instructions. Whether they did

so or not is, of course, a question of construction, and it is possible that the society could adopt instructions which would have this effect. But it would in my judgment require very clear wording to produce so inconvenient and impractical a result. No solicitor could safely accept such instructions, for he could never be certain that he was entitled to complete.

In my judgment the defendant's authority to apply the mortgage money in the completion of the purchase was not conditional on his having first complied with his contractual obligations to the society, was not vitiated by the misrepresentations for which he was responsible but of which he was unaware, and was effective to prevent his payment being a breach of trust. Given his state of knowledge, he had no choice but to complete.

The trust must be performed according to its terms

As a general principle, the trustee must not depart from the terms of the trust as specified by the trustee, and a failure to do so will constitute a breach of the trust.[24] Therefore, on becoming a trustee, there is a general obligation to make oneself aware of the terms of the trust, including what the trust property comprises of, how it has been invested, and who the beneficiaries are.[25] Nevertheless, as we shall see, the trustee does have the scope to vary the trust either in terms of when the beneficiary shall receive the money, or how much each beneficiary is to receive. However, this requires the consent of the adult beneficiaries who are immediately entitled and/or consent by the court on behalf of those who by reason of age, incapacity or the fact that they have a future interest in the trust property.

Duty not to profit from the trust

It is an essential part of the concept of the trust that the trustee must neither benefit from the trust, nor from his or her position as a trustee. This requires both that the trustee should not put him- or herself in a position where there is potential for conflict of interest,[26] and that the trustee makes no actual gain from the trust. Conflict of interest encompasses the notion of making financial gain, as well as allowing personal interest to conflict with the interests of the trust.[27] Therefore, a trustee who invests the trust fund according to his or her personal ethics is allowing his or her interests to conflict with those of the trust, even though the trustee is not making any personal gain from the situation. However, a more serious conflict of interest arises where a person makes a profit from the trust relationship.

A conflict of interest where a gain is made could arise where, for example, the trustee wishes to sell trust property to him- or herself. There is a potential conflict of interest here because the trustee qua seller wishes to obtain the highest possible price for the transaction, whereas the trustee qua buyer wishes to buy for the lowest price. Accordingly, in *Bray v Ford* [1896] AC 44, the then Lord Chancellor, Lord Herschell explains (at p.52):

> It is an inflexible rule of a Court of Equity that a person in a fiduciary position, such as the respondent's, is not, unless otherwise expressly provided, entitled to make a profit; he is not allowed to put himself in a position where his interest and duty conflict. It

[24] *Clough v Bond* (1838) 3 My and Cr 490.
[25] *Hallows v Lloyd* (1888) 22 Ch D 255.
[26] *Keech v Sandford* (1726) Sel Cas Ch 61.
[27] *Chan v Zacharia* (1984) 154 CLR 178.

> does not appear to me that this rule is, as has been said, founded upon principles of morality. I regard it rather as based on the consideration that, human nature being what it is, there is danger, in such circumstances, of the person holding a fiduciary position being swayed by interest rather than by duty, and thus prejudicing those whom he was bound to protect. It has, therefore, been deemed expedient to lay down this positive rule.

Therefore, the trustee must not make any financial gain from the trust, either by being paid for his work[28] or by using information that has been obtained under the auspices of the trust, or by selling the trust property to him- or herself. Accordingly, in the judgment in *Ex p Lacey* (1802) 6 Ves 625 Lord Eldon explains:

> The rule I take to be this; not, that a trustee cannot buy from his Cestuy que trust, but, that he shall not buy from himself. If a trustee will so deal with his Cestuy que trust, that the amount of the transaction shakes off the obligation, that attaches upon him as trustee, then he may buy . . . The rule is this. A trustee, who is entrusted to sell and manage for others, undertakes in the same moment, in which he becomes a trustee, not to manage for the benefit and advantage of himself. It does not preclude a new contract with those, who have entrusted him. It does not preclude him from bargaining, that he will no longer act as a trustee. The Cestuys que trust may by a new contract dismiss him from that character: but even then that transaction, by which they dismiss him, must according to the rules of this Court be watched with infinite and the most guarded jealousy; and for this reason; that the Law supposes him to have acquired all the knowledge a trustee may acquire; which may be very useful to him; but the communication of which to the Cestuy que trust the Court can never be sure he has made, when entering into the new contract, by which he is discharged. I disavow that interpretation of Lord Rosslyn's doctrine, that the trustee must make advantage. I say, whether he makes advantage, or not, if the connection does not satisfactorily appear to have been dissolved, it is in the choice of the Cestuy que trusts, whether they will take back the property, or not; if the trustee has made no advantage. It is founded upon this; that though you may see in a particular case, that he has not made advantage, it is utterly impossible to examine upon satisfactory evidence in the power of the Court, by which I mean, in the power of the parties, in ninety-nine cases out of an hundred, whether he has made advantage, or not. Suppose, a trustee buys any estate; and by the knowledge acquired in that character discovers a valuable coal-mine under it; and locking that up in his own breast enters into a contract with the Cestuy que trust: if he chooses to deny it, how can the Court try that against that denial. The probability is, that a trustee, who has once conceived such a purpose, will never disclose it; and the Cestuy que trust will be effectually defrauded. As to the purchase of the debts by the assignee, as assignees cannot buy the estate of the bankrupt, so also they cannot for their own benefit buy an interest in the bankrupt's estate; because they are trustees for the creditors. In that respect there is no difference between assignees and executors; who cannot for their own benefit buy the debts of the creditors. I do not say, there may not be cases of that kind, in which in a moral view the transaction between the executor and the creditor may not be blameable: but the Court must act upon general principles. Consider the prodigious power of assignees, connected with Solicitors under the Commission, and bankers, receiving the money, over the creditors and the bankrupt. Unless the policy of the Law makes it impossible for them to do

[28] *Guinness v Saunders* [1990] 2 AC 663.

> anything for their own benefit, it is impossible to see, in what cases the transaction is morally right. But it is enough to say, the assignee was a trustee for the benefit of those entitled to the interest in the residue. He must buy for them, and not for himself. Therefore as to the debts bought this assignee must be a trustee either for the creditors or for the bankrupt; for which upon the circumstances is doubtful yet. If persons, who are trustees to sell an estate, are there professedly as bidders to buy, that is a discouragement to others to bid. The persons present seeing the seller there to bid for the estate to or above its value do not like to enter into that competition. It is the duty of the solicitor to the Commission in point of law to insist, that the assignee should make the utmost value. In this case the Solicitor had two interests, drawing him different ways . . .

Neither is the trustee permitted to take advantage of information he has acquired qua trustee in order to make personal gains. Accordingly, in *Aberdeen Town Council v Aberdeen University* (1877) 2 App Cas 544, the Town Council as trustees of some land held on trust for the benefit of the university sold that land to their own agents. The Town Council then applied for fishing rights in relation to the land. However, the House of Lords concluded that both transactions were in breach of trust because the trustees were clearly benefiting from the fact that they had sold the land effectively to themselves, and then had obtained a benefit from that land that they could only have acquired as its owners. The key statement of the law is to be found in the case of *Boardman v Phipps*.

EXTRACT

Boardman v Phipps [1966] 3 All ER 721

Case facts

The trust fund comprised of company shares. The company's financial situation was unsatisfactory, and one of the trustees and the solicitor retained by the trust (who was therefore the trust's agent) decided, following attendance at an annual general meeting of the company, to improve the company's situation by buying more shares in order to obtain control of the company. The trustees could not buy more shares on behalf of the trust. However, the solicitor and one of the trustees succeeded in buying enough shares to obtain control of the company. They succeeded in making the company extremely successful, which resulted in a considerable profit for all the shareholders, which included the shares owned on behalf of the trust, as well as, of course, the shares owned by the solicitor and the trustee personally. A bare majority in the House of Lords concluded that this was a breach of the trust.

Lord Cohen

In the case before your lordships it seems to me clear that the appellants throughout were obtaining information from the company for the purpose stated by Wilberforce J ([1964] 2 All ER at pp 200, 201), but it does not necessarily follow that the appellants were thereby debarred from acquiring shares in the company for themselves. They were bound to give the information to the trustees, but they could not exclude it from their own minds. As Wilberforce J said ([1964] 2 All ER at p 203), the mere use of any knowledge or opportunity which comes to the trustee or agent in the course of his trusteeship or agency does not necessarily make him liable to account. In the present case had the company been a public company and had the appellants bought the shares on the market, they would not I think have been accountable. The company, however, is a private company and not only the information but also the opportunity to

purchase these shares came to them through the introduction which Mr Fox gave them to the board of the company and, in the second phase, when the discussions related to the proposed split up of the company's undertaking, it was solely on behalf of the trustees that Mr Boardman was purporting to negotiate with the board of the company. The question is this: when in the third phase the negotiations turned to the purchase of the shares at £4 10s a share, were the appellants debarred by their fiduciary position from purchasing on their own behalf the 21,986 shares in the company without the informed consent of the trustees and the beneficiaries?

The question one asks is whether the information could have been used by the principal for the purpose for which it was used by his agents? If the answer to that question is no, the information was not used in the course of their duty as agents. In the present case the information could never have been used by the trustees for the purpose of purchasing shares in the company; therefore purchase of shares was outside the scope of the appellants' agency and they are not accountable.

This is an attractive argument, but it does not seem to me to give due weight to the fact that the appellants obtained both the information which satisfied them that the purchase of the shares would be a good investment and the opportunity of acquiring them as a result of acting for certain purposes on behalf of the trustees. Information is, of course, not property in the strict sense of that word and, as I have already stated, it does not necessarily follow that, because an agent acquired information and opportunity while acting in a fiduciary capacity, he is accountable to his principals for any profit that comes his way as the result of the use he makes of that information and opportunity. His liability to account must depend on the facts of the case. In the present case much of the information came the appellants' way when Mr Boardman was acting on behalf of the trustees on the instructions of Mr Fox, and the opportunity of bidding for the shares came because he purported for all purposes except for making the bid to be acting on behalf of the owner seems to me that the principle of the *Regal* case [*Regal (Hastings) Ltd.* v *Gulliver* [1942] 1 All ER 378] applies and that the courts below came to the right conclusion.

That is enough to dispose of the case but I would add that an agent is, in my opinion, liable to account for profits which he makes out of the trust property if there is a possibility of conflict between his interest and his duty to his principal. Mr Boardman and Mr Tom Phipps were not general agents of the trustees, but they were their agents for certain limited purposes. The information which they had obtained and the opportunity to purchase the 21,986 shares afforded them by their relations with the directors of the company – an opportunity they got as the result of their introduction to the directors by Mr Fox – were not property in the strict sense but that information and that opportunity they owed to their representing themselves as agents for the holders of the eight thousand shares held by the trustees. In these circumstances they could not, I think, use that information and that opportunity to purchase the shares for themselves if there was any possibility that the trustees might wish to acquire them for the trust. Mr Boardman was the solicitor whom the trustees were in the habit of consulting if they wanted legal advice. Granted that he would not be bound to advise on any point unless he were consulted, he would still be the person they would consult if they wanted advice. He would still be the person they would consult if they wanted advice. He would clearly have advised them that they had no power to invest in shares of the company without the sanction of the court. In the first phase he would also have had to advise on the evidence then available that the court would be unlikely to give such sanction: but the appellants learnt much more during the second phase. It may well be that even in the third phase the answer of the court would have been the same but, in my opinion, Mr Boardman would not have been able to give unprejudiced advice if he had been consulted by the trustees and was at the same time negotiating for the purchase of the shares on behalf of himself and Mr Tom Phipps. In other words, there was, in my opinion, at the crucial date (March, 1959) a possibility of a conflict between his interest and his duty.

In making these observations I have referred to the fact that Mr Boardman was the solicitor to the trust. Mr Tom Phipps was only a beneficiary and was not as such debarred from bidding for the shares, but no attempt was made in the courts below to differentiate between them. Had such an attempt been made it would very likely have failed, as Mr Tom Phipps left the negotiations largely to Mr Boardman and it might well be held that, if Mr Boardman was disqualified from bidding, Mr Tom Phipps could not be in a better position. Be that as it may, counsel for the appellants rightly did not seek at this stage to distinguish between the two. He did, it is true, say that Mr Tom Phipps as a beneficiary would be entitled to any information that the trustees obtained. This may be so, but none the less I find myself unable to distinguish between the two appellants. They were, I think, in March, 1959, in a fiduciary position *vis-à-vis* the trust. That fiduciary position was of such a nature that (as the trust fund was distributable) the appellants could not purchase the shares on their own behalf without the informed consent of the beneficiaries: it is now admitted that they did not obtain that consent. They are therefore, in my opinion, accountable to the respondent for his share of the net profits which they derived from the transaction.

I desire to repeat that the integrity of the appellants is not in doubt. They acted with complete honesty throughout, and the respondent is a fortunate man in that the rigour of equity enables him to participate in the profits which have accrued as the result of the action taken by the appellants in March, 1959, in purchasing the shares at their own risk. As the last paragraph of his judgment clearly shows, the trial judge evidently shared this view. He directed an inquiry as to what sum was proper to be allowed to the appellants or either of them in respect of their or his work and skill in obtaining the said shares and the profits in respect thereof. The trial judge concluded by expressing the opinion that payment should be on a liberal scale. With that observation I respectfully agree.

Lord Hodson

I agree with the decision of the learned judge, and with that of the Court of Appeal which, in my opinion, involves a finding that there was a potential conflict between Mr Boardman's position as solicitor to the trustees and his own interest in applying for the shares. He was in a fiduciary position *vis-à-vis* the trustees and through them *vis-à-vis* the beneficiaries. For these reasons in my opinion the appeal should be dismissed.

Lord Guest

If Mr Boardman was acting on behalf of the trust, then all the information that he obtained in phase 2 became trust property. The weapon which he used to obtain this information was the trust holding; and I see no reason why information and knowledge cannot be trust property. In *Hamilton v Wright* Lord Brougham said ((1842), 9 Cl & Fin at p 124):

> 'The knowledge which he acquires as trustee is of itself sufficient ground of disqualification, and of requiring that such knowledge shall not be capable of being used for his own benefit to injure the trust; the ground of disqualification is not merely because such knowledge may enable him actually to obtain an undue advantage over others.'

In *Regal (Hastings) Ltd v Gulliver* Viscount Sankey said ([1942] 1 All ER at p 382, letter d):

> '*Imperial Hydropathic Hotel Co., Blackpool* v. *Hampson* makes no exception to the general rule that a solicitor or director, if acting in a fiduciary capacity, is liable to account for the profits made by him from knowledge acquired when so acting.'

Aas v Benham [[1891] 2 Ch 244] is another case where the use of information by a person in a fiduciary capacity was challenged.

The position of a person in a fiduciary capacity is referred to in *Regal (Hastings) Ltd v Gulliver* by Lord Russell of Killowen where he said ([1942] 1 All ER at p 386, letter a):

> 'My lords, with all respect I think there is a misapprehension here. The rule of equity which insists on those, who by use of a fiduciary position make a profit, being liable to account for that profit, in no way depends on fraud, or absence of bona fides; or upon such questions or considerations as whether the profit would or should otherwise have gone to the plaintiff, or whether the profiteer was under a duty to obtain the source of the profit for the plaintiff, or whether he took a risk or acted as he did for the benefit of the plaintiff, or whether the plaintiff has in fact been damaged or benefited by his action. The liability arises from the mere fact of a profit having, in the stated circumstances, been made. The profiteer, however honest and well-intentioned, cannot escape the risk of being called upon to account.'

Again Lord Russell quotes with approval from the judgment of the Lord Ordinary in *Huntington Copper Co v Henderson* ((1877), 4 R (Ct of Sess) 294 at p 308) the following passage ([1942] 1 All ER at p 389, letter b):

> 'Whenever it can be shown that the trustee has so arranged matters as to obtain an advantage whether in money or money's worth to himself personally through the execution of his trust, he will not be permitted to retain, but be compelled to make it over to his constituent.'

Lord Wright in the same case said ([1942] 1 All ER at p 392, letter c):

> 'That question can be briefly stated to be whether an agent, a director, a trustee or other person in an analogous fiduciary position, when a demand is made upon him by the person to whom he stands in the fiduciary relationship to account for profits acquired by him by reason of his fiduciary position, and by reason of the opportunity and the knowledge, or either, resulting from it, is entitled to defeat the claim upon any ground save that he made profits with the knowledge and assent of the other person.'

Again Lord Wright said ([1942] 1 All ER at p 392, letter e):

> 'The courts below have held that it does not apply in the present case, for the reason that the purchase of shares by the respondents, though made for their own advantage, and though the knowledge and opportunity which enabled them to take the advantage came to them solely by reason of their being directors of the appellant company, was a purchase which, in the circumstances, the respondents were under no duty to the appellant to make, and was a purchase which it was beyond the appellant's ability to make, so that, if the respondents had not made it, the appellant would have been no better off by reason of the respondents abstaining from reaping the advantage for themselves. With the question so stated, it was said that any other decision than that of the courts below would involve a dog-in-the-manger policy. What the respondents did, it was said, caused no damage to the appellant and involved no neglect of the appellant's interests or similar breach of duty. However I think the answer to this reasoning is that, both in law and equity, it has been held that, if a person in a fiduciary relationship makes a secret profit out of the relationship, the court will not inquire whether the other person is damnified or has lost a profit which otherwise he would have got. The fact is in itself a fundamental breach of the fiduciary relationship. Nor can the court adequately investigate the matter in most cases.'

Applying these principles to the present case I have no hesitation in coming to the conclusion that the appellants hold the Lester & Harris Ltd shares as constructive trustees and are bound to account to the respondent. It is irrelevant that the trustees themselves could not have profited by the transaction. It is also irrelevant that the appellants were not in competition with the trustees in relation to the shares in Lester & Harris, Ltd. The appellants argued that as the shares

were not acquired in the course of any agency undertaken by the appellants they were not liable to account. Analogy was sought to be obtained from the case of *Aas v Benham*, where it was said that before an agent is to be accountable the profits must be made within the scope of the agency (see per Lindley LJ ([1891] 2 Ch at pp 255, 256). That, however, was a case of partnership where the scope of the partners' power to bind the partnership can be closely defined in relation to the partnership deed. In the present case the knowledge and information obtained by Mr Boardman was obtained in the course of the fiduciary position in which he had placed himself. The only defence available to a person in such a fiduciary position is that he made the profits with the knowledge and assent of the trustees. It is not contended that the trustees had such knowledge or gave such consent.

Nevertheless, the dissenting judgments are also worth reading, as a strong counter-argument may be made in opposition of the judgment.

Viscount Dilhorne

In my opinion, despite the able arguments advanced by counsel for the appellants the unanimous opinion of the Court of Appeal and of Wilberforce J, that their relationship to the trust was fiduciary is correct. In my opinion that relationship arose from their being employed as agents of the trust on the occasions that I have mentioned and continued throughout. It does not, however, necessarily follow that they are liable to account for the profit that they made. If they had entered into engagements in which they had or could have had a personal interest conflicting with the interests of those they were bound to protect, clearly they would be liable to do so. On the facts of this case there was not, in my opinion, any conflict or possibility of a conflict between the personal interests of the appellants and those of the trust. There was no possibility so long as Mr Fox was opposed to the trust buying any of the shares of any conflict of interest arising through the purchase of the shares by the appellants. . . . The information which they obtained during the second phase was clearly of great value to the appellants for it enabled them to form an estimate of the profits that they might secure if all went well. Without it they might not have been prepared to pay £4 10s a share and without it they might not have been able to secure the necessary finance. Was the information which they obtained the property of the trust? If so, then they made use of trust property in securing a profit for themselves and they would be accountable. While it may be that some information and knowledge can properly be regarded as property, I do not think that the information supplied by Lester & Harris, Ltd and obtained by Mr Boardman as to the affairs of that company is to be regarded as property of the trust in the same way as shares held by the trust were its property. Nor do I think that saying that they represented the trust without authority amounted to use of the trust holding.

Boardman v Phipps is a controversial judgment, and the fact that two of their Lordships gave a dissenting judgment means that it is not as strong a precedent as one where all the judges are unanimous. Accordingly, it may be possible to consider a number of arguments, including those outlined by Viscount Dilhorne and Lord Upjohn regarding why the law should not be as strict. Nevertheless, the current position remains that the trustees must not make any gain or have any possibility of making any gain from the trust relationship.

ACTIVITY

Do you consider that in each of the following situations, there has been a breach of trust because the trustee has put him- or herself in a position where he or she could profit from the trust relationship?

1. Company A wishes to buy Company B. Company B sells 2000 shares to Company A and 500 shares each to five individuals – who are also directors of Company A. The shares sold to the individuals are sold for a considerable profit.
2. A company's board of directors sets up a committee which agrees to pay the defendant £5.2 million for his work in connection with the take-over of another company. The defendant is a director of the company, and the company argues that he should therefore have declared his interest in the agreement before being party to the decision.
3. A is a stockbroker who is employed on the basis that he would obtain commission for every client he introduces to his firm. At A's recommendation, the trust for which A is the trustee employs the firm for which A works to value the securities that form the trust property.
4. A hospital's directors pass a by-law permitting them to be paid for their professional services.

In fact, all of these cases constituted a breach of trust (as is decided *in Regal (Hastings) v Gulliver* [1942] 1 All ER 378, *Guinness v Saunders* [1990] 2 AC 663*, Williams v Barton* [1927] 2 Ch 9 and *Re The French Protestant Hospital* [1951] Ch 567 respectively), even though the beneficiaries either also benefited from the arrangement in a way that would not have been possible without the trustee's intervention, or the trustee's contribution was significant, and may be argued as being deserving of remuneration.

Nevertheless, although on the facts of these specific cases, the trustee's good faith and honourable conduct were not in doubt, it is likely that the courts are unwilling to relax the rule in any way because they acknowledge that the trust provides the trustee with considerable opportunities to make a gain, and that not all trustees would act with the same degree of integrity. It is for this reason that the courts will not permit even an indirect gain to be made from the trust relationship. Accordingly in the case of *Re Macadam* [1946] Ch 73, the trustees were accountable to the trust for the remuneration they had received as company directors. Company directors are appointed by the shareholders with each share held being equivalent to one vote. The shares held by the trust had been used to procure the trustees' appointment as directors, and therefore they were held to account to the trust for their remuneration, even though the remuneration had not come directly from the trust fund. In *Re Gee* [1948] Ch 284 however, there was no breach of trust because the trustee had not procured his appointment to the board of directors using trust shares. The simple rule is this therefore: the trustees may not gain in any way from their office. This is known as the principle in *Keech v Sandford* (1726) Sel Cas Ch 61.

The law categorises conflict of interest under the headings of fair dealing and self-dealing. Self-dealing is the situation where the trustee wishes to buy property from the trust. The law's approach is to consider this transaction as being voidable[29] because there is considerable potential for the trustee's interests as both seller and buyer to conflict. However, the transaction is not void, but is instead voidable. Nevertheless, it would be

[29] *British Coal Corporation v British Coal Staff Superannuation Scheme Trustees Ltd* [1993] PLR 303.

very difficult for the trustee to argue that the transaction was fair. If the beneficiaries wish to void the transaction, it is unlikely that the trustee would successfully prevent this, even if he or she argued that a fair price was paid.[30] In the case of *Campbell v Walker* (1800) 5 Ves 678 for example, the trustee was unable to prevent the transaction from being voided, even though he had paid a much higher price than the auctioneer's reserve. Ultimately therefore, the law seeks to discourage the trustee from selling trust property to him- or herself.[31] Nevertheless, the court may approve the transaction,[32] and therefore if there is some item of trust property that the trustee is adamant that he or she wishes to purchase, an application may be made to the court in advance for approval of the transaction.

On the other hand, the fair dealing rule relates to the situation where the trustee deals with the interests of the beneficiary. Again, this transaction is voidable, but the law is more willing to accept this as being fair provided that the trustee is able to show that he or she has not taken advantage of his or position as the trustee, and has made a full disclosure to the beneficiary of the proposed transaction.[33] The reason why fair dealing is dealt with more leniently is because the beneficiary is, necessarily, a party to the transaction. Accordingly, the beneficiary effectively approves the transaction, and thus it is seen as being less repugnant to the notion of trusteeship.

However, there are exceptions to the principle that the trustee must not profit from the trust. Firstly, the trustee may be remunerated for his or her work if the trust expressly or impliedly authorises remuneration. A professionally drawn will where the solicitor is appointed as trustee will therefore include a remuneration clause such as this one, from *Williams on Wills*:

> Any of my trustees being in a profession or business may charge and be paid all usual professional and other proper charges for business transacted, acts done, advice given and time spent by him or his firm in connection with the administration of my estate or in connection with the trusts hereof including acts which a personal representative or trustee not being in any profession or business could have done personally.[34]

Furthermore, the courts may authorise remuneration or compensation for the trustee's work, but will only do so where the trustee's obligations have been particularly onerous, as the case of *Re Worthington* [1954] 1 All ER 677 confirms.

EXTRACT

Re Worthington [1954] 1 All ER 677

Case facts

Under the terms of a will, the deceased's wife was appointed both as the executrix of the will and as its sole beneficiary. The wife appointed the claimant, who was a solicitor, to administer the estate. The solicitor discovered that the deceased had been insolvent when he died, and therefore attempted to negotiate a compromise with his creditors in order to ensure that some of the estate might be left over for the wife. Once it had become apparent that the creditors' claims could not be satisfied, the solicitor attempted to have the deceased's estate administered in bankruptcy. The claimant therefore claimed for the costs incurred in effecting this.

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[30] *Wright v Morgan* [1926] AC 788.
[31] *Tito v Waddell (No 2)* [1977] Ch 106.
[32] *Holder v Holder* [1967] 2 AC 46.
[33] *Tito v Waddell (No 2)* [1977] Ch 106.
[34] Sherrin, C.H. *et al.* (2002) *Williams on Wills*, 8th ed. Butterworth-Heinemann: Oxford.

Lord Upjohn

I think it is clear that, although there is a jurisdiction in the court to allow remuneration to trustees, that jurisdiction should be exercised only sparingly and in exceptional cases. In *Re Masters* ([1953] 1 All ER 19) Danckwerts J gave one example of a case where the jurisdiction was exercised. That was *Re Macadam* [[1948] Ch 73], where trustees, by virtue of the trust holding of shares in a company, became directors and received directors' fees, and it was held that in the circumstances of that particular case it would be proper to allow them to keep, at any rate, part of those fees as and by way of remuneration for doing the exceptional work of acting as directors. Another illustration was given by Lord Langdale MR in *Bainbrigge v Blair* [(1845) 50 ER 231], which was decided in 1845. In that case it was held that a trustee acting as solicitor in the trust matters was merely entitled to costs out of pocket. Referring, purely by way of example, to the case of a trustee who said that he was willing to do certain matters which required to be carried out for the benefit of the trust, but was not prepared to spend the time necessary to do those things unless he received some remuneration, Lord Langdale MR said (8 Beav 596):

> 'In such a cash, it is competent for the court, considering what is beneficial to the cestuis que trust, and is calculated to promote their interest, to take the matter into consideration, and to give proper remuneration to that person who alone, by his own exertion, can produce that benefit.'

. . . I think that, having regard to the statement which I have quoted from the judgment of Lord Langdale MR the decision is useful as showing by way of example the sort of cases in which the court might exercise its discretion to allow remuneration. I must not be taken as laying down any rule that where trustees act as directors or refuse to undertake work in the future without remuneration the court ought to treat them as exceptional cases and allow remuneration. I merely refer to those cases as examples of what may in some circumstances be considered exceptional cases, and where the court, on a review of all the relevant facts, may come to the conclusion that remuneration should be allowed. . . .

In the present case Mr Leighton has acted with absolute propriety and solely in the interests of those interested in the estate. It is said that the whole object of his becoming attorney administrator was to keep the costs down to a minimum. The work that Mr Leighton did of preparing the petition and preparing the necessary accounts was work which had to be done by somebody, and the estate, therefore, has suffered no loss. On the contrary, it has benefited because Mr Leighton was acquainted with the whole matter and, therefore, could prepare the petition and the various accounts more quickly and less expensively than anyone else. I think that there is much force in that. But the rule seems to me to be a strict one, and, if I granted the application in this case, it might be open to solicitors in almost every case to say: 'We have acted honestly and properly. There has been no loss to the estate. Let us have our costs', and the salutary rule that a solicitor trustee cannot charge for his services would be virtually destroyed. Though I have must sympathy with Mr Leighton, I can find nothing in this case which can be described as exceptional in any way, and on that ground I must refuse this motion.

Accordingly, it is only where the trustee's work has been exceptionally onerous that the court will authorise the trustee to be remunerated for the work undertaken, as in the case of *In Re Duke of Norfolk's Settlement Trusts* [1982] Ch 61. If the trustees have done no more than was expected of them, then it is unlikely that the court will see fit to remunerate them.

EXTRACT

In Re Duke of Norfolk's Settlement Trusts [1982] Ch 61

Case facts

A discretionary trust was created of property that comprised of the issued share capital of a company whose main asset was the settlor's life interest in a plot of land, 3000 acres of land in Yorkshire, and four blocks of buildings between the Strand and the Thames in London. The trust was complicated by the fact that, firstly, there was a possibility that the trust fund would not be distributed until 2038, and secondly that further land was added to the trust, and that this led to the estate being redeveloped in a substantial way. Accordingly, the trustees' work went far beyond anything they could have foreseen when the trust was initially created.

Fox LJ

There is, in my judgment, no doubt that the court has an inherent jurisdiction to authorise payment of remuneration to trustees. Danckwerts J. in *In re Masters, decd.* [1953] 1 W.L.R. 81 and Upjohn J. in *In re Worthington, decd.* [1954] 1 W.L.R. 526 accept that. The older authorities lead me to the same conclusion . . . The question is the extent of that jurisdiction. There can, in my view, be no doubt that there is an inherent jurisdiction, upon the appointment of a trustee, to direct that he be remunerated; that is accepted by Sir John Leach V.-C. in *Brocksopp v. Barnes*, 5 Mad. 90 and must be inherent in what is said in *In re Masters, decd.* [1953] 1 W.L.R. 81 and *In re Worthington, decd.* [1954] 1 W.L.R. 526. Indeed, it is not really in dispute at all. In the present case, however, what is sought is the increase of remuneration authorised by the trust instrument. The judge said that there had never been a case in which that was done, unless it was *In re Codd's Will Trusts (Practice Note)* [1975] 1 W.L.R. 1139 where the matter was not argued. I feel much doubt whether that proposition is in fact correct. Most cases relating to trustees' remuneration are dealt with in chambers and are not reported. My own impression and, I understand, that of Brightman L.J. also is that since the early 1950s orders have been made in chambers, under the inherent jurisdiction, authorising increases in remuneration given by the trust instrument. But I do not rely upon that. I will approach the matter as one of principle and on the reported cases. If it be the law, as I think it clearly is, that the court has inherent jurisdiction on the appointment of a trustee to authorise payment of remuneration to him, is there any reason why the court should not have jurisdiction to increase the remuneration already allowed by the trust investment? . . . The position, it seems to me, is this. Trust property is held by the trustees upon the trusts and subject to the powers conferred by the trust instrument and by law. One of those powers is the power to the trustee to charge remuneration. That gives the trustee certain rights which equity will enforce in administering the trust. How far those rights can properly be regarded as beneficial interests I will consider later. But it seems to me to be quite unreal to regard them as contractual. So far as they derive from any order of the court they simply arise from the court's jurisdiction and so far as they derive from the trust instrument itself they derive from the settlor's power to direct how his property should be dealt with . . . There remains the question whether, upon principle and authority, we can properly infer that the jurisdiction does exist. As to principle, it seems to me that if the court has jurisdiction, as it has, upon the appointment of a trustee to authorise remuneration though no such power exists in the trust instrument, there is no logical reason why the court should not have power to increase the remuneration given by the instrument . . . I appreciate that the ambit of the court's inherent jurisdiction in any sphere may, for historical reasons, be irrational and that logical extensions are not necessarily permissible. But I think that it is the basis of the jurisdiction that one has to consider. The basis, in my view, in relation to a trustee's remuneration is the good administration of trusts. The fact that in

earlier times, with more stable currencies and with a plenitude of persons with the leisure and resources to take on unremunerated trusteeships, the particular problem of increasing remuneration may not have arisen, does not, in my view, prevent us from concluding that a logical extension of admitted law and which is wholly consistent with the apparent purpose of the jurisdiction is permissible. If the increase of remuneration be beneficial to the trust administration, I do not see any objection to that in principle . . . I conclude that the court has an inherent jurisdiction to authorise the payment of remuneration of trustees and that that jurisdiction extends to increasing the remuneration authorised by the trust instrument. In exercising that jurisdiction the court has to balance two influences which are to some extent in conflict. The first is that the office of trustee is, as such, gratuitous; the court will accordingly be careful to protect the interests of the beneficiaries against claims by the trustees. The second is that it is of great importance to the beneficiaries that the trust should be well administered. If therefore the court concludes, having regard to the nature of the trust, the experience and skill of a particular trustee and to the amounts which he seeks to charge when compared with what other trustees might require to be paid for their services and to all the other circumstances of the case, that it would be in the interests of the beneficiaries to increase the remuneration, then the court may properly do so.

Brightman LJ

I entirely agree with the judgment of Fox L.J. and wish to add only a few words of my own.

In this appeal we are concerned with the power of the High Court to authorise a trust corporation, which has been in office for some 20 years, to charge fees for its future services in excess of those laid down in the trust instrument. In his admirable submissions in the unwelcome role of *advocatus diaboli* which this court imposed upon him, Mr. Romer confined himself to that narrow issue. He did not dispute that the High Court can, in the exercise of its inherent jurisdiction, authorise a trustee to retain remuneration where none is provided by the terms of the trust. What the court has no jurisdiction to do, he submitted, was to authorise an increase in the general level of remuneration of a paid trustee by way of addition to the remuneration which is allowed by the trust, once the trust has been unconditionally accepted.

Where the court appoints a trust corporation to be a trustee, it has a statutory power to authorise it to charge remuneration: Trustee Act 1925, section 42. The inherent power of the court to authorise a prospective trustee to charge remuneration is exemplified by such cases as *In re Freeman's Settlement Trusts*, 37 Ch.D. 148. The inherent power to authorise an unpaid trustee to charge remuneration, notwithstanding prior acceptance of the unpaid office, was regarded by Lord Langdale M.R. in *Bainbrigge* v. *Blair*, 8 Beav. 588, as undoubted.

If the court has an inherent power to authorise a prospective trustee to take remuneration for future services, and has a similar power in relation to an unpaid trustee who has already accepted office and embarked upon his fiduciary duties on a voluntary basis, I have some difficulty in appreciating the logic of the principle that the court has no power to increase or otherwise vary the future remuneration of a trustee who has already accepted office. It would mean that, if the remuneration specified in the trust instrument were lower than was acceptable to the incumbent trustee or any substitute who could be found, the court would have jurisdiction to authorise a substitute to charge an acceptable level of remuneration, but would have no jurisdiction to authorise the incumbent to charge precisely the same level of remuneration. Such a result appears to me bizarre, and to call in question the validity of the principle upon which it is supposedly based . . .

Outcome

The Court of Appeal allowed the appeal.

Thirdly, a trustee may acquire trust property for him- or herself if doing so is permitted either by statute (in the form of the Settled Land Act 1925,[35] s.68, although as no new settlements may be created since the Trusts of Land and Appointment of Trustees Act 1996[36] came into force, the scope for statute to permit acquisition is decreasing) or by a court order or with the consent of all the beneficiaries.

Therefore, if the trustee wishes to purchase property from the trust, without running the risk that the transaction will be voided, he or she must not take advantage of the beneficiary in any way. It seems therefore that as far as possible, it is preferable for the trustee not to acquire trust property, and if he or she chooses to do so, they must exercise a significant degree of caution in order to avoid any imputation of improper conduct and any allegation that the transaction was procured with any risk of disbenefit to the beneficiary will be dealt with very severely by the courts, as the case of *Movitex v Bulfield* [1988] BCLC 104 confirms.

EXTRACT

Movitex Ltd v Bulfield [1988] BCLC 104

Case facts

The claimant entered into a contract to buy a plot of land. When Movitex could not raise the necessary finances to complete the transaction, its two directors arranged for the land to be transferred to a company called CRS of which the defendants were the directors and shareholders. CRS paid the purchase price, and then leased the land to the claimants. The lease was then mortgaged to a company called Harper. Harper's shares were owned by trustees of various trusts created by the first defendant (Perry). Furthermore, the second defendant (Bulfield) was a director of Harper. The mortgage loan was then transferred to CRS, essentially creating a situation where CRS owned the freehold of the land, which it leased to Movitex, and then CRS became the mortgagee in respect of Movitex' loan over the land. The company's articles permitted self-dealing provided that the director made full disclosure of his interest and that he could not vote on the matter. Movitex argued therefore that the lease and the mortgage had not been properly authorised, and that neither Perry nor Bulfield had made proper disclosure of their interest in the transactions.

Vinelott J

It seems to me that it is one thing to say that a breach of the fair-dealing rule by a trustee in, for instance, purchasing a beneficiary's beneficial interest in trust property (or what is, I think, substantially the same thing, in purchasing the trust property with the consent of the beneficiary without making proper disclosure) is not a breach of trust and quite another to say that it involves no breach of duty. It seems to me that while such a breach may not be a breach of the trustee's primary duty to deal with the trust property in the interests of its beneficiaries and so not a breach of trust, the trustee in dealing with the beneficiary owes a duty to him to make full disclosure and to deal fairly with him, which is founded on the inequality in the relationship between the trustee and the beneficiary and the opportunity which the trustee had in the course of managing the trust property of acquiring knowledge relevant to its value which

[35] (1925 c.18).
[36] (1996 c.47).

is denied to the beneficiary. Similarly if a director seeks the approval of the company in general meeting to the purchase by him of the company's property, he owes a duty to make full disclosure to the company . . . The remaining question is whether in relation to the first transaction Mr Bulfield or Mr Perry was in breach of either of these duties. As regards the first of these duties, the duty 'to declare the nature of his interest' must, I think, impose on a director the duty to disclose full information as to the nature of any transaction which it is proposed to enter into. The disclosure must be such that the other director or directors can see what his interest is and how far it goes.

Outcome

Accordingly, the transaction could be set aside on the basis that the dealing, although authorised had not come about as a result of full disclosure being made by the defendants.

Accounts and information

According to the judgment of Lord Eldon, the Lord Chancellor, in the case of *Freeman v Fairlie* (1817) 3 Mer 24, the trustee owes a duty to maintain accounts pertaining to the trust. The trustee must also provide information to the beneficiary who requests it, as well as to any successor trustees, concerning the manner in which the trust fund has been invested, as well as the documents relating to the trust, as is shown in the case of *Clarke v Earl of Ormonde* (1821) Jac 108. Accordingly, there is a duty to inform the beneficiaries about the terms of the trust.[37]

Nevertheless, there is no obligation to disclose documents relating to the trustee's exercise of discretion to the beneficiary, as is shown in the case of *Re Londonderry's Settlement* [1965] Ch 918, unless a change of policy by the trustee defeats a legitimate expectation that has arisen in the minds of the beneficiaries, as is confirmed in the case of *Ex p Scott* [1998] 1 WLR 226. Furthermore, there is no obligation to disclose to the beneficiary any documents that reveal the trustees' reasons for their decisions,[38] the contents of which are confidential.

The court may however intervene if the trustee makes a decision that he or she would not have made if he or she had considered only information that was relevant to the decision-making process. This is known as the principle in *Hastings Bass*. *Re Hastings Bass* [1974] 2 All ER 193 concerned a will (written in 1947) which gave a life interest to Peter Hastings, and then after Peter's death to such of Peter's sons or remoter male issue (grandsons, great-grandsons etc.) as Peter should appoint. Peter acted in accordance with the terms of the trust, and decided that his eldest son, William Hastings-Bass would be entitled to the interest in remainder when he, William, reached the age of 25. Peter's sister also created a trust which gave a life interest to William. However, it was discovered that, on Peter's death, the amount of tax payable on the testator's estate would be significant, and in order to reduce this burden, the trustees of the 1947 will decided to advance the sum of £50,000 to the trustees of the 1957 trust. Essentially what this meant that there was less money in the trust fund of the 1947 will, but that the life interest to William under the 1957 trust would be substantial. However, it transpired that this arrangement was void as it breached the rule against perpetuities. Because the trustees

[37] *Hawkesley v May* [1956] 1 QB 304.
[38] *O'Rourke v Darbishire* [1964] 3 All ER 855.

would not have entered into this transaction knowing this fact, the court was willing to intervene. Buckley LJ explained:

> They made the transfer to the 1957 settlement trustees because they considered that it would benefit William. There is no reason to suppose that, in the light of their own understanding or advice as to the law, they failed to ask themselves the right questions or to arrive in good faith at a reasonable conclusion. . . . If by operation of law one or more of those benefits cannot take effect, it does not seem to us to follow that those which survive should not be regarded as having been brought into being by an exercise of the discretion. If the resultant effect of the intended advancement were such that it could not reasonably be regarded as being beneficial to the person intended to be advanced, the advancement could not stand, for it would not be within the powers of the trustees under s 32 . . . , in our judgment, where by the terms of a trust (as under s 32) a trustee is given a discretion as to some matter under which he acts in good faith, the court should not interfere with his action notwithstanding that it does not have the full effect which he intended, unless (1) what he has achieved is unauthorised by the power conferred on him, or (2) it is clear that he would not have acted as he did (a) had he not taken into account considerations which he should not have taken into account, or (b) had he not failed to take into account considerations which he ought to have taken into account. In the present case (2) above has not, in our judgment, been established; but the commissioners contend that for reasons stated in their third submission, sub-head (a), and their final submission what the trustees achieved in the present case was in excess of their power.

Therefore, because the transaction did not in fact benefit William, the court could intervene, overturn the trustees' decision, and allow the trust to continue on the original basis.

In the case of *Pitt v Holt* [2011] EWCA Civ 197, the Court of Appeal revisited the judgment in *Re Hastings-Bass* and concluded that cases such as *Edge v Pensions Ombudsman* (below) had expanded the rule in *Re Hastings-Bass* beyond its original scope. It should be noted that *Pitt v Holt* later went before the Supreme Court and is reported as *Pitt v Holt* [2013] AC 108. However, the Supreme Court cited Lloyd LJ's judgment extensively, and it is therefore the Court of Appeal's judgment that provides the more detailed analysis of the situation. Lloyd LJ explains:

> In *Re Hastings-Bass* the issue was whether what the trustees had done was an exercise of the power of advancement under s 32 at all. If it was not, then it was entirely void. If on the other hand it was within the power, then there was no reason to regard it as ineffective to the extent that the rule against perpetuities permitted, i.e. as regards the life interest in favour of William Hastings-Bass. Only if it was void could the Revenue succeed. They had no right to challenge it as voidable (even if there had been any grounds for saying that it was) and no person who had such a right had sought to do so.
>
> None of the later cases has raised an issue of that kind. In each case the trustees' exercise of their discretionary power has undoubtedly been within the scope of the relevant power. The trustees' act has been said to be vitiated by a failure on their part to comply with their duty to take all relevant matters into account, and not to take irrelevant matters into account.

Accordingly, Lloyd LJ explains:

> The purported exercise of a discretionary power on the part of trustees will be void if what is done is not within the scope of the power. There may be a procedural defect, such as the use of the wrong kind of document, or the failure to obtain a necessary prior consent. There may be a substantive defect, such as an unauthorised delegation

or an appointment to someone who is not within the class of objects. Cases of a fraud on the power are similar to the latter, since the true intended beneficiary, who is not an object of the power, is someone other than the nominal appointee. There may also be a defect under the general law, such as the rule against perpetuities, whose impact and significance will depend on the extent of the invalidity. *Re Abrahams* [1967] 1 Ch 463 and *Re Hastings-Bass* together show that the effect on an advancement of invalidity by reason of something such as the rule against perpetuities may be such that what remains of the advancement is not reasonably capable of being regarded as for the benefit of the advance. In that case the advancement will be void, since the power can only be used for the benefit of the relevant person and the purported exercise was not for his or her benefit. That is an example of an exercise outside the scope of the power. Otherwise, as in Re Hastings-Bass itself, it will be valid.'

Lloyd LJ then goes on to explain what the duties of a trustee are, and what matters should be taken into account when making decisions.

EXTRACT

Pitt v Holt [2011] EWCA Civ 197

It is therefore necessary to consider the nature and extent of the duty of trustees in relation to their dispositive discretionary powers. This has been the subject of a number of authoritative observations and decisions, in different contexts. In *Re Baden's Deed Trusts*, [1971] AC 424 at 449, Lord Wilberforce considered the nature of the duty of trustees with a discretion exercisable as between the members of a very wide defined class. Taking first the case in which the discretion was not backed up by a trust to distribute, he said, at 449D:

> 'Any trustee would surely make it his duty to know what is the permissible area of selection and then consider responsibly, in individual cases, whether a contemplated beneficiary was within the power and whether, in relation to other possible Claimants, a particular grant was appropriate.'

He then went on:

> 'Correspondingly a trustee with a duty to distribute, particularly among a potentially very large class, would surely never require the preparation of a complete list of names, which anyhow would tell him little that he needs to know. He would examine the field, by class and category; might indeed make diligent and careful inquiries, depending on how much money he had to give away and the means at his disposal, as to the composition and needs of particular categories and of individuals within them; decide upon certain priorities or proportions, and then select individuals according to their needs or qualifications.'

Summarising the position, a little later he said, at 449F:

> 'Differences there certainly are between trust (trust powers) and powers, but as regards validity, should they be so great as that in one case complete, or practically complete, ascertainment is needed, but not in the other? Such distinction as there is would seem to lie in the extent of the survey which the trustee is required to carry out: if he has to distribute the whole of a fund's income, he must necessarily make a wider and more systematic survey than if his duty is expressed in terms of a power to make grants. But just as, in the case of a power, it is possible to underestimate the fiduciary obligation

> of the trustee to whom it is given, so, in the case of a trust (trust power), the danger lies in overstating what the trustee requires to know or to inquire into before he can properly execute his trust.'

Those observations were directed to the test for validity of a trust creating a duty to distribute within a very wide class, which was said to depend on whether the court could enforce the duty. In *Re Pauling's Settlement Trusts* [1964] Ch 303, [1963] 3 All ER 1, [1963] 3 WLR 742, which was the basis for some of the submissions made to the court in *Re Hastings-Bass*, at issue was the propriety of a number of advancements made under a particular provision in a settlement. The Court of Appeal said this about the exercise of the power at p 333:

> 'Being a fiduciary power, it seems to us quite clear that the power can be exercised only if it is for the benefit of the child or remoter issue to be advanced or, as was said during argument, it is thought to be 'a good thing' for the advanced person to have a share of capital before his or her due time. That this must be so, we think, follows from a consideration of the fact that the parties to a settlement intend the normal trusts to take effect, and that a power of advancement be exercised only if there is some good reason for it. That good reason must be beneficial to the person to be advanced; it cannot be exercised capriciously or with some other benefit in view. The trustees, before exercising the power, have to weigh on the one side the benefit to the proposed advance, and on the other hand the rights of those who are or may hereafter become interested under the trusts of the settlement.'

I have already quoted passages from the judgment of the Court of Appeal in *Re Hastings-Bass* which were influenced by the earlier decision, including that set out at para 52 above. Issues have in the past arisen as to whether a particular disposition is within the scope of the statutory power of advancement. As a notable example, the power has been held to enable trustees to advance money directly to charity if the beneficiary to be advanced in this way accepts that he is under a moral obligation to make donations to charity. In such a case it is for the benefit of the advancee to have his moral obligation to charity discharged more economically than if he made equivalent provision out of his own assets: *Re Clore's Settlement Trusts* [1966] 2 All ER 272, [1966] 1 WLR 955, 110 Sol Jo 252. That shows the width of the factors that may be regarded as relevant in a given case.

I have quoted at para 76 above a pertinent passage from the judgment of Chadwick LJ in Edge *v* Pensions Ombudsman [[2000] Ch 602] referring to the duty of trustees to give proper consideration to the matters which are relevant.

In addition, trustees are under a duty of care, obliging them to exercise such skill and care as is reasonable in the circumstances, under s 1 of the Trustee Act 2000. This puts into statutory form (in relation to specific functions of the trustees) the duty recognised in *Speight v Gaunt* (1883) 22 Ch D 727 and (1883) 9 App Cas 1, which continues to apply to cases where the statutory duty does not.

To consider the point from another angle, we were taken to the decision of Lord Truro, Lord Chancellor, in *Re Beloved Wilkes' Charity* (1851) 20 LJ Ch 588, (1851) 3 Mac & G 440, 17 LTOS 101, in which a decision by charity trustees to identify a particular young man as the appropriate object of the charity was challenged. The trustees had not stated the reasons for their decision, and the judgment is important, among other things, as recognising that charity trustees are not under a duty to give reasons for such a decision. So far as the substance of the trustees' duty is concerned, Lord Truro said at p 448:

> 'it is to the discretion of the trustees that the execution of the trust is confided, that discretion being exercised with an entire absence of indirect motive, with honesty of

> intention, and with a fair consideration of the subject. The duty of supervision on the part of this court will thus be confined to the question of the honesty, integrity, and fairness with which the deliberation has been conducted, and will not be extended to the accuracy of the conclusion arrived at, except in particular cases. If, however, as stated by Lord Ellenborough in *The King v The Archbishop of Canterbury* (15 East 117), trustees think fit to state a reason, and the reason is one which does not justify their conclusion, then the court may say that they have acted by mistake and in error, and that it will correct their decision; but if, without entering into details, they simply state, as in many cases it would be most prudent and judicious for them to do, that they have met and considered and come to a conclusion, the court has then no means of saying that they have failed in their duty, or to consider the accuracy of their conclusion.'

The duty there stated to undertake 'a fair consideration of the subject', as part of the process of deciding how to exercise a power of choice as to the preferred object of the charity, has something in common with the duty addressed in more recent cases to take all relevant matters, and no irrelevant matters, into account, though it is stated in a less precise and possibly a less demanding manner.

We were reminded of *Gisborne v Gisborne* (1877) 2 App Cas 300, [1874–80] All ER Rep Ext 1698, 46 LJ Ch 556 in which the House of Lords declined to interfere with the exercise of a discretion given to trustees as being, in express terms, uncontrollable, Lord Cairns, Lord Chancellor, stating that the trustees' discretion is to be without any check or control from the court unless there be some bad faith as regards the exercise. That was a strong case;
the House of Lords did not call on Counsel for the Respondent trustees, and the judgments of the Court of Appeal in Chancery are not reported. While both this case and *Re Beloved Wilkes' Charity* make it clear that the court will respect the exercise by trustees of a discretion vested in them, neither of them excludes the possibility of challenge if it appears that the trustees have acted in breach of their duties in respect of the exercise, for example by failing to give fair consideration to the question.

Reference was also made to *Dundee General Hospitals Board of Management v Walker* [1952] 1 All ER 896, 1952 SC (HL) 78, 1952 SLT 270. The issue there was significantly different, as the gift claimed was payable only if the trustees were satisfied of a state of facts as to which, with the benefit of counsel's advice, they said that they were not so satisfied. That is not the same as a discretion to pay or not, as they thought fit.
Lord Reid (at p 905) said that even where trustees are expressed to have an absolute discretion:

> 'If it can be shown that the trustees considered the wrong question, or that, although they purported to consider the right question they did not really apply their minds to it or perversely shut their eyes to the facts or that they did not act honestly or in good faith, then there was no true decision and the court will intervene.'

In similar vein, Viscount Radcliffe said in *Pilkington* at [1964] AC 641: 'there does remain at all times a residual power in the court to restrain or correct any purported exercise that can be shown to be merely wanton or capricious and not to be attributable to a genuine discretion.'

Those cases set a high test for the ability of the court to intervene where trustees have exercised a discretion in a way that is within the terms of the relevant power. The task for the Claimant is all the greater if the trustees do not give reasons for their decision, though even in such a case reasons can often be inferred. In the cases since *Mettoy* the trustees have been forthcoming about their reasons, and have asserted their own failure to take into account a factor which they say they would have regarded as relevant.

What ought trustees to take into account?

The decided cases do not give a great deal of guidance in detail as to what the trustees ought to take into account, in the case of a private discretionary trust. (Pension trusts and charities may well each be different in some respects, as may be discretionary trusts for a very large class, such as that at issue in *Re Baden's Deed Trusts*, and I do not deal with such trusts for the present.) Older cases tended to focus on what ought not be to taken into account, such as personal disapproval: see *Klug v Klug* [1918] 2 Ch 67, 87 LJ Ch 569, 118 LT 696 and *Re Lofthouse* (1885) 29 ChD 921 at 925–6 (both being cases where the trustees declined to exercise their discretion). *Abacus v Barr* shows that the wishes of a settlor may well be one thing that trustees should take into account. The wishes, circumstances and needs of beneficiaries, so far as made known to the trustees, may also be relevant.

In *Sieff v Fox* I said that I was in no doubt that 'fiscal consequences may be relevant considerations which the trustees ought to take into account': see paras 85 and 86. I remain of that view. Although it is often said that decisions as regards the creation and operation of trusts ought not to be dictated by considerations of tax, the structure and development of personal taxation in the UK over the past decades, the use of trusts in order to deflect or defer the impact of taxation, and in turn the development of taxation as it applies to property held by trustees, have been such that there can be few instances in which trustees of a private discretionary trust with assets, trustees or beneficiaries in England and Wales could properly conclude that it was not relevant for them to address the impact of taxation that would or might result from a possible exercise of their discretionary dispositive powers.

In *Nestle v National Westminster Bank plc* [1994] 1 All ER 118 at 137, [1993] 1 WLR 1260, 12 LDAB 243 Staughton LJ held that the trustees were entitled and bound to take into account the fact that life tenants were not UK resident and that therefore, if the fund was invested in exempt gilts, the trust income to which they were entitled would not be subject to deduction of UK income tax. The other members of the court (Dillon and Leggatt LJJ) did not put that point in the same way and it is therefore not part of the ratio. Moreover the issue there was the proper investment of a fund which was not the subject of discretionary trusts. However, it is at least an indication supporting the relevance of fiscal matters. Similarly, fiscal considerations were relevant, for example, in *Re Clore's Settlement* (see para 105 above), and of course it was the prospect of a heavy liability to estate duty that led the trustees of the Hastings-Bass settlement itself to make the advancement that had to be considered in that case.

As Counsel pointed out, the extent of the proper consideration on the part of the trustees would be affected by the nature and circumstances of what was proposed. It might be different if what was proposed was the release from the trust of a relatively modest sum of capital to meet an extremely urgent need of one of several beneficiaries. In such a case it might not be necessary to undertake the same degree of enquiry and examination as it would be if the proposed transaction affected a very large proportion of the trust fund, or was not required as a matter of extreme urgency.

It is not possible to lay down any clear rule as to the matters which trustees ought to take into account when considering the exercise of a power of advancement or some other dispositive discretionary power. Circumstances will differ a great deal from one trust to another, and even within one trust they may change from time to time or according to the nature of the particular exercise which is under consideration.

Accordingly, although a number of cases heard during the 1990s sought to expand the scope of the *Hastings-Bass* judgment, beginning with the case of *Mettoy Pension Fund Trustees Ltd v Evans* [1990] 1 WLR 1587, recent cases have returned to the traditional *Hastings-Bass* approach. Essentially therefore, following the case of *Pitt v Holt* [2013] 3 All ER 429 (although see also the judgment of Lloyd LJ in the Court of Appeal [2011] EWCA Civ 197), there must be a breach of duty on the part of the trustees as opposed to insufficient deliberation. Lord Walker SCJ explains:

> Trustees may be liable, even if they have obtained apparently competent professional advice, if they act outside the scope of their powers (excessive execution), or contrary to the general law (for example, in the Australian case, the law regulating entitlement on intestacy). That can be seen as a form of strict liability in that it is imposed regardless of personal fault. Trustees may also be in breach of duty in failing to give proper consideration to the exercise of their discretionary powers, and a failure to take professional advice may amount to, or contribute to, a flawed decision-making process. But it would be contrary to principle and authority to impose a form of strict liability on trustees who conscientiously obtain and follow, in making a decision which is within the scope of their powers, apparently competent professional advice which turns out to be wrong.

Therefore *Hastings-Bass* can no longer be used where the beneficiaries merely disagree with the trustees' decision making. The decision must be such that it means that the trustees have not fulfilled their obligations, such as where they have conferred a benefit on a beneficiary in such a way that went beyond the objectives of the trust instrument.

EXTRACT

Firth, Michael L. (2013) 'Monetary Mistakes' *Taxation* 23 May

In the *Pitt* and *Futter* cases, the initial decisions in the High Court were in favour of the taxpayers. HMRC therefore appealed against the decisions and the Court of Appeal allowed the appeal, holding that the rule in *Re Hastings-Bass* did not apply and dismissing Mrs Pitt's alternative claim that her disposition, based on a mistake, should be rescinded. The taxpayers appealed to the Supreme Court.

Distilling the conjoined appeals down to their essence, the Supreme Court had to answer two questions:

(1) If a person in a fiduciary position takes a decision in the exercise of a discretion, but that decision was based on a mistake about the tax consequences of carrying it into effect, are the decision and its consequences voidable and does this bind HMRC? (Basically, whether the rule in re Hastings-Bass applied in these cases.)

(2) If a person (whether or not in a fiduciary position) makes a voluntary disposition (ie the recipient gives no consideration for it) and the decision to make that voluntary disposition was based on a mistake about the tax consequences of carrying it into effect, are the decision and its consequences voidable and does this bind HMRC? (Whether the disposition could be rescinded on the grounds of mistake.)

The answer to the first question was that if the fiduciary has taken advice from a professional, then he or she has discharged his or her fiduciary duties and the court will not interfere with the disposition on that basis. The answer to the second question was that if the mistake is

sufficiently serious and it would be unconscionable to uphold the disposition, the disposition (and, therefore, its tax consequences) can be set aside . . . The disposition would only be voidable on this basis if the fiduciary had acted in breach of his or her duty, and because both Mr Futter and Mrs Pitt had taken professional tax advice, they were not in breach of their duties. . . . The second question (ground 2) addressed by the Supreme Court related to voluntary dispositions and mistakes about tax . . . the Supreme Court accepted that although Mrs Pitt had never considered inheritance tax, she held an incorrect conscious belief that her disposition would have no adverse tax consequences and this was sufficiently serious to merit equity's intervention. Very little additional guidance on 'seriousness' was given and its meaning will certainly require development on a case-by-case basis.

Impartiality

Another important duty is that of impartiality, as Turner LJ explains in *Re Tempest* (1866) LR 1 Ch App 485 at p.487:

> Another rule which may, I think, safely be laid down is this – that the Court will not appoint a person to be trustee with a view to the interest of some of the persons interested under the trust, in opposition either to the wishes of the testator or to the interests of others of the *cestuis que* trusts. I think so for this reason, that it is of the essence of the duty of every trustee to hold an even hand between the parties interested under the trust. Every trustee is in duty bound to look to the interests of all, and not of any particular member or class of members of his *cestuis que* trusts.

While on the one hand this encompasses the duty not to allow personal interests to conflict with the obligation of trusteeship, discussed above, this duty also encompasses the duty to act impartially as regards the different beneficiaries and as regards the different classes of beneficiaries.[39] This means that the trustee should not confer a benefit on those with an immediate entitlement to the detriment of those with a future entitlement, and, similarly, must not benefit those with a future entitlement to the detriment of those whose entitlement does not vest until some future time. For example, if a trust is created that divides a fund between Benny (who is an adult beneficiary) and Mina (who is an infant beneficiary below the age of 18) the trustee could pay Benny his or her share immediately. However, in doing so, the trustee must not deprive Mina of her entitlement. Similarly, if the trust confers a life interest on Dai and then provides that Vita is entitled to the remainder on Dai's death, the trustee has a duty to ensure that the capital of the trust fund is not depleted by the payments to Dai, but must also ensure that the fund generates a suitable income to be given to Vita.[40] In the case of *Re Tempest*[41] for example, the testator's will gave the appellants the power to appoint trustees to administer the will. One of the appellants objected to the choice of trustee on the basis that there was evidence to suggest that he would not act fairly in relation to the different beneficiaries, and that he would benefit some of the beneficiaries to the detriment of the others. Turner LJ explains:

> Then, as to the second ground, the objection to the appointment of Mr. Petre seems to me to be still more decisive. The evidence, in my opinion, very plainly shews that Mr. Petre has been proposed as trustee, and has accepted that office, with a view to his acting in the trust in the interests of some only of the objects of it, and in opposition to the

[39] *Stephenson v Barclays Bank Trust Co Ltd* [1975] 1 WLR 882.
[40] *Re Barton's Trusts* (1868) LR 5 Eq 238.
[41] (1866) LR 1 Ch App. 485.

> wishes of the testator, and not with a view to his acting as an independent trustee for the benefit of all the objects of the trusts, and I do not hesitate to say that, in my opinion, this fact is alone sufficient to prevent us from confirming his appointment. It was objected on the part of the respondents, that the proof of this fact rests upon evidence of what has occurred since the order under appeal was pronounced and ought not, therefore, to be attended to; but this is a re-hearing of the Petition under which Mr. Petre has been appointed. The question before us, therefore, is, whether he ought now to be appointed or not – a question of his present fitness or unfitness – and I am aware of no rule which precludes us from receiving upon such a question evidence of what has occurred since the original hearing. Supposing, however, that there was any difficulty upon that point, I apprehend there can be no doubt that the evidence of what has so occurred ought to be looked at as shewing the purpose for which he was proposed, and that it was not proper that he should be appointed at the time when the order appointing him was made. It was also argued on the part of the respondents, that their interests ought to be considered in the appointment to be made by the Court, and there would have been great force in this argument, if it could have been considered that Mr. Petre was proposed as an independent trustee to act on behalf of, and with a view to, the interests of all the *cestui que* trusts; but when the purpose for which he is proposed is seen, this argument loses all weight and cannot be attended to. It is in the appointment of a trustee for the benefit of all, and not with a view to the interests of some, that the wishes of cestui que trusts are to be consulted, for the trustee to be appointed must represent and consult the interests of all, and not of some only of the cestui que trusts. It was indeed with this view, that in the course of the argument I suggested to the parties the expediency of their agreeing upon the appointment of an independent trustee.

Accordingly, because the proposed trustee was likely to breach the duty to act impartially in relation to the beneficiaries, the court appointed a more suitable trustee in his place.

Duty to act personally

Historically, the trustee had a duty to act personally. As has been shown, the Trustee Act 2000 in particular grants wide powers of delegation. Nevertheless, there are some functions of the trustee that remain non-delegable, namely decisions regarding the distribution of assets, decisions regarding whether payments should be made from income or capital, and the appointment of trustees or agents, nominees and custodians (Trustee Act 2000, s.11). In relation to charitable trusts most functions are non-delegable, with the exception of investments, fundraising and other functions prescribed by an order made by the Secretary of State.

Unanimity

With the exception of charitable trusts and pension trusts where the trustees may act pursuant to a majority decision, the administration of a trust requires the trustees to act unanimously, as Lord Jessel MR confirms in *Luke v South Kensington Hotel Company* (1879) 11 Ch D 121:

> . . . two out of three trustees have no power to bind cestuis que trust. There is no law that I am acquainted with which enables the majority of trustees to bind the minority. The only power to bind is the act of the three, and consequently the act of the two, even if it could bind them by reason of delay or acquiescence, could not bind the trust estate, and therefore in no way was the trust estate bound or the mortgage released.

Trustees' powers

The nature of the trustee's powers fall under two main headings. Firstly, there are powers concerning the administration of the trust, and secondly there are powers concerned with the distribution of trust property. Administration powers relate to the trustees' powers in terms of managing and investing the trust property, as well as how best to maintain it. Dispositive powers on the other hand relate to the power to distribute the trust fund to the beneficiaries.

Administration powers

Administration powers therefore include some of the situations described above such as the power to appoint agents (and the duties that arise where that occurs), the power to invest the trust fund, the power to insure and the power to acquire land – all of which, if exercised are subject to the duty of care detailed in s.1 Trustee Act 2000. On the other hand disposition powers include the trustees' powers under a discretionary trust to select the beneficiaries and the sum each beneficiary is entitled to receive.

Advancement and maintenance

A specific aspect of the dispositive power is the power of maintenance and advancement conferred either by the trust instrument, or by statute in the form of s.31 and s.32 Trustee Act 1925. Section 31 permits the trustee to pay income from the trust fund for the maintenance or education of an infant or a person who is over the age of 18 whose interest has not yet vested.[42] This means that where there is a need to maintain a beneficiary, the trustee may use the income from the trust fund in order to achieve that objective. Accordingly, the income from the fund may be used to pay any sum required for the maintenance of the child. This may include basic provision such as food and clothing, but could also include aspects such as a child's school fees, or for any specific or specialist equipment that the child may require because of a disability – or indeed a talent. The income from the fund may also be used to maintain an adult whose interest has not yet vested, such as the beneficiary who has an interest in remainder after the death of a person who owns a life interest, or a trust whereby the beneficiary does not become entitled to the trust fund until he reaches an age that is older than 18.

The trustees also have the power of advancement under s.32 Trustee Act 1925. Advancement is a payment out of capital or income to any person who is entitled to a vested or a contingent[43] interest in the trust fund. Therefore, a beneficiary who is currently entitled to the trust fund, or a beneficiary who will become entitled once a particular contingency has occurred (such as reaching the age of 18) may be given an advancement of up to half their entitlement. Advancement or benefit for the purposes of s.32 means improving the material situation of the beneficiary,[44] and accordingly,

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[42] Vesting is the term used to describe when a person becomes entitled to a trust fund. An adult beneficiary's interest is vested from the date upon which the trust comes into effect – they are entitled to the trust fund from that date. A child on the other hand may not be entitled to receive the trust fund until they are 18. Their interest does not vest in them until they reach the age of 18.

[43] A contingent interest is an interest to which a beneficiary may or may not become entitled. For example, a trust along the lines of 'to A, or if A predeceases me, to B'. B's interest in this case is contingent – B may be a beneficiary under the trust, but his entitlement is contingent upon A predeceasing the settlor. If A survives, then B is not entitled to benefit from the trust.

[44] *Pilkington v IRC* [1964] AC 612.

enabling the beneficiary to fulfil a moral obligation to a charity was accepted as a form of advancement or benefit,[45] as was setting a person up in business,[46] or repaying debts owed by the beneficiary.[47] However, the trustees must not advance more than one half of the beneficiary's share (s.32(1)(a)), and the beneficiary cannot benefit twice from the trust. Therefore if William and Harry are to receive the benefit of a £100,000 trust fund in equal shares, and the trustees make an advancement to William of £20,000 of his share, the trustees must take this into account, so that when the trust fund comes to be distributed, William cannot then claim half of the money left over in the fund (£40,000). Instead, when the trust fund comes to be distributed, William will get £30,000 and Harry will get £50,000 to take account of the fact that William has already been granted part of his entitlement. The third restriction on advancement is that any person whose prior interest would be prejudiced by the advancement must consent to the proposed arrangement.

Where the trustee exercises a power, he or she must exercise that power reasonably, and in good faith, and the court will not interfere with the exercise of a power undertaken in this way.[48] However, in order to show good faith, the trustee must not consider factors that are irrelevant to making the decision.

EXTRACT

Edge v Pensions Ombudsman [1999] 1 All ER 546

Case facts

The trustees of a pension trust amended the pension scheme in order to provide an additional credit for scheme members who were still in work. Retired members complained that this constituted a breach of trust because the trust favoured members who were still in work over retired members. The Pension Ombudsman accepted this view. However, the claimants appealed, arguing that the Pension Ombudsman was not entitled to interfere with the trustees' decision simply because he would have considered different relevant factors.[49] However, the case of *Re Hastings-Bass* confirms that the court will intervene if the trustee exercises a power in such a way that he or she would not have embarked upon if he or she had considered relevant factors.

Chadwick LJ

The need to consider the circumstances in which the surplus has arisen does not lead to the conclusion that the trustees are bound to take any particular course as a result of that consideration. They are not constrained by any rule of law either to increase benefits or to reduce contributions or to adopt any particular combination of those options. Nor does the need to consider the circumstances in which the surplus has arisen lead to the conclusion that the trustees are not required to take – or are prohibited from taking – any other matters into account in deciding what course to adopt. They must, for example, always have in mind the

[45] *Re Clore's Settlement Trusts* [1966] 2 All ER 272.
[46] *Re Kershaw's Trusts* (1868) LR 3 Eq 322.
[47] *Lowther v Bentinck* (1874) LR 19 Eq 166.
[48] *Gisborne v Gisborne* (1877) 2 App Cas 300.
[49] *Edge v Pensions Ombudsman* [1999] 4 All ER 546.

main purpose of the scheme – to provide retirement and other benefits for employees of the participating employers. They must consider the effect that any course which they are minded to take will have on the financial ability of the employers to make the contributions which that course will entail. They must be careful not to impose burdens which imperil the continuity and proper development of the employers' business or the employment of the members who work in that business. The main purpose of the scheme is not served by putting an employer out of business. They must also consider the level of benefits under their scheme relative to the benefits under comparable schemes; or in the pensions market generally. They should ask themselves whether the scheme is attractive to the members whose willingness to continue paying contributions is essential to its future funding. Are the benefits seen by the members to be good value in relation to the contributions; would the members find it more attractive to pay higher contributions for higher benefits; or to pay lower contributions and accept lower benefits? The main purpose of the scheme is not served by setting contributions and benefits at levels which deter employees from joining; or which causes resentment. And they must ask themselves whether the benefits enjoyed by members in pension have kept up with increases in the cost of living; so that the expectations of those members during their service – that they were making adequate provision for their retirement through contributions to an occupational pensions scheme – are not defeated by inflation.

The matters to which we have referred are not to be taken as an exhaustive or a prescriptive list. It is likely that, in most circumstances, pensions trustees who fail to take those matters into account will be open to criticism. But there may well be other matters which are of equal or greater importance in the particular circumstances with which trustees are faced. The essential requirement is that the trustees address themselves to the question what is fair and equitable in all the circumstances. The weight to be given to one factor as against another is for them.

> Properly understood, the so-called duty to act impartially-on which the ombudsman placed such reliance-is no more than the ordinary duty which the law imposes on a person who is entrusted with the exercise of a discretionary power: that he exercises the power for the purpose for which it is given, giving proper consideration to the matters which are relevant and excluding from consideration matters which are irrelevant. If pension fund trustees do that, they cannot be criticised if they reach a decision which appears to prefer the claims of one interest-whether that of employers, current employees or pensioners-over others. The preference will be the result of a proper exercise of the discretionary power.

Delegation

The trustees have the power to delegate some of their functions if they wish. The extent to which this is permitted is discussed further in relation to how the duty of care must be exercised (above).

Obtaining advice

In addition to delegation, the trustees may obtain advice regarding the operation and administration of the trust. Indeed s.5 Trustee Act 2000 requires that the trustees obtain advice before investing or reviewing the investments, unless they consider that doing so would be inappropriate – such as where one of the trustees is a financial expert.

The power to give receipts

Under s.14 Trustee Act 1925, the trustees have the power to give receipts for monies received, and doing so will discharge those who have paid the money from further liability under the trust. In land law for example, the fact that there is a minimum of two trustees in relation to a trust of land means that the interests of a beneficiary under a trust, or a person who has contributed to the purchase price, may be overreached in accordance with s.2 of the Law of Property Act 1925. What this means therefore is that the buyer of the land owes no further obligation to the beneficiaries, and it is not possible for the beneficiary to argue that their interest in the land is overriding under Schedule 3 to the Land Registration Act 2002[50] against the buyer.[51]

The power to compromise

Section 15 of the Trustee Act 1925 permits the trustees to compromise in relation to litigation. Therefore, where it is appropriate to settle a dispute, or to reach a compromise agreement between the parties, the trustees may consent to this if it is appropriate in all the circumstances. Although the financial interests of the beneficiaries are an important factor in this consideration, it is not the only consideration, as the case of *Re Ridsdel* [1947] Ch 597 demonstrates.

Dispositive powers

Dispositive powers relate to the powers of a trustee to determine how to distribute the trust fund. For example, a trust may give the trustees the power to decide upon the appropriate means of distributing the funds in a discretionary trust fund between the beneficiaries. This may mean identifying which beneficiaries from the larger class are to benefit from the fund and how much each should receive. For example, where a trust supports educational grants, the amount awarded will depend on factors such as the number of applicants to the fund, the quality of their application, and their evidence of financial need. The Wellcome Trust, a charity that funds research into human and animal health for example explains that it determines awards based on:

> The Trust's decision-making committees comprise independent scientists from the research community with appropriate expertise and research experience. They are asked to express their own views on the research proposal and to adjudicate on the external expert opinions received on it.[52]

Furthermore, the trustees have the power to award the grant in full, or to award a reduced grant. The trustees also have the power to attach conditions to the grant, and to defer the award of the grant until further information has been obtained. With some types of trust, known as non-exhaustive trusts, the trustees may be given the power to defer the payment of the fund. Again this may be more common with charitable trusts, where the trustees may decide that in a given period, no applicant is eligible to receive the fund. Consider for example, the situation where prizes are awarded for outstanding performance in examinations. Perhaps in a given year, no student fulfils the eligibility criteria for the prize to be awarded. If that is the case, then the trustees have the power

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[50] (2002 c.9).

[51] *City of London Building Society v Flagg* [1987] 3 All ER 435.

[52] The Wellcome Trust (2013) 'Grant decision making process' http://www.wellcome.ac.uk/Funding/Biomedical-science/Application-information/WTD004051.htm (site accessed 29 July 2013).

to withhold the prize until such time as when an eligible candidate emerges. With an exhaustive trust however, the trustees' powers are more limited – they must award the prize to the most deserving candidate, even though their performance has been mediocre.

Breach of trust

An act or omission which is in breach of the trustee's duties will be a breach of trust.[53] Acting in excess of the permitted authority will also constitute a breach, as will neglecting to fulfil a duty. Acquiescence to a breach of trust committed by the other trustees will also be a breach of trust.[54] Where the trustee's breach has caused a loss to the trust fund, then the trustee will be required to account for that loss, and repay the sum lost to the beneficiary. The key case in relation to breaches of trust is the case of *Target Holdings v Redferns* [1996] 1 AC 421.

EXTRACT

Target Holdings v Redferns [1996] 1 AC 421

Case facts

This case concerned a firm of solicitors which was acting for both the mortgagor and the mortgagee in a mortgage transaction. The property that was to be the subject of the mortgage loan had been valued at £2 million. However, the mortgagor was only paying £775,000 for it. Having received the money from the mortgagee, the solicitor then paid the money to the buyer before the purchase had been completed, and failed to ensure that the charge on the land had been registered, meaning that if the mortgagor failed to repay the loan, the mortgagee could sue for breach of contract, but could not sell the land in order to recover the loan, nor enforce the mortgage against subsequent owners. The mortgagee therefore sued the solicitor arguing that the firm had acted in breach of trust.

Lord Browne-Wilkinson

The transaction in the present case is redolent of fraud and negligence. But, in considering the principles involved, suspicions of such wrongdoing must be put on one side. If the law as stated by the Court of Appeal is correct, it applies to cases where the breach of trust involves no suspicion of fraud or negligence. For example, say an advance is made by a lender to an honest borrower in reliance on an entirely honest and accurate valuation. The sum to be advanced is paid into the client account of the lender's solicitors. Due to an honest and non-negligent error (e.g. an unforeseeable failure in the solicitors' computer) the moneys in client account are transferred by the solicitors to the borrower one day before the mortgage is executed. That is a breach of trust. Then the property market collapses and when the lender realises his security by sale he recovers only half the sum advanced. As I understand the Court of Appeal decision, the solicitors would bear the loss flowing from the collapse in the market value: subject to the court's discretionary power to relieve a trustee from liability under section 61 of the Trustee Act 1925, the solicitors would be bound to repay the total amount wrongly paid out of the client account in breach of trust receiving credit only for the sum received on the sale of the security.

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[53] *Target Holdings v Redferns* [1996] 1 AC 421.
[54] *Luke v South Kensington Hotel Co* (1879) 11 Ch D 121.

To my mind in the case of an unimpeachable transaction this would be an unjust and surprising conclusion. At common law there are two principles fundamental to the award of damages. First, that the defendant's wrongful act must cause the damage complained of. Second, that the plaintiff is to be put 'in the same position as he would have been in if he had not sustained the wrong for which he is now getting his compensation or reparation:' Although, as will appear, in many ways equity approaches liability for making good a breach of trust from a different starting point, in my judgment those two principles are applicable as much in equity as at common law. Under both systems liability is fault-based: the defendant is only liable for the consequences of the legal wrong he has done to the plaintiff and to make good the damage caused by such wrong. He is not responsible for damage not caused by his wrong or to pay by way of compensation more than the loss suffered from such wrong. The detailed rules of equity as to causation and the quantification of loss differ, at least ostensibly, from those applicable at common law. But the principles underlying both systems are the same. On the assumptions that had to be made in the present case until the factual issues are resolved (i.e. that the transaction would have gone through even if there had been no breach of trust), the result reached by the Court of Appeal does not accord with those principles. Redferns as trustees have been held liable to compensate Target for a loss caused otherwise than by the breach of trust . . . I approach the consideration of the relevant rules of equity with a strong predisposition against such a conclusion.

The considerations urged before your Lordships, although presented as a single argument leading to the conclusion that the views of the majority in the Court of Appeal are correct, on analysis comprise two separate lines of reasoning, viz.: (A) an argument developed by Mr. Patten (but not reflected in the reasons of the Court of Appeal) that Target is now (i.e. at the date of judgment) entitled to have the 'trust fund' restored by an order that Redferns reconstitute the trust fund by paying back into client account the moneys paid away in breach of trust. Once the trust fund is so reconstituted, Redferns as bare trustee for Target will have no answer to a claim by Target for the payment over of the moneys in the reconstituted 'trust fund.' Therefore, Mr. Patten says, it is proper now to order payment direct to Target of the whole sum improperly paid away, less the sum which Target has received on the sale of property; and (B) the argument accepted by the majority of the Court of Appeal that, because immediately after the moneys were paid away by Redferns in breach of trust there was an immediate right to have the 'trust fund' reconstituted, there was then an immediate loss to the trust fund for which loss Redferns are now liable to compensate Target direct.

The critical distinction between the two arguments is that argument (A) depends upon Target being entitled now to an order for restitution to the trust fund whereas argument (B) quantifies the compensation payable to Target as beneficiary by reference to a right to restitution to the trust fund at an earlier date and is not dependent upon Target having any right to have the client account reconstituted now.

Before dealing with these two lines of argument, it is desirable to say something about the approach to the principles under discussion. The argument both before the Court of Appeal and your Lordships concentrated on the equitable rules establishing the extent and quantification of the compensation payable by a trustee who is in breach of trust. In my judgment this approach is liable to lead to the wrong conclusions in the present case because it ignores an earlier and crucial question, viz., is the trustee who has committed a breach under any liability at all to the beneficiary complaining of the breach? There can be cases where, although there is an undoubted breach of trust, the trustee is under no liability at all to a beneficiary. For example, if a trustee commits a breach of trust with the acquiescence of one beneficiary, that beneficiary has no right to complain and an action for breach of trust brought by him would fail completely. Again there may be cases where the breach gives rise to no right

to compensation. Say, as often occurs, a trustee commits a judicious breach of trust by investing in an unauthorised investment which proves to be very profitable to the trust. A carping beneficiary could insist that the unauthorised investment be sold and the proceeds invested in authorised investments: but the trustee would be under no liability to pay compensation either to the trust fund or to the beneficiary because the breach has caused no loss to the trust fund. Therefore, in each case the first question is to ask what are the rights of the beneficiary: only if some relevant right has been infringed so as to give rise to a loss is it necessary to consider the extent of the trustee's liability to compensate for such loss.

The basic right of a beneficiary is to have the trust duly administered in accordance with the provisions of the trust instrument, if any, and the general law. Thus, in relation to a traditional trust where the fund is held in trust for a number of beneficiaries having different, usually successive, equitable interests, (e.g. A for life with remainder to B), the right of each beneficiary is to have the whole fund vested in the trustees so as to be available to satisfy his equitable interest when, and if, it falls into possession. Accordingly, in the case of a breach of such a trust involving the wrongful paying away of trust assets, the liability of the trustee is to restore to the trust fund, often called 'the trust estate,' what ought to have been there.

The equitable rules of compensation for breach of trust have been largely developed in relation to such traditional trusts, where the only way in which all the beneficiaries' rights can be protected is to restore to the trust fund what ought to be there. In such a case the basic rule is that a trustee in breach of trust must restore or pay to the trust estate either the assets which have been lost to the estate by reason of the breach or compensation for such loss. Courts of Equity did not award damages but, acting *in personam*, ordered the defaulting trustee to restore the trust estate . . . Thus the common law rules of remoteness of damage and causation do not apply. However there does have to be some causal connection between the breach of trust and the loss to the trust estate for which compensation is recoverable, viz. the fact that the loss would not have occurred but for the breach.

Outcome

The solicitor's appeal was allowed because the mortgagee had sustained no loss. Despite the suspicions of fraud and negligence on the part of the solicitor, the mortgagee was in exactly the same situation as he would have been had the trust not been breached.

However, the beneficiaries may choose to condone the breach, and may in fact prefer to do so if there has been no loss to the trust. Therefore if a trustee has made a personal gain, alongside the trust – as in the situation that arose in *Boardman v Phipps* (discussed above), the beneficiary may prefer to condone the breach rather than go to the expense of undertaking litigation where he or she can prove no loss. The modern approach to breaches of trust has developed along similar lines to the law of negligence, in that there is a need to show that the defendant trustee's conduct caused the loss.[55] Earlier case law seemed to place greater store upon the notion of strict liability.[56]

A trust, being an equitable obligation is also remedied in equity, which means that the appropriate remedy is at the court's discretion. Therefore, in situations where there has been a failure to exercise a duty, it is likely that accounting for the loss will be the preferred remedy. However, where there has been a dishonest misappropriation of the trust fund on the part of the trustee, then there will also be criminal liability for theft, and therefore the criminal courts may award compensation to the beneficiary.

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[55] *Target Holdings v Redferns* [1996] 1 AC 421.
[56] *Clough v Bond* (1838) 3 My & Cr 490.

In other contexts a form of injunction may be appropriate, such as, for example, a *quia timet* injunction where a breach is threatened, or a freezing injunction where the trustee is threatening to dissipate assets pending trial. Injunctions are discussed further in Chapter 5.

Vacating the office of trustee

There are many ways in which the office of trusteeship may become vacant. The trustee may die, or may choose to retire from office (as is permitted under s.36 Trustee Act 1925). Section 36 permits a trustee to refuse to accept the obligation, or, having been a trustee for a period of time, may choose to retire from that office. However, the trustee may also be removed from office either in accordance with the terms of the trust instrument, or if the beneficiaries or the court so directs. Again, the governing law is s.36, which provides that a trustee may be removed by the other trustees if he or she is out of the jurisdiction, or if he or she is incapable or unfit to act, or if he or she is a child. The beneficiaries may also require that a trustee is removed according to the principle in *Saunders v Vautier* (1841) 4 Beav 115. Alternatively, s.41 permits the court to remove a trustee, if it considers that it would be appropriate to do so. In the case of *Re Tempest* (1866) 1 Ch 485, Turner LJ considered the grounds upon which the court would intervene in order to remove a trustee:

> It was said in argument, and has been frequently said, that in making such appointments the Court acts upon and exercises its discretion; and this, no doubt, is generally true; but the discretion which the Court has and exercises in making such appointments, is not, as I conceive, a mere arbitrary discretion, but a discretion in the exercise of which the Court is, and ought to be, guided by some general rules and principles, and, in my opinion, the difficulty which the Court has to encounter in these cases lies not so much in ascertaining the rules and principles by which it ought to be guided, as in applying those rules and principles to the varying circumstances of each particular case. The following rules and principles may, I think, safely be laid down as applying to all cases of appointments by the Court of new trustees. First, the Court will have regard to the wishes of the persons by whom the trust has been created, if expressed in the instrument creating the trust, or clearly to be collected from it. I think this rule may be safely laid down, because if the author of the trust has in terms declared that a particular person, or a person filling a particular character, should not be a trustee of the instrument, there cannot, as I apprehend, be the least doubt that the Court would not appoint to the office a person whose appointment was so prohibited, and I do not think that upon a question of this description any distinction can be drawn between express declarations and demonstrated intention. The analogy of the course which the Court pursues in the appointment of guardians affords, I think, some support to this rule. The Court in those cases attends to the wishes of the parents, however informally they may be expressed.
>
> Another rule which may, I think, safely be laid down is this – that the Court will not appoint a person to be trustee with a view to the interest of some of the persons interested under the trust, in opposition either to the wishes of the testator or to the interests of others of the *cestuis que* trusts. I think so for this reason, that it is of the essence of the duty of every trustee to hold an even hand between the parties interested under the trust. Every trustee is in duty bound to look to the interests of all, and not of any particular member or class of members of his *cestuis que* trusts.

> A third rule which, I think, may safely be laid down, is, – that the Court in appointing a trustee will have regard to the question, whether his appointment will promote or impede the execution of the trust, for the very purpose of the appointment is that the trust may be better carried into execution.

Therefore, where the trustee has committed a breach of trust that involves dishonest conduct, or conduct that is grossly negligent, the beneficiaries or the court may direct that the trustee is removed.

What is shown in this chapter is that the obligations imposed on a trustee are significant. His or her duties are extensive, and the rights and powers of the trustees are restricted, to a large extent, to entitlements to act in a way that benefits the trust. Accordingly, the character and responsibility of the trustee are paramount to the trust relationship.

Chapter summary

This chapter may be useful for assessments and assignments on:

- The powers and duties of a trustee
- The role of the trustee
- The trustee's duty of care
- Investment of the trust fund
- Gains and losses made by the trustee.

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12

The beneficiary

Chapter outline

This chapter will consider:

- Who may be a beneficiary?
- The beneficiary's role
- The rights of the beneficiary.

Introduction

In many ways, the beneficiary is the most important party in the trust relationship and, as has been shown in Chapter 8, no valid trust can exist without there being certainty as to the identity of the beneficiaries. Accordingly, in this chapter the role and identities of the beneficiary will be considered.

Who may be a beneficiary?

The beneficiary may encompass a broad range of person, and there are no requirements regarding age and capacity. Indeed, in the family context, a trust may be set up precisely because the intended beneficiary does not possess the required age or capacity to be able to own or deal with property on their own behalf. A beneficiary may be an individual, as in the case where a person writes a will leaving specific items of property to a named individual. Furthermore, the case of *Re Bowles* [1902] 2 Ch 650 demonstrates that the beneficiary under a trust may even be someone who does not yet exist. In *Re Bowles*, a trust was created for the benefit of any issue of George and Anne Downing. However the trust stipulated that in order to be a beneficiary under the trust, the issue had to be born during the lifetime of either George or Anne. Therefore, when the trust was created, on the marriage of George Downing to his wife Anne, they had no children. However, the trust was created, so that when either of them died, the other would acquire a life interest in the trust property, with the remainder going to the children and any remoter issue who were in existence when the survivor died.

What this means is that if Marie and Rich are married, and Marie dies, Rich will obtain a life interest for his lifetime, and then on his death, the estate would be divided between any of his children or his children's children etc. who were living at the time of Rich's death. Therefore if Marie and Rich had three grown-up children, Alice, Bob and Carol, and Alice had two children of her own, then Alice, Bob, Carol and Alice's two children would inherit the estate. It is of course possible that Bob and Carol might have children after Rich's death. However, under the terms of the trust in *Re Bowles*, those children would not be permitted to inherit. The extent to which unborn children may inherit in this way will depend on the term of the trust, and also on ensuring that the trust comes to an end within the perpetuity period. By only permitting the trust to subsist in favour of those alive at the time of the settlor's death ensures that the trust does not breach the rule against perpetuities.

On the other hand, there is a possibility that some types of trusts of this nature, such as a trust that includes future-born grandchildren, could conflict with the rule against perpetuities. Consider the situation described above again. Marie writes a will leaving Rich a life interest, and then distributing the remainder between Marie's children, grand-children and great grand-children. When Marie dies in 2001, her son Bob is one year old. When Bob is 80 years old (in 2080) he fathers a son, Dennis. When Dennis is 50, he fathers a daughter, Ellen. However, this trust would fall outside the perpetuity period, and would fail unless it is stipulated that only beneficiaries born within the perpetuity period could inherit.

Beneficiaries may also be a group of persons, and the group may be a small group – such as the settlor's children collectively. In *Re Hastings-Bass* [1974] Ch 25, the sole beneficiary was the settlor's eldest son, one William Edward Robin Hood Hastings-Bass, while in the case of *Inland Revenue Commissioners v Trustees of Sir John Aird's Settlement* [1984] Ch 382, the beneficiaries were the settlor's two children – John and Susan Aird.

However, the group of beneficiaries may also be comparatively large, such as, for example, the members of a society or a club, or a company's customers. For example, in *Re Denley's Deed Trust* [1972] 1 Ch 73, the trust was for the benefit of a company's employees.

Furthermore, under a charitable trust, the beneficiaries may comprise of the public at large. Therefore a museum or an art gallery that has charitable status will confer a benefit upon anyone who chooses to visit the gallery, as well as those who may benefit from the materials produced by the gallery, and its programme of activities for schools and other institutions. For example, the Tate Galleries[1] are a charity, and the public may benefit from visiting the galleries and being able to access the artworks they contain. However, the Tate also produces research resources, commissions research, provides a library and has an archive of records and materials. The benefit to the public is more extensive therefore than merely the galleries themselves.

The role of the beneficiary

Unlike the settlor and the trustee, the beneficiary does not have a specific role to perform – the trust exists for his or her benefit, and the beneficiary does not therefore have any obligation under the trust. Indeed, as has been demonstrated, this is sometimes imperative because the purpose of the trust is for the benefit of those who are not able to safeguard their own interests. Therefore in *Re T's Settlement Trusts* [1964] Ch 158, the trust was for the benefit of two infants, and the application was made in order to postpone the entitlement of one of them on the basis that her mother described her as '*irresponsible and immature*'.

Nevertheless, the beneficiary may wish to oversee the proper administration of the trust, and is entitled therefore to request the trust accounts[2] from the trustee as well as any documents about the trust.[3] The trustee has a duty to provide this information, which will assist the beneficiary in determining whether there has been a breach of the trust.[4] However, as we have seen, this does not extend to confidential information, for example information concerning the income of the trust when one is only entitled to the capital,[5] or information concerning the trustees' decisions,[6] although the judgment in *Schmidt v Rosewood Trust Ltd* [2003] 2 WLR 1442 indicates that the court has the power to order access to trust documents under its inherent jurisdiction, and therefore the beneficiaries could apply to the court if they considered that it was necessary for them to inspect the trust.

It is the beneficiary, and not the settlor who is entitled to sue in the event that there has been a breach of the trust. Once the trust has been created and the property transferred to the trustee, the settlor, as has been demonstrated in Chapter 8, plays no further part in the trust relationship. The settlor cannot therefore sue if the trust obligation has not been carried out in accordance with his or her directions. However, the beneficiary may sue if the trustee does not fulfil the obligations of the trust.[7]

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[1] Tate (2012) Research. www.tate.org.uk. Site accessed 28 August 2012.
[2] *O'Rourke v Darbishire* [1920] AC 581.
[3] *Hawksley v May* [1956] 1 QB 304.
[4] *Springett v Dashwood* (1860) 2 Giff 521.
[5] *Nestle v National Westminster Bank PLC* [1994] 1 All ER 118.
[6] *Re Londonderry* [1964] 3 All ER 855.
[7] *Morice v Bishop of Durham* (1805) 9 Ves 399.

The rights of the beneficiary

The beneficiary has a number of rights under a trust. These include:

The right to sue

A beneficiary is entitled to sue the trustee if the trust is breached. However, it is generally thought that the beneficiary's right of action lies only against the trustee, and therefore the beneficiary cannot litigate against, for an example, an agent who has acted wilfully or negligently in such a way as to cause a loss to the trust; a proposition that is outlined by Hargreaves in 'The nature of beneficiaries' rights under trusts'[8] where she explains:

> The first proposition is that, as a matter of jurisdictional history, a trust beneficiary cannot rely on his equitable title in order to ground a common law claim. For the purposes of this article, it suffices to note that traditionally 'the common law did not recognise the equitable title of the beneficiary under the trust', such that a beneficiary could not enforce his rights in the common law courts using common law claims. As Rushworth and Scott explain: 'As against the claimant, the defendant breaches no common law duty, and equity's jurisdiction over the defendant, as a stranger to the trust, is not engaged.'
>
> The second proposition is that, because of the special nature of the 'trustee-beneficiary relationship', the beneficiary has rights only against the trustee. This is because 'the interest of the beneficiary (however analysed) is derivative rather than competitive,' or in other words, the trustee-beneficiary relationship is parasitic. The trustee holds the legal title while the beneficiary has the rights to the benefit of the property. Any claim in relation to the trust property is therefore vested in the trustee who, as part of their duty to protect the trust property, has a duty to sue third parties who interfere with the trust. The trustee is the proper claimant. The beneficiary can only enforce their beneficial interest indirectly through the trustee.

Nevertheless, Hargreaves argues that allowing the beneficiary to litigate may be advantageous in some situations such as, for example, where the trustee refuses to litigate or where the trustee has suffered no loss.

Entitlement to the trust property

Generally, the beneficiary is also entitled to the trust property. The beneficiary is treated as the 'true' owner of the trust property, and therefore an adult beneficiary may require that the trust fund be transferred to him or her under the principle in *Saunders v Vautier* (1841) 4 Beav 115. The trust property is also treated as belonging to the beneficiary, and the beneficiary may therefore create a trust out of their own equitable interest.

Nevertheless, the law distinguishes between a beneficiary and a beneficial owner. Where the trust is discretionary, a person does not become a beneficiary until the trustees have exercised their discretion in that individual's favour. Accordingly, the objects of a trust may sue for any breach of the trust even though they have no entitlement to the trust fund, and cannot therefore be classed as beneficiaries.[9] Instead, they are termed beneficial owners. They have a hope of being selected as beneficiaries, but have no

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[8] Hargreaves, E. (2011) 'The nature of beneficiaries' rights under trusts' *Trusts Law International* 163.

[9] *Richstar Enterprises Pty Ltd v Carey (No 6)* [2006] FCA 814.

entitlement to the trust fund. The extent of the object of a discretionary trust's rights is explained by Neuberger J in *Re Murphy's Settlements* [1998] 3 All ER 1, where he cites the judgment of Lord Templeman in *Re Manisty's Settlements*. Neuberger J explains:

> So far as the plaintiff's claim relating to the defendant's 1965 settlement is concerned, Mr McDonnell pointed out that, as a person in the class of discretionary beneficiaries under the trusts, the plaintiff has certain rights. These are described by Templeman J in *Re Manisty's Settlement* [1973] 2 All ER 1203 at 1210, [1974] Ch 17 at 25:
>
> > 'If a person within the ambit of the power is aware of its existence he can require the trustees to consider exercising the power and in particular to consider a request on his part for the power to be exercised in his favour. The trustees must consider this request, and if they decline to do so or can be proved to have omitted to do so, then the aggrieved person may apply to the court which may remove the trustees and appoint others in their place. This, as I understand it, is the only right and only remedy of any object of the power . . .'
>
> Further, Mr McDonnell said that, as a discretionary object of the defendant's 1965 settlement, the plaintiff is entitled to ask the trustees for information as to the nature and value of the trust property, the trust income, and as to how the trustees have been investing and distributing it. Although there is no English authority on this point, this submission appears to be supported by the Irish case of *Chaine-Nickson v Bank of Ireland* [1976] IR 393, and it is treated as being the law of England in the two leading textbooks on the topic, namely *Snell's Equity* (29th edn) pp 231–232 and *Underhill on Trusts and Trustees* (15th edn) p 657. On behalf of the defendant, Mr Mark Blackett-Ord, quite rightly in my view, accepts that the plaintiff does, as a matter of principle, have these rights in relation to the defendant's 1965 settlement.

The fact that the objects of a discretionary trust have no entitlement to the trust fund means that the settlor may use the discretionary trust in such a way as to keep family property outside the control of an irresponsible beneficiary. The fact that the trust is discretionary means that the irresponsible object of the trust cannot use his or her equitable interest as security for a loan. Neither can he or she sell or give away his or her equitable interest. Furthermore, the object of the trust cannot require that the trust fund is transferred to him or her without the consent of the other beneficial owners.

Accordingly, the discretionary trust may be a very astute way of conferring a benefit on a family member without him or her having control over the asset. For example, the trustees' discretion may be framed in such a way that the trustee's discretion only becomes exercisable once all the objects of the trust have proved in some way that they will not squander it. Alternatively, the trustees may have a discretion to ensure that a beneficial owner only receives the trust fund in modest proportions, thus preventing him or her from being able to deal with the trust fund in an irresponsible manner.

EXTRACT

Arter, A. (2012) 'Trusts and banking relationships – who is a beneficial owner?' *Trust Law International* 3

The creation of a business relationship between a trustee and a bank is subject to special considerations. These relate less to the relationship between trustee and bank under civil law, rather in the definition of the so-called beneficial owner who is also designated as a person

acting as beneficial owner. The concept of the beneficial owner first arises when entering into a banking relationship because the bank must determine who this is in order to comply with legislation concerning the fight against money laundering and the financing of terrorism . . . Moreover, the concept of the beneficial owner is in practice often erroneously used (and ratification of the Hague Trust Convention changed little in this regard) as a synonym for the concept of the beneficiary of a trust.

The beneficiary of a trust

The nature of trusts can vary according to various criteria. Express trusts, trusts by operation of law and statutory trusts differ in terms of the manner in which they are incorporated. Express trusts in fixed trusts and discretionary trusts differ in terms of the type of authorisation of the beneficiaries to the trust. The beneficiaries of fixed trusts have a definable, fixed claim to a share of the trust proceeds or trust capital. By contrast, discretionary trusts have no definable claim to a share of the trust proceeds or trust capital. Rather, it is at the trustees' discretion to determine the class of a beneficiary to which, if any, trust proceeds or trust capital received are to be paid out or who in the class of beneficiaries, for a determined period of time or duration, shall be included or excluded. Further distinctions can be made for discretionary trusts, such as whether the trustee is obliged to distribute trust proceeds or not, or if he merely has the discretionary power to decide to whom they shall be paid out, or whether the trustee can additionally decide, whether and to what extent distributions, if any, will be made. A fundamental difference between a fixed trust and a discretionary trust is that a beneficiary of a fixed trust has a claim to their share in the trust property against the trustee, whilst with a discretionary trust they merely hope that the trustee will exercise his authority in their favour. There can be no claim against the trustee until the trustee of a discretionary trust has exercised his authority over the disbursement of trust proceeds or trust capital in favour of a beneficiary.

Provisions relating to the fight against money laundering and terrorism in connection with trusts

A bank's due diligence procedures under the federal law on the fight against money laundering and terrorist financing in the finance sector states, inter alia, that a financial intermediary must identify the contracting part and must ascertain the person acting as beneficial owner . . .

The concept of beneficiary is interpreted differently from country to country. There is a particular lack of coherency regarding whether the concept of beneficiary simply means classes of beneficiaries or specific individuals.

The FATF recommendations reveal two things: on the one hand, the beneficial owner(s) is/are identified as the/those person(s) who actually determine the decision-making processes regarding assets and, on the other hand, information must – independent of the concept of beneficial owner – be available from trusts on the settlor, the trustee as well as on the beneficiaries. Otherwise it follows that, contrary to what was just illustrated by federal case law on the concept of beneficial owner who is the one who can actually dispose of assets and not the one to whom the assets belong to from an economic standpoint or, in other words, the one who benefits from them. Thus beneficial owner can thereby be either the one who can actually dispose of the assets or the one who benefits from them.

Wolfsberg Principles

The Wolfsberg Group comprising 11 global banks whose mission includes defining a set of standards for private banking has the following to say on beneficial owners:

> 'The term "beneficial ownership" is conventionally used in anti-money laundering contexts [. . .] to refer to that level of ownership in funds that, as a practical matter, equates with control

> over such funds or entitlement to such funds. "Control" or "entitlement" in this practical sense is to be distinguished from mere signature authority or mere legal title. The term reflects a recognition that a person in whose name an account is opened with a bank is not necessarily the person who ultimately controls such funds or who is ultimately entitled to such funds. This distinction is important because the focus of anti-money laundering guidelines [. . .] needs to be on the person who has this ultimate level of control or entitlement. Placing the emphasis on this person is a necessary step in determining what the source of funds is.'

Further explanation is provided on beneficial owners in the context of trusts:

> 'In the typical case, it would be clear which person has "beneficial ownership" for purposes of the Guidelines. For instance, in the case of an industrialist who establishes a trust for the benefit of his wife or minor children, the beneficial owner would be the industrialist settlor, namely, the "provider of funds" [. . .]. The appropriate due diligence should be conducted with regard to the industrialist, including background checks and the requisite inquiry as to source of funds. If appropriate, the banker should consider identifying the beneficial owner by reference to official identity papers. Even though the wife or children have a beneficial interest in the trust, they should not be treated as "beneficial owners" for anti-money laundering purposes. That is, it would not make sense to do due diligence with respect to the wife's or children's source of funds, although it may be appropriate to do some due diligence with respect to their background and reputation.'

The definition of beneficial owner according to the Wolfsberg Group's Principles also shows that between power of disposition and beneficiary neither identity prevails. Rather, both elements have their own separate relevance but both fall under the definition of beneficial owner. By way of clarification, it should be added that in terms of the beneficial owner the Wolfsberg Principles focus on who controls the assets and not on the person who is beneficiary of these assets in terms of the obligations concerning the fight against money laundering and terrorism. It should also be noted that the Wolfsberg Principles state that it must not only be established who the beneficial owner is but also require an in-depth examination of the background and origins of the beneficial owner's funds. It is therefore easy to understand why the obligations concerning the beneficial owner vary according to the persons, their respective power of disposition over assets and persons who should be beneficiaries of assets.

Message on the law against money laundering

The following message on the law against money laundering can be gathered with regards to the duties to determine who the person acting as beneficial owner is in the context of trusts:

> 'When the person acting as beneficial owner has yet to be determined, and this is occasionally the case with trusts, all relevant information must be collected, for example, the names of the persons authorised to give instructions to the contracting party or the persons considered to be potential beneficiaries of the trust.'

Even though little can be gathered from the message on the law against money laundering, it does determine that both those who are actually able to make decisions about assets as well as those, who should be beneficiaries of the assets, to the degree that this can be ascertained, should be considered beneficial owners.

Own definition of beneficial owner

One definition of beneficial owner in the context of the fight against money laundering and terrorism for interpretation under Swiss law based on the view put forward here encompasses two parts, namely (I) power of disposition and (II) beneficiary, and can be expressed in the following manner: a beneficial owner is someone who either (I) (1) is the owner of the contracting party; (2) controls the contracting party legally or operationally; (3) carries out

transactions on the instruction and on the account of the contracting party; or (II) is the beneficiary and thus the person to whom the enjoyment of the assets held through the contracting party (1) belongs or (2) should belong. A person to whom assets at best only supposedly or could belong to is not a beneficial owner.

General information on establishing the beneficial owner

Principle: Assumption that the contractual partner and the beneficial owner are the same

As a matter of principle, banks may assume that the contractual partner is the same as the beneficial owner. There are, however, a number of exceptions.

Exception 1: the contractual partner is identifiably not the same as the beneficial owner or there are doubts about this

Should the contractual partner be identifiably not the same as the beneficial owner or there are any doubts as to this, a written declaration specifying the beneficial owner is required from the contractual partner. In a trust, the trustee is routinely not the same as the beneficial owner.

Exception 2: the contracting party is a domiciliary company

Banks must obtain another written declaration from the contracting party indicating who the beneficial owner party is when the contracting party is a domiciliary company. The definition of a domiciliary company is outlined below.

Exception in the identification of the beneficial owner: Assets without beneficial ownership

For assets without any beneficial ownership by designated persons, for example as is the case with discretionary trusts or foundations, instead of identifying the beneficial owner a written declaration must be obtained from the contractual partner which confirms these facts. The contracting party's explanation contains information on the actual (ie not the trust) founders or settlors and, where it can be ascertained, those persons that are entitled to issue instructions to the contracting party or their organs as well as those persons to be included as beneficiaries according to the category, such as, for example, dependents of the founders or settlors. If curators or protectors exist, they shall also be included in the contracting parties' declaration. Form T must be used for completing this declaration. The form may be amended but the contents such stay the same . . .

Case law of the Federal Administrative Court

Concept of beneficial owner

There is no specific definition of the concept of a beneficial owner in State Treaty 10.165 The identification criterion for a beneficial owner in State Treaty 10 should ensure that account information from a US person will be forwarded to American tax authorities where they have an advanced corporate structure from a fiscal point of view in order to circumvent the obligation to submit a declaration for the assets on the company account and the income deriving therefrom. Correspondingly, the concept of beneficial owner should serve to create constellations 'through which, from an economic perspective (substance over form) the offshore company exists simply to evade the compulsory tax reporting requirements or for the purpose of tax evasion with respect to the USA'.

It is thus key for beneficial ownership to what extent the beneficial owners were able to continue controlling economically and dispose of the assets on a bank account and the income derived therefrom through the formal framework of an offshore company.

Transfer of the trust property

An adult beneficiary with the requisite capacity is entitled to call for the transfer of the trust property to him or her under what is termed the rule in *Saunders v Vautier* (1841) Cr& Ph 240. This will be discussed further in Chapter 24. In the case of a discretionary trust, the case of *Re Smith, Public Trustee v Aspinall* [1928] Ch 915 confirms that the objects of a discretionary trust may agree to the even distribution of the trust fund between them. However, this depends upon the class of potential beneficiaries to be sufficiently small that an unanimous agreement may be reached. Therefore, for example, a discretionary trust for the benefit of the settlor's children could operate in this way. However, under a *McPhail v Doulton* [1971] AC 424 type trust for the benefit of relatives, where it is impossible (and unnecessary) to list all the potential beneficiaries, the postulants would not be able to call for the distribution of the trust fund because it would be impossible to determine whether unanimous acquiescence had been given to the proposal.

An extension of this principle means that adult beneficiaries are able to call for, or alternatively, to approve a variation of the trust. This means that in many respects they are the most powerful party to the trust, in that they are able to require the trust to be administered in a manner that is different from that which the settlor intended.

Right to receive accounts and information

The beneficiary is entitled to receive accounts from the trustees. However, some uncertainty prevails regarding what other information the trustees are obliged to provide. In *Re Londonderry's Settlement* [1964] 3 All ER 855, the court concluded that there was no obligation to disclose information concerning the reasons behind the trustees' decisions, as these were confidential. The rationale behind this was that there was felt to be a need to protect the trustee from having his or her judgement called into question unless there was evidence of the trustee having acted in bad faith. Of course, without knowing the basis upon which decisions were made it is difficult to know whether the trustee has acted in bad faith.

Nevertheless, attitudes towards disclosure have changed, and accountability has become an important concept. Accordingly, a duty to disclose information about the trust may arise under the Data Protection Act 1998.[10] Furthermore, the threat of litigation by the beneficiary may mean that the trustee must disclose information pertaining to the trust.

Accordingly, the beneficiary is simultaneously the most powerful party in the trust relationship, because he or she is able to litigate in relation to a breach of the trust, and yet has the fewest obligations under the trust. Nevertheless, despite the power wielded by the beneficiaries, there are a number of limitations on the beneficiaries' powers in terms of their entitlement to the trust fund, and the obligations they may impose on the trustee.

[10] (1998 c.29).

Chapter summary

This chapter may be useful for assessments and assignments on:

- The rights of the beneficiary
- Litigation for breach of trust.

Further reading

Ambrose, M. (2006) 'Disclosure to beneficiaries – whither confidentiality?' *Private Client Business* 236.

Lightman, G. (2004) 'The trustees' duty to provide information to beneficiaries' *Private Client Business* 236.

Panico, P. (2013) 'Private purpose foundations: from a classic "beneficiary principle" to modern legislative creativity' 19(6) *Trusts and Trustees* 542.

Taube, S. (2005) 'Discovering the reasons for trustees' decisions' *Private Client Business* 280.

Part 3

Types of trusts

Part 3 is sub-divided as follows:

Family trusts – covered in Chapters 13, 14 and 15
Commercial trusts – covered in Chapters 16 and 17
Purpose trusts – covered in Chapters 18, 19, 20 and 21
Implied trusts – covered in Chapter 22

13

Family trusts

Chapter outline

This chapter will cover:

- Trusts for the preservation of family wealth
- Family commercial trusts.

Introduction

The mechanics of how a trust works, and the interaction of the parties and the trust property, have been considered in Part 2. Part 3 of this book seeks to develop that discussion and explain how trusts work in different contexts. In essence, the relationship does not change – the trust continues to operate on the basis of there being a settlor who creates a trust, and a trustee who administers it for the benefit of a beneficiary. However, as shall be shown, the constitution of the trust and the obligations it imposes may vary slightly according to context. This and the following two chapters are concerned with what may be broadly termed family trusts, as the objective is to confer a benefit on members of one's family – most commonly one's immediate family in the form of one's spouse or cohabitant, and perhaps more commonly one's children, although of course, it is perfectly acceptable to confer a benefit on more distant relatives if desired.

The family trust

One of the reasons for creating a trust is as a mechanism for preserving family wealth. A trust may be created either on an *inter vivos* basis (meaning 'during one's lifetime'), or under the terms of a will in order to provide property for the benefit of family members after one's death. On a simple level, this may be undertaken in order to provide a capital sum, or a specific asset for one's spouse and children in the event of one's death or, for when the children reach adulthood. In *Lilleyman v Lilleyman* [2013] 1 All ER 302 for example, the testator left his watch, his china collection and his car to his sons, while jewellery belonging to his first wife was left to his granddaughters. All his other personal chattels were left to his wife. As for his money, his grandchildren received £25,000 each, and his house and other land that he owned was given to his wife, subject to certain conditions for her lifetime, and then to his sons after his wife's death, or if she failed to fulfil some of the conditions.

An *inter vivos* trust or a will trust may therefore provide a life interest for a spouse, with the remainder going, on the spouse's death to the settlor's children.[1] Alternatively, a settlor may create a trust for his or her children whereby each child becomes entitled to the fund when they reach adulthood[2] – or, if the settlor wishes, even later.[3] A trust is particularly useful where the settlor's child would be especially vulnerable in the event of a parent's death.[4] Clearly this would be an issue where a parent dies during a child's minority, but also if a child has a severe disability that would impair their ability to work or that could cause them to require constant care. A trust may therefore be particularly beneficial in order to ensure that after their parent's death, the child is adequately provided for, even in adulthood.

However, the family trust may also be used in more sophisticated ways. For example, a discretionary trust may be used in order to take account of circumstances that are as yet unknown. For example, the settlor may wish to create a trust that will ensure that a larger proportion of the trust fund will be given to the family member who has the greatest need of support.

The discretionary trust may also be used in order to protect family wealth from the excesses of potential beneficiaries. One of the advantages of the discretionary trust is that

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[1] *Re Goodchild* [1996] 1 All ER 670.
[2] *Re T's Settlement Trusts* [1964] Ch 158.
[3] *Re Holt* [1969] 1 Ch 100.
[4] *J v J (C Intervening) (Minors: Financial Provision)* [1989] Fam 29.

the objects of the trust acquire no interest in the trust property until the trustees have exercised their discretion in a specific postulant's favour.[5] Therefore, the discretionary trust may be used to keep trust property out of the hands of a particularly irresponsible beneficiary.

The following is an example of how this might work. Alf has three adult children – Ben, Claire and David. David has a poor record with money and, as soon as he has any money, he takes to gambling, and loses most of his money on horses and roulette tables. Alf is concerned that if he gives a third of his estate to David, David will lose it and then try to borrow money off Ben and Claire. Therefore, Alf decides to create a trust. The trust fund is a discretionary trust for the benefit of Ben, Claire and David. Accordingly, none of them acquires an equitable interest in the trust fund. The trustees are given a discretion regarding how to distribute the trust fund between the three children. They decide to give Ben and Claire a capital sum each. They decide to give David a smaller sum, but agree to review the decision annually. David cannot argue that the trustees are in breach of their obligation – they are acting in accordance with the discretion bestowed upon them by Alf. However, David is unable to require that the trust fund is transferred to him, as the distribution of the fund and the termination of the trust would require the consent of Ben and Claire – whose interests would not be served by such an arrangement. Furthermore, because he has no entitlement to the money remaining in the fund until the trustees have decided to exercise their discretion in his favour, David is unable to mortgage his equitable interest in order to obtain money by borrowing. Neither can he sell his entitlement as a way of obtaining money. In this way, Alf is able to ensure that David does not squander the money he wishes to give him, but at the same time, he is able to ensure that David is provided for.

The trust is a particularly useful mechanism for ensuring that a family business remains in family control. The settlor creates a trust of the shares in a company. Because the shares are held on a trust, the beneficiaries (who are family members) cannot sell them without the consent of all the other beneficiaries. Accordingly, because selling the shares is rendered more difficult, the trustees are able to ensure that the business remains in family ownership. This is particularly useful in the context of agricultural land. If a farm were to be divided between, for example, three children, then the three small farms would be worth less than one large farm. Accordingly, a trust may be used to ensure that the land remains in the ownership of the trustees, but that the beneficiaries are entitled to derive the benefit of the undivided land.

Another advantage of the family trust is that it enables a settlor to provide for his or her children in the event of the settlor's death and their spouse's remarriage. Unfortunately, the wicked step-parent from children's fairy tales is a common (although hopefully unrealised) fear for many parents. However, the law of trusts enables the settlor to put a fund in the hands of trustees that will protect it from being inherited by the settlor's spouse in the event of the settlor's death, and then by the spouse's second spouse in the event of the spouse dying. The settlor is able to ensure that a proportion of his or her estate is kept away from the spouse, and that it is kept for the benefit of the settlor's children in the event of the settlor's death.

Grandparents may also wish to use a trust in order to provide for their grandchildren – perhaps in ways that their children may not approve of. For example, grandparents who wish to ensure that their grandchildren are privately educated may create a trust for this purpose so as to ensure that adequate sums of money are available to pay the school fees.

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[5] *Murphy v Murphy* [1999] 1 WLR 282.

A family trust may also have advantages from the viewpoint of tax savings. For example, the trust mechanism may be used to transfer smaller sums of money to the beneficiary over a period of time in order to take advantage of inheritance tax nil-rate thresholds in situations where a large amount of inheritance tax would become payable on the settlor's death. It may also be advantageous for the settlor to pay regular sums into the trust fund in order to fund a life policy that is held under a trust.

A trust may also enable individuals to obtain particular benefits that outright ownership of an asset would prevent. For example, a trust for the benefit of a minor will ensure that the fund is not taxed as though it were owned by the settlor – something that may be particularly advantageous if the settlor is a higher rate taxpayer. Furthermore, if certain state benefits are means tested, then it may be advantageous to put any compensation awarded into a trust in order to ensure that the beneficiary is still eligible for means tested benefits.

ACTIVITY

Choose a famous/fictitious person. If you wish, you could imagine your own situation, or that of a family member. Consider what type of trust you might employ in order to ensure that the assets they do (or you imagine they might) own remains within their family. You may wish to consider:

- whether they have any minor children or children with disabilities;
- whether they have a spouse;
- whether they have grandchildren;
- whether they own land that would be devalued if divided;
- whether they own a family business;
- whether they are a higher-rate tax payer and who from their known family may be lower-rate tax payers.

What sort of trust would you create for them?

The family commercial trust

Although specifically commercial trusts will be considered later (in Chapter 16), the commercial and the familial do nevertheless intersect. A trust may be a useful device for ensuring that the assets of a family business are not divided on the parent's death. By making the (adult) children trustees of the trust for the benefit of themselves and their siblings, an individual is effectively precluded from introducing new owners to the business, and is also restricted in his or her ability to sell their share in the business. Furthermore, the trust instrument may specify that only, for example, children of the original owner may be the beneficiaries of the trust, and excluding the trustees from conferring the benefit of the trust on spouses (who may otherwise acquire a share in the business as part of a divorce settlement). Accordingly, Baghurst and Laing[6] argue that a

[6] Baghurst, E. and Laing, S. (2005) 'Protecting the family business' 155(7193) *New Law Journal* 1382.

trust may be a more effective mechanism than a pre-nuptial agreement for protecting the family business in the event of a marriage breakdown. It also means that the parent who has built the business up is able to safeguard what he or she considers to be the family's interests, whereas the parties to a pre-nuptial agreement are merely the husband and wife themselves, neither of whom may regard the preservation of the family business as being as significant a concern. A trust may also be useful in relation to agricultural land. For example, if a large farm were to be passed by will to one child, then that child may sell the farm in its entirety. On the other hand, dividing the farm between the testator's children may devalue it. Accordingly by creating a trust, the settlor is able to ensure that all his or her children are able to benefit from the farm, and the self-interest of one does not cause detriment to the others.

The trust is therefore extremely useful in the family context, and is frequently used in such a way as to minimise the tax payable by an individual, to preserve wealth, and to confer a benefit on successive generations. Two specific types of family trusts will be considered later (in the following two chapters). One of these is the trust of the family home, while the other relates to the law of succession. It must be borne in mind however, that these are not solely family trusts, in that friends or commercial partners may co-own property, and one's family is not necessarily the sole focus of the law of succession. However, because these situations most commonly arise in family relationships, it is logical to view them, for the purposes of this book at least, as types of family trusts.

Chapter summary

This chapter may be useful for assessments and assignments on:

- The modern role of trusts
- Family trusts
- Trusts and taxation
- The advantages of creating a trust.

Further reading

Baghurst, E. and Laing, S. (2005) 'Protecting the family business' 155(7193) *New Law Journal* 1382.

Coldrick, D. (2009) 'Whatever happened to family trusts?' *Elderly Client Adviser* 5.

Directgov (2012) Types of trusts and tax implications. http://www.direct.gov.uk/en/MoneyTaxAndBenefits/Taxes/Trusts/Typesoftrustandtaximplications/index.htm. (Site accessed 29 August 2012.)

14

Trusts relating to land

Chapter outline

This chapter will cover:

- Trusts affecting land
- The different types of implied trust
- Establishing an interest in the family home via a resulting trust
- Establishing an interest in the family home via a constructive trust.

Introduction

This chapter is concerned with two distinct, but overlapping areas of trusts law, namely the different instances where trusts relating to land arise. On the one hand any type of trust – commercial or domestic, private or charitable – could include land, and therefore, the first part of this chapter will address the operation of trusts of land. The second area where the trust is used specifically in relation to land is in the context of trusts of the family home, where it sometimes becomes necessary for the courts to imply that a trust has been created.

Trusts of land

Land is commonly the subject of a trust. Firstly, it is a valuable commodity and the wealth preservation objective means that the use of trusts is commonplace. Secondly, because its value makes land an expensive asset to purchase, land is often co-owned.

As has been discussed elsewhere in this book, co-ownership of land necessitates a trust, and plural co-owners will own the land on trust for themselves and the other co-owner(s). The only type of co-ownership permitted at law is the joint tenancy (Law of Property Act 1925, s.26), whereby the co-owners are trustees of the entirety of the land for the benefit of themselves and the other co-owners. In other words, all the beneficiaries are beneficiaries of the whole of the land, with the result that after all the other beneficiaries have died, the sole survivor becomes the sole legal owner of the land. The advantage of joint ownership at law is that the trustees have undivided ownership of the land, which means that the buyer does not need to ascertain each separate person's entitlement to sell. The co-owners are treated as a single entity, so all the buyer must establish is that the sellers as an entity are entitled to sell.

In equity, there are two types of co-ownership – joint tenancy and tenancy in common. A joint tenancy is as described above. However, under a tenancy in common, the joint legal owners hold the land on trust on what is termed undivided shares (Law of Property Act 1925, s.34). Accordingly, the trustees are able to specify how much of a share of the proceeds of sale each beneficiary will be entitled to receive, thus allowing for the possibility that co-owners may own land in shares that are unequal.

This is how the trust of land operates under the Law of Property Act 1925. A further requirement under that Act is that where land is subject to a trust, there must be two trustees or a trust corporation to give a valid receipt to a buyer of the land. If the land is sold by a single trustee, then the beneficiary is able to enforce the trust against the buyer. This is known as overreaching, and is explained in s.2 Law of Property Act 1925.

EXTRACT

Law of Property Act 1925, s.2

2 Conveyances overreaching certain equitable interests and powers

(1) A conveyance to a purchaser of a legal estate in land shall overreach any equitable interest or power affecting that estate, whether or not he has notice thereof, if-

(i) the conveyance is made under the powers conferred by the Settled Land Act 1925 or any additional powers conferred by a settlement, and the equitable interest or power is

capable of being overreached thereby, and the statutory requirements respecting the payment of capital money arising under the settlement are complied with;

(ii) the conveyance is made by [trustees of land] and the equitable interest or power is at the date of the conveyance capable of being overreached by such trustees under the provisions of sub-section (2) of this section or independently of that sub-section, and [the requirements of section 27 of this Act respecting the payment of capital money arising on such a conveyance] are complied with;

(iii) the conveyance is made by a mortgagee or personal representative in the exercise of his paramount powers, and the equitable interest or power is capable of being overreached by such conveyance, and any capital money arising from the transaction is paid to the mortgagee or personal representative;

(iv) the conveyance is made under an order of the court and the equitable interest or power is bound by such order, and any capital money arising from the transaction is paid into, or in accordance with the order of, the court.

[(1A) An equitable interest in land subject to a trust of land which remains in, or is to revert to, the settler shall (subject to any contrary intention) be overreached by the conveyance if it would be so overreached were it an interest under the trust.]

(2) [Where the legal estate affected is subject to [a trust of land], then if at the date of a conveyance made after the commencement of this Act [by the trustees], the trustees (whether original or substituted) are either-]

(a) two or more individuals approved or appointed by the court or the successors in office of the individuals so approved or appointed; or

(b) a trust corporation,

[any equitable interest or power having priority [to the trust]] shall, notwithstanding any stipulation to the contrary, be overreached by the conveyance, and shall, according to its priority, take effect as if created or arising by means of a primary trust affecting the proceeds of sale and the income of the land until sale.

(3) The following equitable interests and powers are excepted from the operation of subsection (2) of this section, namely-

(i) Any equitable interest protected by a deposit of documents relating to the legal estate affected;

(ii) The benefit of any covenant or agreement restrictive of the user of land;

(iii) Any easement, liberty, or privilege over or affecting land and being merely an equitable interest (in this Act referred to as an "equitable easement");

(iv) The benefit of any contract (in this Act referred to as an "estate contract") to convey or create a legal estate, including a contract conferring either expressly or by statutory implication a valid option to purchase, a right of pre-emption, or any other like right;

(v) Any equitable interest protected by registration under the Land Charges Act 1925 other than-

(a) an annuity within the meaning of Part II of that Act;

(b) a limited owner's charge or a general equitable charge within the meaning of that Act.

(4) Subject to the protection afforded by this section to the purchaser of a legal estate, nothing contained in this section shall deprive a person entitled to an equitable charge of any of his rights or remedies for enforcing the same.

(5) So far as regards the following interests, created before the commencement of this Act (which accordingly are not within the provisions of the Land Charges Act 1925), namely-

(a) the benefit of any covenant or agreement restrictive of the user of the land;

(b) any equitable easement;

(c) the interest under a puisne mortgage within the meaning of the Land Charges Act 1925 unless and until acquired under a transfer made after the commencement of this Act;

(d) the benefit of an estate contract, unless and until the same is acquired under a conveyance made after the commencement of this Act;

a purchaser of a legal estate shall only take subject thereto if he has notice thereof, and the same are not overreached under the provisions contained or in the manner referred to in this section.

The Law of Property Act 1925 provides the framework under which the trust operates. Overlaid on this is the Trusts of Land and Appointment of Trustees Act 1996[1] which governs how trusts of land are administered, and also the rights of the beneficiary under the trust. Much of what is contained in the Act as regards the administration of the trust is later replicated on a more general basis in the Trustee Act 2000,[2] such as for example allowing the trustees to deal with the land as though they were the owner[3] and the ability to delegate responsibilities to an agent.[4]

However, one important aspect of the Trusts of Land and Appointment of Trustees Act 1996 is that unlike its predecessors (in the form of the Trustee Act,[5] the Settled Land Act[6] and Law of Property Act, all of which date from 1925), the Trusts of Land and Appointment of Trustees Act 1996 provides the beneficiaries with a limited entitlement to occupy the land. The earlier legislation operated on the basis that the beneficiaries' only entitlement to the land was an entitlement to the proceeds of sale once the land had been sold by the trustees, and therefore assumed that the trustees' role was primarily to sell the land in order to realise its capital value. Section 4 provides that even where the trust document requires that the land be sold, the trustees are permitted to postpone the sale indefinitely if they wish (and of course, if this benefits the trust!).

Section 12 of the Trusts of Land and Appointment of Trustees Act 1996 however allows the beneficiaries to occupy the land where their interest is an interest in possession (as opposed to a future interest) provided that the trust instrument allows the beneficiary to be in occupation of the land.

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[1] (1996 c.47).
[2] (2000 c.29).
[3] Trusts of Land and Appointment of Trustees Act 1996, s.6.
[4] Trusts of Land and Appointment of Trustees Act 1996, s.9.
[5] (1925 c.19).
[6] (1925 c.18).

EXTRACT

Trusts of Land and Appointment of Trustees Act 1996, ss.12 and 13

12 The right to occupy

(1) A beneficiary who is beneficially entitled to an interest in possession in land subject to a trust of land is entitled by reason of his interest to occupy the land at any time if at that time-

(a) the purposes of the trust include making the land available for his occupation (or for the occupation of beneficiaries of a class of which he is a member or of beneficiaries in general), or

(b) the land is held by the trustees so as to be so available.

(2) Subsection (1) does not confer on a beneficiary a right to occupy land if it is either unavailable or unsuitable for occupation by him.

(3) This section is subject to section 13.

13 Exclusion and restriction of right to occupy

(1) Where two or more beneficiaries are (or apart from this subsection would be) entitled under section 12 to occupy land, the trustees of land may exclude or restrict the entitlement of any one or more (but not all) of them.

(2) Trustees may not under subsection (1)-

(a) unreasonably exclude any beneficiary's entitlement to occupy land, or

(b) restrict any such entitlement to an unreasonable extent.

(3) The trustees of land may from time to time impose reasonable conditions on any beneficiary in relation to his occupation of land by reason of his entitlement under section 12.

(4) The matters to which trustees are to have regard in exercising the powers conferred by this section include-

(a) the intentions of the person or persons (if any) who created the trust,

(b) the purposes for which the land is held, and

(c) the circumstances and wishes of each of the beneficiaries who is (or apart from any previous exercise by the trustees of those powers would be) entitled to occupy the land under section 12.

(5) The conditions which may be imposed on a beneficiary under subsection (3) include, in particular, conditions requiring him-

(a) to pay any outgoings or expenses in respect of the land, or

(b) to assume any other obligation in relation to the land or to any activity which is or is proposed to be conducted there.

(6) Where the entitlement of any beneficiary to occupy land under section 12 has been excluded or restricted, the conditions which may be imposed on any other beneficiary under subsection (3) include, in particular, conditions requiring him to-

(a) make payments by way of compensation to the beneficiary whose entitlement has been excluded or restricted, or

(b) forgo any payment or other benefit to which he would otherwise be entitled under the trust so as to benefit that beneficiary.

(7) The powers conferred on trustees by this section may not be exercised-

(a) so as prevent any person who is in occupation of land (whether or not by reason of an entitlement under section 12) from continuing to occupy the land, or

(b) in a manner likely to result in any such person ceasing to occupy the land,

unless he consents or the court has given approval.

(8) The matters to which the court is to have regard in determining whether to give approval under subsection (7) include the matters mentioned in subsection (4)(a) to (c).

Nevertheless, the trust of land confers certain other rights on the trustees. For example, where consent is required before the trustees are able to sell or mortgage the trust property, s.10 permits the trustees to proceed after obtaining consent from two of the people whose consent is required. However, the trustees may apply for a court order in order to enable them to undertake a transaction without the consent of the beneficiaries and any other person or person who is required by the trust instrument to give consent.

The beneficiaries are also entitled under the Act to nominate new trustees. This is contained in s.19 of the Act. This right is only conferred where all the beneficiaries under the trust are of full age and their entitlement to the trust property is a current entitlement rather than a future entitlement.

The Trusts of Land and Appointment of Trustees Act 1996 therefore confers greater freedoms on the trustees to act, and confers some new rights on the beneficiaries. However, it also gives more specific and direct scope for the trustees to sideline the beneficiaries by seeking the necessary consents from the court rather than from the beneficiaries.

Implied trusts

Most of Part 2 of this book focused primarily on express trusts. However, trusts may also arise as a result of the parties' conduct. These are known as implied trusts, and are construed in situations where it is considered improbable that the settlor transferred the property with any other intention than the creation of a trust, usually where the settlor is also the sole beneficiary or one of the beneficiaries.

The implied trust takes three key forms. Firstly, there is the resulting trust. A resulting trust will occur where the settlor contributes to the acquisition of an asset, without intending for his or her contribution to be by way of a gift. A resulting trust may also occur where a trust fails, for example where its objects have not been adequately defined (discussed further in Chapter 22). It is clear in this situation that a trust was intended and not a gift to the purported trustee. Therefore, the trust property returns ('results') back to the settlor, or if the trust is created under a will, to the deceased settlor's estate.

The second type of implied trust is the constructive trust. A constructive trust will be recognised wherever it would be unjust to deny that the trustee has put him- or herself in the position of a trustee *vis-a-vis* the beneficiary.

The third type of situation where a trust is imposed is where proprietary estoppel exists. Proprietary estoppel is the law's mechanism for recognising and remedying unconscionable conduct where the defendant has, through his or her words or conduct, induced the claimant to act in a particular way to the claimant's detriment. The courts then consider what would be an appropriate mechanism for remedying the wrong that has occurred – one method being to prevent ('to estop') the defendant from denying that there is a trust in existence. Proprietary estoppel will be discussed further in Chapter 22.

Although these three forms of implied trust may arise in a number of different contexts (see Chapter 22 for a more detailed discussion of their more general application) one way in which they have been commonly used in recent years is in the context of co-ownership of the family home. Although the courts are able to divide the property of married couples who are divorcing and civil partners who are separating, under their powers under the Matrimonial Causes Act 1973,[7] they have no such powers in relation to cohabitants who are separating. Accordingly, cohabitants must rely on the law of trusts in order to establish their interest in the family home. The law of trusts may also be relevant to married couples who are separating, but who have no intention of divorcing. The application of the law of trusts also cannot be entirely ignored in the matrimonial or civil partnership context, in that when the parties' legal representatives are negotiating a financial settlement on divorce or dissolution of a civil partnership, it may be useful for them to know what they have contributed in order to negotiate the settlement in the way that is most appropriate to them. For example if there is an intention that Donna will have an equal share of the home in which she has been living, but which is in Ricky's sole name, then Donna may wish to negotiate that Ricky compensates her for this contribution when the couple divorces. However, if Donna does not know that she is entitled to a share of the sale proceeds of the matrimonial home, she may not recognise that the offer of a share as part of a divorce settlement does not represent an advantageous offer – Ricky is merely offering her that to which she is already entitled.

The situation that arises is this. Donna and Ricky are a cohabiting couple, who split up. They must decide how to divide the proceeds of sale of the house. The law's response is to look at the Land Register, and to determine ownership on that basis. If Ricky is the sole owner, then the proceeds of sale belong to him alone. If Donna and Ricky are joint owners, then the proceeds of sale must be divided equally between them. The difficulty arises when Donna and Ricky argue that what is recorded on the Land Register does not reflect the true picture – either because Donna argues that she is entitled to a share of Ricky's house, or because Donna and Ricky argue that an equal division of the proceeds of sale fails to reflect their respective entitlements.

Sometimes this will be governed by an express trust – in other words one partner makes an express declaration of trust in favour of the other. This must be made in writing and comply with the formalities of s.53 Law of Property Act 1925. This is fairly easily achieved at the time of acquisition, in that the form that the seller must complete in order to effect the transfer to the buyer will give the buyer the opportunity to indicate the percentage share of each party's entitlement (known as a tenancy in common). The difficulty is that parties' intentions may change over time, especially if one person contributes to any improvements made to the home (e.g. an extension) or if one person moves in to a house owned by their partner. Declaring an express trust in these situations is unlikely in the reality of most people's lives. It is something to which most people give little or no thought.

Accordingly separating couples must rely on implied trusts in the form of resulting trusts and constructive trusts in order to establish their entitlement. Implied trusts consider the conduct of the parties, and the court identifies a trust as having come into existence when the parties have acted as though they are trustees and beneficiaries. Accordingly, where a person has put themselves in the position where it would be inequitable to deny that there is a trust in existence, then a trust will be identified.

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[7] (1973 c.18).

Resulting trusts of the family home presumed from the conduct of the settlor/beneficiary

The most straightforward type of implied trust is a resulting trust. A presumed resulting trust occurs where the settlor/beneficiary has contributed to the cost of buying some asset but vested in the name of another. Under a resulting trust, the non-owning contributor will be entitled to a share in the property that is proportionate to the extent of his or her contribution to the purchase price.[8] There is a presumption here that the person in whose name the property is vested will hold it on trust for the benefit of the settlor/beneficiary.

Therefore if Alice and Bob contribute equally to the purchase price of a house which is registered in Alice's name, Alice is presumed to own the house on trust for herself and Bob. The trust arises because it is presumed that Bob would not have contributed in this way if Bob was not intending to obtain a share of the proceeds of sale when it is sold. Such a trust may be useful if Bob either does not wish to be registered as the proprietor of the land (for example where Bob wishes to cohabit with Alice after having separated from, but not being divorced from, his spouse) or cannot be registered as a proprietor (by virtue of being below the age of 18 for example). Nevertheless, the resulting trust is only a presumption, and can therefore be rebutted where there is evidence to the contrary, such as for example, where Bob's contribution was by way of either a gift or a loan to Alice. The relevance of the resulting trust in the context of the family home is explained by Lord Walker and Lady Hale SCJJ in *Kernott v Jones* [2011] 3 FCR 495.

EXTRACT

Kernott v Jones [2011] 3 FCR 495

Lord Walker and Lady Hale SCJJ

The competing presumption: a resulting trust?

In an illuminating article, 'Explaining Resulting Trusts' (2008) 124 LQR 72 at p 73, footnote (6) William Swadling has commented:

> 'A resulting trust also traditionally arose where A and B contributed unequally to the purchase price and the title was conveyed to A and B as joint tenants, whereby A and B held as equitable tenants in common in proportion to their contributions (*Lake v Gibson* (1729) 1 Eq Cas Abr 290). In *Stack v Dowden* [2007] UKHL 17, a majority of the House of Lords held that this rule no longer applied in the case of 'matrimonial or quasi-matrimonial homes.'

That is probably a reference to para [31] of Lord Walker's opinion. Lady Hale's opinion does not in terms reach that conclusion. But the extended discussion from para [56] to [70] (and in particular, the express disapproval of *Walker v Hall* [1984] FLR 126, *Springette v Defoe* [1992] 2 FCR 561, [1992] 2 FLR 388 and *Huntingford v Hobbs* [1993] 1 FCR 45, [1993] 1 FLR 736) is inconsistent with a resulting trust analysis in this context. It is not possible at one and the same time to have a presumption or starting point of joint beneficial interests and a presumption (let alone a rule) that the parties' beneficial interests are in proportion to their respective financial contributions.

[8] *Springette v Defoe* [1982] 2 FCR 561.

In the context of the acquisition of a family home, the presumption of a resulting trust made a great deal more sense when social and economic conditions were different and when it was tempered by the presumption of advancement. The breadwinner husband who provided the money to buy a house in his wife's name, or in their joint names, was presumed to be making her a gift of it, or of a joint interest in it. That simple assumption-which was itself an exercise in imputing an intention which the parties may never have had-was thought unrealistic in the modern world by three of their Lordships in *Pettitt v Pettitt* [1969] 2 All ER 385, [1970] AC 777. It was also discriminatory as between men and women and married and unmarried couples. That problem might have been solved had equity been able to extend the presumption of advancement to unmarried couples and remove the sex discrimination. Instead, the tool which equity has chosen to develop law is the 'common intention' constructive trust. Abandoning the presumption of advancement while retaining the presumption of resulting trust would place an even greater emphasis upon who paid for what, an emphasis which most commentators now agree to have been too narrow: hence the general welcome given to the 'more promising vehicle' of the constructive trust: see Gardner and Davidson (2011) 127 LQR 13 at p 16. The presumption of advancement is to receive its quietus when s 199 of the Equality Act 2010 is brought into force.

The time has come to make it clear, in line with *Stack v Dowden* (see also *Abbott v Abbott* [2007] UKPC 53, [2008] 2 LRC 511, [2008] 1 FLR 1451), that in the case of the purchase of a house or flat in joint names for joint occupation by a married or unmarried couple, where both are responsible for any mortgage, there is no presumption of a resulting trust arising from their having contributed to the deposit (or indeed the rest of the purchase) in unequal shares. The presumption is that the parties intended a joint tenancy both in law and in equity. But that presumption can of course be rebutted by evidence of a contrary intention, which may more readily be shown where the parties did not share their financial resources . . . This sort of constructive intention (or any other constructive state of mind), and the difficulties that they raise, are familiar in many branches of the law. Whenever a judge concludes that an individual 'intended, or must be taken to have intended', or 'knew, or must be taken to have known', there is an elision between what the judge can find as a fact (usually by inference) on consideration of the admissible evidence, and what the law may supply (to fill the evidential gap) by way of a presumption. The presumption of a resulting trust is a clear example of a rule by which the law does impute an intention, the rule being based on a very broad generalisation about human motivation, as Lord Diplock noted in *Pettitt v Pettitt* [1969] 2 All ER 385 at 414, [1970] AC 777 at 824:

> 'It would, in my view, be an abuse of the legal technique for ascertaining or imputing intention to apply to transactions between the post-war generation of married couples "presumptions" which are based upon inferences of fact which an earlier generation of judges drew as to the most likely intentions of earlier generations of spouses belonging to the propertied classes of a different social era.'

That was 40 years ago and we are now another generation on.

The decision in *Stack v Dowden* produced a division of the net proceeds of sale of the house in shares roughly corresponding to the parties' financial contributions over the years. The majority reached that conclusion by inferring a common intention (see Lady Hale's opinion at [92], following her detailed analysis of the facts starting at [86]). Only Lord Neuberger reached the same result by applying the classic resulting trust doctrine (which involved, it is to be noted, imputing an intention to the parties).

In deference to the comments of Lord Neuberger and Rimer LJ, we accept that the search is primarily to ascertain the parties' actual shared intentions, whether expressed or to be inferred from their conduct. However, there are at least two exceptions. The first, which is not this case,

is where the classic resulting trust presumption applies. Indeed, this would be rare in a domestic context, but might perhaps arise where domestic partners were also business partners: see *Stack v Dowden* at [32]. The second, which for reasons which will appear later is in our view also not this case but will arise much more frequently, is where it is clear that the beneficial interests are to be shared, but it is impossible to divine a common intention as to the proportions in which they are to be shared. In those two situations, the court is driven to impute an intention to the parties which they may never have had.

Nevertheless, it is generally considered that the resulting trust has become less relevant in matrimonial home cases. In the case of *Curley v Parkes* [2004] EWCA Civ 1515 for example, it was concluded that the resulting trust only applies to the parties intentions' before or at the time of purchase. Accordingly, the fact that the non-owning spouse contributes to the mortgage instalments would not be relevant to the resulting trust. However, it is rare that a home will be acquired without a mortgage loan, and therefore it is unlikely that the resulting trust principles will reflect the full nature of the parties' contributions. Accordingly, it has become more common for non-owning cohabitants to rely on the concept of the constructive trust when arguing that they should acquire a share of the home in which they have been living.

Constructive trusts of the family home

A significant area where the constructive trust has been used, and has been particularly problematic, is in relation to co-ownership of the family home. Where a couple is married or is in a civil partnership, the law allows the courts to determine how the assets should be divided when a couple is divorced or when a civil partnership is dissolved. The law's role is therefore fairly clearly defined, and the law is entitled to intervene in any way it considers fair. Similarly, where two or more people co-own property without there being any familial relationship between them, again the law's role is fairly clearly defined. The co-owners are able to identify their respective shares when the land is acquired, or the resulting trust mechanism is fairly easily employed to determine that each person is entitled to receive the share they contributed when the land is sold.

Family co-ownership without marriage however is more problematic, and has become significantly more common over the last half-century, when ownership of one's home and the perception of the home as an asset and an investment have also become more common. Therefore, at a time when more people are choosing not to commit to a form of relationship in which the law has entitled itself to intervene (i.e. marriage or civil partnership), it is also a time when more people regard their home as something they wish to protect themselves from being deprived of unjustly.

Of course many cases are unproblematic. A couple whether married or unmarried, will buy a home, and declare their intentions as to how it is to be owned on the TR1 form, and do not deviate from this over time. Alternatively, one may move into the other's home, and an express declaration of trust is made creating a trust by one partner in favour of the other. However, this does not always occur, and therefore, when the couple separates, the parties commence litigation in order to establish that, despite what is stated on the Land Register, their intentions regarding the share each of them intended to obtain is different.

One possibility is that the couple do become joint owners of the family home. The law therefore presumes that the parties intend to share the home equally. However,

sometimes one of the parties will argue that they contributed more than the other and should therefore be entitled to a larger share of the proceeds of sale when the relationship comes to an end and the family home is sold.[9] The first issue for the law therefore is whether, and when, it may rebut the presumption that 'equality is equity'.

However, a second problem is where one cohabitant moves into the other's house. The former is not therefore registered as a co-owner, but nevertheless argues that he or she should be entitled to a share in the family home.

The difficulty, in both cases, is that the parties' intentions may change over the course of time. Therefore, although there may be an intention to share everything when the couple is in that first flush of togetherness, time and disenchantment may breed resentment, with the result that, when the couple splits up, there may be a reluctance to allow the ex-partner anything more than that to which he or she is entitled. There may also be a sense of wanting some form of compensation for the break-up of the relationship and that which the cohabitant feels they he or she has sacrificed for the relationship. Although these are understandable human emotions, emotion cannot be the basis upon which a court judgment may be based. Accordingly, the law's approach has been to utilise the concept of the constructive trust to displace the presumption that joint owners intend to share the proceeds equally.

The early developments of the constructive trust

The twists and turns in the development of the constructive trust are extremely interesting. Early cases such as *Pettit v Pettit* [1970] AC 777 looked at whether there was a common intention between the parties regarding whether and how the property should be divided, and in the absence of a common intention being manifested, what conduct would suffice to imply that a different division of the land from that detailed in the deeds or on the Land Register should be undertaken. The court concluded that financial contributions did suffice, but that improvements to the house should not. Similar conclusions were arrived at in cases such as *Gissing v Gissing* [1971] AC 886, where again it was held that a constructive trust could only be identified where there had been a contribution to the acquisition cost of the property.

EXTRACT

Pettit v Pettit [1970] AC 777

Case facts

In this case, the husband was claiming a share of a matrimonial home owned solely by his wife, on the basis that he had undertaken work to redecorate and improve the property.

Lord Upjohn

If a spouse purchases property out of his or her own money and puts it into his or her own name, then (in the absence of evidence) I can see absolutely no reason for drawing any inference save that it was to be the property of that spouse; bought of course for the common use or common occupation during the marriage, but if sold during the marriage the proceeds

[9] *Stack v Dowden* [2007] UKHL 17.

belong to the purchasing spouse as does the property upon termination of the marriage whether brought about by death or divorce.

Lord Diplock

How, then, does the court ascertain the 'common intention' of spouses as to their respective proprietary interests in a family asset when at the time that it was acquired or improved as a result of contributions in money or money's worth by each of them they failed to formulate it themselves? It may be possible to infer from their conduct that they did in fact form an actual common intention as to their respective proprietary interests and where this is possible the courts should give effect to it. But in the case of transactions between husband and wife relating to family assets their actual common contemplation at the time of its acquisition or improvement probably goes no further than its common use and enjoyment by themselves and their children, and while that use continues their respective proprietary interests in it are of no practical importance to them. They only become of importance if the asset ceases to be used and enjoyed by them in common and they do not think of the possibility of this happening. In many cases, and most of those which come before the courts, the true inference from the evidence is that at the time of its acquisition or improvement the spouses formed no common intention as to their proprietary rights in the family asset. They gave no thought to the subject of proprietary rights at all.

But this does not raise a problem which is peculiar to transactions between husband and wife. It is one with which the courts are familiar in connection with ordinary contracts and to its solution they apply a familiar legal technique. The common situation in which a court has to decide whether or not a term is to be implied in a contract is when some event has happened for which the parties have made no provision in the contract because at the time it was made neither party foresaw the possibility of that event happening and so never in fact agreed as to what its legal consequences would be upon their respective contractual rights and obligations. Nevertheless the court imputes to the parties a common intention which in fact they never formed and it does so by forming its own opinion as to what would have been the common intention of reasonable men as to the effect of that event upon their contractual rights and obligations if the possibility of the event happening had been present to their minds at the time of entering into the contract . . .

In imputing to them a common intention as to their respective proprietary rights which as fair and reasonable men and women they presumably would have formed had they given their minds to it at the time of the relevant acquisition or improvement of a family asset, the court, it has been suggested, is exercising in another guise a jurisdiction to do what it considers itself to be fair and reasonable in all the circumstances and this does not differ in result from the jurisdiction which Lord Denning, in *Appleton v. Appleton* [1965] 1 W.L.R. 25, considered was expressly conferred on the court by section 17 of the Married Women's Property Act, 1882 . . .

In applying the general technique the court is directing its attention to what would have been the common intention of the spouses as fair and reasonable husband and wife at the time of the relevant transaction while they were still happily married and not contemplating its breakdown. The family asset might cease to be needed for the common use and enjoyment of themselves and their children without the marriage breaking down at all. The circumstances of the subsequent breakdown and the conduct of the spouse which contributed to it are irrelevant to this inquiry. If these circumstances are such as to call for an adjustment of the spouses' respective proprietary rights which resulted from their previous transactions the court has jurisdiction to make such adjustments under the Matrimonial Causes Act, 1965 (see *Ulrich v. Ulrich and Felton* [1968] 1 W.L.R. 180). It has no such jurisdiction under section 17 of the Married Women's Property Act, 1882.

> In the present case we are concerned not with the acquisition of a matrimonial home on mortgage, but with improvements to a previously acquired matrimonial home. There is no question that at the time that it was acquired the matrimonial home was the wife's property. It was bought not with the help of a mortgage, but with the proceeds of sale of the previous matrimonial home which the wife had inherited from her grandmother. The husband made no contribution to its purchase and the conveyance of it was to the wife alone. The conduct of the parties is consistent only with the sole proprietary interest in it being that of the wife. During the four years that the spouses lived together in their new home the husband in his spare time occupied himself, as many husbands do, in laying out the garden with a lawn and patio, putting up a side wall with a gate, and in various jobs of redecoration and the like in the house itself. He claimed that these leisure activities had enhanced the value of the property by £1,000 and that he was entitled to a beneficial interest in it of that amount. The learned registrar declared that the husband had a beneficial interest in the proceeds of sale of the property in the sum of £300 . . .
>
> It is common enough nowadays for husbands and wives to decorate and to make improvements in the family home themselves, with no other intention than to indulge in what is now a popular hobby, and to make the home pleasanter for their common use and enjoyment. If the husband likes to occupy his leisure by laying a new lawn in the garden or building a fitted wardrobe in the bedroom while the wife does the shopping, cooks the family dinner or bathes the children, I, for my part, find it quite impossible to impute to them as reasonable husband and wife any common intention that these domestic activities or any of them are to have any effect upon the existing proprietary rights in the family home on which they are undertaken. It is only in the bitterness engendered by the break-up of the marriage that so bizarre a notion would enter their heads.

The 1980s seem to indicate a departure from this purely financial approach, with Lord Denning in particular advocating a more remedial approach to the constructive trust and arguing that a broader range of factors should be acceptable in order to give the 'deserted wife' (or indeed husband) an equitable interest in the family home. He advocated a constructive trust of the new order that could be imposed by way of a remedy (hence the term 'remedial constructive trust) '*whenever justice and good conscience require it*'.[10] Accordingly, where it was considered fair that a spouse or cohabitant should be given a share of the house when the relationship ended, the court should be able to effect this. Lord Denning's approach was essentially to take into consideration the contribution that had been made to the relationship, as opposed to the contribution made to a share of the matrimonial home.

However, since the 1970s and 1980s, the courts have moved away from this approach, and although they are willing to permit the use of the constructive trust where one person has acted fraudulently, to allow the constructive trust to be used whenever an individual court considers that it would be just to do so is felt to be too uncertain, because that which is fair according to one point of view may be unjust according to another. In the context of determining whether one owns a share of a matrimonial home, one argument regarding fairness might be to say that a person should not have an expectation of acquiring a share in something to which they have made no contribution. On the other hand, another argument would be to say that it is unfair to have regard only to one's financial contribution to 'investment' assets such as land, which overlooks the fact that the other person may have contributed to the everyday expenses of food and

[10] *Hussey v Palmer* [1972] 3 All ER 744 at 747.

clothing, household bills, as well as making non-financial contributions to sustaining the relationship. In the New Zealand case of *Carly v Farrelly* [1975] 1 NZLR 356 at 367 for example, Mahon J explains that Lord Denning's approach '*is not only vague in its outline but which must disqualify itself from acceptance as a valid principle of jurisprudence by its total uncertainty of application and result*'. Accordingly, for this reason, the law searches for a greater degree of certainty as to the mutually agreed intentions before it will identify that a constructive trust has come into being.

Therefore, by 1990 the pendulum had swung back again, and the leading authority has for a long time been *Lloyds Bank v Rosset* [1991] 1 AC 107 which required that there must either be an express common intention between the parties or an implied common intention, coupled with a detrimental reliance upon that express or implied common intention on the part of the claimant.

Common intention

An express common intention might arise from any agreement, arrangement or understanding between the parties, either prior to, or at the time the house was bought, or exceptionally after the house is initially purchased (such as where the cohabitant and the owner later agree that the cohabitant will make the mortgage repayments to compensate the owner for the fact that he or she paid the initial deposit). Accordingly, cases such as *Eves v Eves* [1975] 3 All ER 768 and *Grant v Edwards* [1986] Ch 638 have been interpreted as being express common intention cases because the landowner had reassured his cohabitant that, were it not for their specific circumstances (a mistaken belief in *Eves v Eves* that the cohabitant was too young to be registered as a co-owner, and, in *Grant v Edwards*, the cohabitant's ongoing divorce proceedings from her ex-husband), the house would have been put into the parties' joint names. If there was no express discussion or arrangement, then it is necessary for the court to imply a common intention. In order for a common intention to be implied, in *Lloyds Bank v Rosset*, Lord Bridge doubted whether anything other than a direct contribution to the acquisition of the land would suffice.

EXTRACT

Lloyds Bank v Rosset [1991] 1 AC 107

Case facts

Mr and Mrs Rosset wished to buy a house, which was funded partly by a trust fund for the benefit of Mr Rosset, and partly by a mortgage loan from Lloyds Bank. The trustees of Mr Rosset's trust fund insisted that the house should be put in Mr Rosset's sole name. The sellers of the house had agreed to let Mr and Mrs Rosset begin the renovation work on the house before the sale and purchase contracts were exchanged, and therefore, when the Rossets failed to repay the mortgage loan, Mrs Rosset argued, firstly, that Mr Rosset was a constructive trustee of the house for her benefit because of the work she had undertaken on its renovation, and, secondly, that because she was in actual occupation since before the exchange of contracts, her entitlement to the house preceded that of Lloyds Bank and therefore the bank could not sell her share of the house.

Lord Bridge

Both the purchase price of the property and the cost of the works of renovation were paid by Mr. Rosset alone and Mrs. Rosset made no financial contribution to the acquisition of the property.

The case pleaded and carefully particularised by Mrs. Rosset in support of her claim to an equitable interest in the property was that it had been expressly agreed between her and her husband in conversations before November 1982 that the property was to be jointly owned and that in reliance on this agreement she had made a significant contribution in kind to the acquisition of the property by the work she had personally undertaken in the course of the renovation of the property which was sufficient to give rise to a constructive trust in her favour.

There was a conflict of evidence between Mr. and Mrs. Rosset on the vital issue raised by this pleading. The question the judge had to determine was whether he could find that before the contract to acquire the property was concluded they had entered into an agreement, made an arrangement, reached an understanding or formed a common intention that the beneficial interest in the property would be jointly owned. I do not think it is of importance which of these alternative expressions one uses. Spouses living in amity will not normally think it necessary to formulate or define their respective interests in property in any precise way. The expectation of parties to every happy marriage is that they will share the practical benefits of occupying the matrimonial home whoever owns it. But this is something quite distinct from sharing the beneficial interest in the property asset which the matrimonial home represents. These considerations give rise to special difficulties for judges who are called on to resolve a dispute between spouses who have parted and are at arm's length as to what their common intention or understanding with respect to interests in property was at a time when they were still living as a united family and acquiring a matrimonial home in the expectation of living in it together indefinitely.

Since Mr. Rosset was providing the whole purchase price of the property and the whole cost of its renovation, Mrs. Rosset would, I think, in any event have encountered formidable difficulty in establishing her claim to joint beneficial ownership. The claim as pleaded and as presented in evidence was, by necessary implication, to an equal share in the equity. But to sustain this it was necessary to show that it was Mr. Rosset's intention to make an immediate gift to his wife of half the value of a property acquired for £57,500 and improved at a further cost of some £15,000. What made it doubly difficult for Mrs. Rosset to establish her case was the circumstance, which was never in dispute, that Mr. Rosset's uncle, who was trustee of his Swiss inheritance, would not release the funds for the purchase of the property except on terms that it was to be acquired in Mr. Rosset's sole name. If Mr. and Mrs. Rosset had ever thought about it, they must have realised that the creation of a trust giving Mrs. Rosset a half share, or indeed any other substantial share, in the beneficial ownership of the property would have been nothing less than a subterfuge to circumvent the stipulation which the Swiss trustee insisted on as a condition of releasing the funds to enable the property to be acquired. In these circumstances, it would have required very cogent evidence to establish that it was the Rossets' common intention to defeat the evident purpose of the Swiss trustee's restriction by acquiring the property in Mr. Rosset's name alone but to treat it nevertheless as beneficially owned jointly by both spouses. . . . Even if there had been the clearest oral agreement between Mr. and Mrs. Rosset that Mr. Rosset was to hold the property in trust for them both as tenants in common, this would, of course, have been ineffective since a valid declaration of trust by way of gift of a beneficial interest in land is required by section 53(1) of the Law of Property Act 1925 to be in writing. But if Mrs. Rosset had, as pleaded, altered her position in reliance on the agreement this could have given rise to an enforceable interest in her favour by way either of a constructive trust or of a proprietary estoppel.

Having rejected the contention that there had been any concluded agreement or arrangement or any common intention formed before contracts for the purchase of the property were exchanged on 23 November 1982 that Mrs. Rosset should have any beneficial interest, the judge concentrated his attention on Mrs. Rosset's activities in connection with the renovation

works as a possible basis from which to infer such a common intention. It is clear from these passages in the judgment that the judge based his inference of a common intention that Mrs. Rosset should have a beneficial interest in the property under a constructive trust essentially on what Mrs. Rosset did in and about assisting in the renovation of the property between the beginning of November 1982 and the date of completion on 17 December 1982. Yet by itself this activity, it seems to me, could not possibly justify any such inference. It was common ground that Mrs. Rosset was extremely anxious that the new matrimonial home should be ready for occupation before Christmas if possible. In these circumstances it would seem the most natural thing in the world for any wife, in the absence of her husband abroad, to spend all the time she could spare and to employ any skills she might have, such as the ability to decorate a room, in doing all she could to accelerate progress of the work quite irrespective of any expectation she might have of enjoying a beneficial interest in the property. The judge's view that some of this work was work 'upon which she could not reasonably have been expected to embark unless she was to have an interest in the house' seems to me, with respect, quite untenable. The impression that the judge may have thought that the share of the equity to which he held Mrs. Rosset to be entitled had been 'earned' by her work in connection with the renovation is emphasised by his reference in the concluding sentence of his judgment to the extent to which her 'qualifying contribution' reduced the cost of the renovation.

On any view the monetary value of Mrs. Rosset's work expressed as a contribution to a property acquired at a cost exceeding £70,000 must have been so trifling as to be almost de minimis. I should myself have had considerable doubt whether Mrs. Rosset's contribution to the work of renovation was sufficient to support a claim to a constructive trust in the absence of writing to satisfy the requirements of section 51 of the Law of Property Act 1925 even if her husband's intention to make a gift to her of half or any other share in the equity of the property had been clearly established or if he had clearly represented to her that that was what he intended. But here the conversations with her husband on which Mrs. Rosset relied, all of which took place before November 1982, were incapable of lending support to the conclusion of a constructive trust in the light of the judge's finding that by that date there had been no decision that she was to have any interest in the property. . . . These considerations lead me to the conclusion that the judge's finding that Mr. Rosset held the property as constructive trustee for himself and his wife cannot be supported and it is on this short ground that I would allow the appeal . . . The first and fundamental question which must always be resolved is whether, independently of any inference to be drawn from the conduct of the parties in the course of sharing the house as their home and managing their joint affairs, there has at any time prior to acquisition, or exceptionally at some later date, been any agreement, arrangement or understanding reached between them that the property is to be shared beneficially. The finding of an agreement or arrangement to share in this sense can only, I think, be based on evidence of express discussions between the partners, however imperfectly remembered and however imprecise their terms may have been. Once a finding to this effect is made it will only be necessary for the partner asserting a claim to a beneficial interest against the partner entitled to the legal estate to show that he or she has acted to his or her detriment or significantly altered his or her position in reliance on the agreement in order to give rise to a constructive trust or a proprietary estoppel.

In sharp contrast with this situation is the very different one where there is no evidence to support a finding of an agreement or arrangement to share, however reasonable it might have been for the parties to reach such an arrangement if they had applied their minds to the question, and where the court must rely entirely on the conduct of the parties both as the basis from which to infer a common intention to share the property beneficially and as the conduct relied on to give rise to a constructive trust. In this situation direct contributions to the purchase price by the partner who is not the legal owner, whether initially or by payment of mortgage

instalments, will readily justify the inference necessary to the creation of a constructive trust. But, as I read the authorities, it is at least extremely doubtful whether anything less will do.

Outcome

Accordingly, Lloyds' Bank's appeal was allowed, and so it could enter into possession and sell the Rossets' house.

The cases that followed *Lloyds Bank v Rosset* sought to clarify what was meant by a contribution to the purchase price, which was held to include contributions to the deposit or the mortgage instalments – however that was achieved,[11] a contribution to alterations and improvements that increased the value of the home,[12] an entitlement to a discount on the purchase of property being sold by a local authority[13] or an arrangement whereby one person would pay the utility bills in order to free the other up to pay the mortgage instalments. Accordingly, in *Stack v Dowden* [2007] UKHL 17, Baroness Hale explains that the court may look at the entire course of dealing in order to establish what the parties' common intention is. She states:

> In law, 'context is everything' and the domestic context is very different from the commercial world. Each case will turn on its own facts. Many more factors than financial contributions may be relevant to divining the parties' true intentions. These include: any advice or discussions at the time of the transfer which cast light upon their intentions then; the reasons why the home was acquired in their joint names; the reasons why (if it be the case) the survivor was authorised to give a receipt for the capital moneys; the purpose for which the home was acquired; the nature of the parties' relationship; whether they had children for whom they both had responsibility to provide a home; how the purchase was financed, both initially and subsequently; how the parties arranged their finances, whether separately or together or a bit of both; how they discharged the outgoings on the property and their other household expenses. When a couple are joint owners of the home and jointly liable for the mortgage, the inferences to be drawn from who pays for what may be very different from the inferences to be drawn when only one is owner of the home. The arithmetical calculation of how much was paid by each is also likely to be less important. It will be easier to draw the inference that they intended that each should contribute as much to the household as they reasonably could and that they would share the eventual benefit or burden equally. The parties' individual characters and personalities may also be a factor in deciding where their true intentions lay. In the cohabitation context, mercenary considerations may be more to the fore than they would be in marriage, but it should not be assumed that they always take pride of place over natural love and affection. At the end of the day, having taken all this into account, cases in which the joint legal owners are to be taken to have intended that their beneficial interests should be different from their legal interests will be very unusual.

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[11] In *Midland Bank v Cooke* [1995] 4 All ER 462 for example, the contribution was established by the fact that a sum of money had been given to the couple as a wedding present from the husband's parents. This gift was deemed to have been given to both of them in equal shares, and the fact that they had used this money in order to pay the deposit on the house was sufficient to give rise to a contribution on the part of the wife.

[12] *Drake v Whipp* [1996] 2 FCR 296.

[13] *Goodman v Carlton* [2002] EWCA Civ 545.

> This is not, of course, an exhaustive list. There may also be reason to conclude that, whatever the parties' intentions at the outset, these have now changed. An example might be where one party has financed (or constructed himself) an extension or substantial improvement to the property, so that what they have now is significantly different from what they had then.

Detrimental reliance

Once a common intention has been demonstrated, it is then necessary to show that the cohabitant has relied to their detriment on that common intention. As Lord Bridge explains in *Lloyds Bank v Rosset* above, if the parties possess a common intention regarding beneficial ownership then, ordinarily that should be evidenced in writing in accordance with s.53 Law of Property Act 1925. Accordingly it is necessary to go beyond that common intention in order to displace the law's requirement for formality.

In order to overcome this requirement, it is necessary to demonstrate that the cohabitant has relied to their detriment on the common intention. Commonly, the detriment will be in the form of the expenditure of money, such as the cohabitant who contributes to the mortgage repayments in the expectation of acquiring a share. However, the detriment does not have to be financial, or even quantifiable in financial terms. Any change of position in reliance on the common intention will suffice, such as (in *Eves v Eves*):

> extensive decorative work to the downstairs rooms and generally clean[ing] the whole house . . . paint[ing] the brickwork of the front of the house [and breaking] up with a 14-lb. sledge hammer the concrete surface which covered the whole of the front garden and dispos[ing] of the rubble into a skip, work[ing] in the back garden and . . . demolish[ing] a shed there and put[ting] up a new shed. She also prepared the front garden for turfing.

Similarly in *Chan Pu Chan v Leung Kam Ho* [2003] 1 FLR 23, the detriment came in the form of the claimant having worked to maintain the defendant's business.

Essentially, detrimental reliance means doing something that the cohabitant would not have done if they did not expect to acquire a share in the house. Therefore, in *Lloyds Bank v Rosset*, Mrs Rosset's work, which mainly consisted of supervising the activities of others and making the house habitable for her family, was not regarded as acting detrimentally because it was considered that these were perfectly reasonable activities for a person to undertake and that they were activities that a spouse and parent would have undertaken for the benefit of their family even if they were not going to acquire a share of the family home. Accordingly, detrimental reliance excludes that which you would have done irrespective of your expectations. This is why situations where a spouse or a cohabitant has looked after any children is problematic in terms of establishing a constructive trust. It may be argued that one does not care for one's children because one is expecting to acquire a share of a matrimonial (or cohabitational home) – instead one looks after one's children out of a sense of love, responsibility, moral and social duty etc. and that one would look after one's children even where there was no expectation of acquiring a share in the matrimonial home. Nevertheless, the fact that one cohabitant has, for example, given up their work to look after the children, may be one of the relevant factors when the courts unpick the 'whole course of dealing' described by Baroness Hale in *Stack v Dowden* in an attempt to discover how the parties arranged their finances. Accordingly, although a common intention may be established under Baroness Hale's holistic approach, it may be that without some substantial detriment that is financially quantifiable, a constructive trust will not be discovered.

Quantification of entitlement

Once a constructive trust has been established based on common intention and detrimental reliance, the law must then consider how the owner and the cohabitant's shares are to be distributed. Again this will depend on the common intention of the parties where this has been manifested, and the courts will aim to give effect to that common intention. Therefore, if for example, the common intention is that the parties intended that the house be shared equally between them, then the courts will give effect to that intention. In *Gissing v Gissing*, Lord Reid explains:

> . . . if at the time of its acquisition and transfer of the legal estate into the name of one or other of them an express agreement has been made between them as to the way in which the beneficial interest shall be held, the court will give effect to it – notwithstanding the absence of any written declaration of trust.[14]

If no common intention as to the respective shares of the parties can be shown, then the courts must infer the parties' intentions based on the whole course of dealing between them, and whether their conduct indicates that the parties were treating the house as though ownership were shared.[15] Therefore, in *Stack v Dowden*, the fact that the parties had always kept their finances entirely separate from each other indicated that there was no common intention regarding shared ownership of the family assets. Baroness Hale explains:

> This is not a case in which it can be said that the parties pooled their separate resources, even notionally, for the common good. The only things they ever had in their joint names were Chatsworth Road and the associated endowment policy. Everything else was kept strictly separate. Each made separate savings and investments most of which it was accepted were their own property . . . This is, therefore, a very unusual case. There cannot be many unmarried couples who have lived together for as long as this, who have had four children together, and whose affairs have been kept as rigidly separate as this couple's affairs were kept. This is all strongly indicative that they did not intend their shares, even in the property which was put into both their names, to be equal (still less that they intended a beneficial joint tenancy with the right of survivorship should one of them die before it was severed).

The course of Mr Stack and Ms Dowden's relationship did not therefore indicate that they intended to share beneficial ownership of the house as the Land Register indicated. Their whole course of dealing had emphasised very clearly that what was Ms Dowden's belonged to Ms Dowden, and what was Mr Stack's belonged to Mr Stack. Accordingly, the House of Lords quantified their share according to each party's contribution.

Establishing what the common intention was regarding shares involves examining how the parties conducted themselves. In *Oxley v Hiscock* [2004] EWCA Civ 546, Chadwick LJ explains that this is likely to include looking at matters such as 'includes the arrangements which they make from time to time in order to meet the outgoings (for example, mortgage contributions, council tax and utilities, repairs, insurance and housekeeping) which have to be met if they are to live in the property as their home'. Although this approach was endorsed by Baroness Hale in the case of *Stack v Dowden* [2007] UKHL 17 at para 61, Lord Walker was less willing for the principles applied in relation to proprietary estoppel to apply to constructive trusts, because estoppel focuses more on correcting the inequitable behaviour of the registered proprietor (a manifestation of the 'equity will not allow a wrong to be without a remedy' principle, while a constructive trust looks at giving effect to the true objectives of the parties ('equity looks to the intention rather than the form').

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[14] *Gissing v Gissing* [1971] AC 886.
[15] *Stack v Dowden* [2007] UKHL 17.

It is only if no clear division of the shares is apparent that the courts will decide on a share according to what is a fair apportionment of the proceeds of sale.

The current law

Property conveyed into joint names

This then leads us to the current statement of the law, emanating from the case of *Jones v Kernott* [2011] UKSC 53. When the land is conveyed, the buyer must complete a form issued by HM Land Registry. This is called a TR1 form and, as can be seen on page 348, question 10 of this form asks the buyers to indicate whether the parties intend to own the property on trust for themselves as joint tenants, as tenants in common in unequal shares, or as tenants in common in unequal shares (see Figure 14.1). This form therefore requires the parties to discuss their intentions, and the answer given will be presumed to provide an accurate representation of the parties' intentions. Nevertheless, it is conceded that this does not always suffice, particularly in situations where the parties have given no thought to the issue, or where their intentions have changed over time.

EXTRACT

Moran, A. (2007) 'Case Comment: Anything to Declare? Express declaration of trust on Land Registry form TR1: the doubts raised in *Stack v Dowden* [2007]' *Conveyancer and Property Lawyer* 364

Where in a case of a transfer of title to joint proprietors the beneficial interests are expressly declared, the declaration is conclusive save where there is mistake or fraud: *Goodman v Gallant* [1986] Fam 106 . . . Many cases concerning disputes as to the beneficial interests a couple have in their home have arisen from a failure – which was not always the fault of the legal practitioner: *Oxley v Hiscock* – expressly to declare the beneficial interests. In this connection, the despair voiced by Ward L.J. in *Carlton v Goodman* [2002] EWCA Civ 545 at [44] is well known.

Part of the reason for the problem was that forms of transfer, either the old Form 19(JP) or, perhaps, legal practitioners' own precedents, did not provide for an express declaration of trust . . . Form TR1, in use from 1 April 1998, provides a box for the transferees to declare whether they are to hold the property on trust for themselves as joint tenants, or on trust for themselves as tenants in common in equal shares, or on some other trusts which are inserted on the form. If this is invariably complied with, the problem confronting us here will eventually disappear. Unfortunately, however, the transfer will be valid whether or not this part of the form is completed. The form itself states that the transferees are only required to execute it 'if the transfer contains Transferee's covenants or declarations or contains an application by the Transferee (eg for a restriction)'. So there may still be transfers of registered land into joint names in which there is no express declaration of the beneficial interests. However desirable such a declaration may be, it is unrealistic, in the consumer context, to expect that it will be executed independently of the forms required to acquire the legal estate. Not only do solicitors and licensed conveyancers compete on price, but more and more people are emboldened to do their own conveyancing. The Land Registry form which has been prescribed since 1998 is to be applauded. If its completion and execution by or on behalf of all joint proprietors were mandatory, the problem we now face would disappear. However, the form might then include an option for those who deliberately preferred not to commit themselves as to the beneficial interests at the outset and to rely on the principles discussed below. (*continued on p. 350*)

Land Registry
Transfer of whole of registered title(s)

TR1

If you need more room than is provided for in a panel, and your software allows, you can expand any panel in the form. Alternatively use continuation sheet CS and attach it to this form.

Leave blank if not yet registered.	1 Title number(s) of the property:
Insert address including postcode (if any) or other description of the property, for example 'land adjoining 2 Acacia Avenue'.	2 Property:
	3 Date:
Give full name(s).	4 Transferor: For UK incorporated companies/LLPs Registered number of company or limited liability partnership including any prefix: For overseas companies (a) Territory of incorporation: (b) Registered number in the United Kingdom including any prefix:
Complete as appropriate where the transferor is a company.	
Give full name(s).	5 Transferee for entry in the register: For UK incorporated companies/LLPs Registered number of company or limited liability partnership including any prefix: For overseas companies (a) Territory of incorporation: (b) Registered number in the United Kingdom including any prefix:
Complete as appropriate where the transferee is a company. Also, for an overseas company, unless an arrangement with Land Registry exists, lodge either a certificate in Form 7 in Schedule 3 to the Land Registration Rules 2003 or a certified copy of the constitution in English or Welsh, or other evidence permitted by rule 183 of the Land Registration Rules 2003.	
Each transferee may give up to three addresses for service, one of which must be a postal address whether or not in the UK (including the postcode, if any). The others can be any combination of a postal address, a UK DX box number or an electronic address.	6 Transferee's intended address(es) for service for entry in the register:
	7 The transferor transfers the property to the transferee

Figure 14.1 The TR1 form

Place 'X' in the appropriate box. State the currency unit if other than sterling. If none of the boxes apply, insert an appropriate memorandum in panel 11.

8 Consideration

☐ The transferor has received from the transferee for the property the following sum (in words and figures):

☐ The transfer is not for money or anything that has a monetary value

☐ Insert other receipt as appropriate:

Place 'X' in any box that applies.

Add any modifications.

9 The transferor transfers with

☐ full title guarantee

☐ limited title guarantee

Where the transferee is more than one person, place 'X' in the appropriate box.

Complete as necessary.

The registrar will enter a Form A restriction in the register *unless*:
- an 'X' is placed:
  - in the first box, or
  - in the third box and the details of the trust or of the trust instrument show that the transferees are to hold the property on trust for themselves alone as joint tenants, *or*
- it is clear from completion of a form JO lodged with this application that the transferees are to hold the property on trust for themselves alone as joint tenants.

Please refer to Land Registry's Public Guide *18 – Joint property ownership* and Practice Guide *24 – Private trusts of land* for further guidance. These guides are available on our website www.landregistry.gov.uk

10 Declaration of trust. The transferee is more than one person and

☐ they are to hold the property on trust for themselves as joint tenants

☐ they are to hold the property on trust for themselves as tenants in common in equal shares

☐ they are to hold the property on trust:

Insert here any required or permitted statement, certificate or application and any agreed covenants, declarations and so on.

11 Additional provisions

Figure 14.1 (*continued*)

The transferor must execute this transfer as a deed using the space opposite. If there is more than one transferor, all must execute. Forms of execution are given in Schedule 9 to the Land Registration Rules 2003. If the transfer contains transferee's covenants or declarations or contains an application by the transferee (such as for a restriction), it must also be executed by the transferee.

If there is more than one transferee and panel 10 has been completed, each transferee may also execute this transfer to comply with the requirements in section 53(1)(b) of the Law of Property Act 1925 relating to the declaration of a trust of land. Please refer to Land Registry's Public Guide *18 – Joint property ownership* and Practice Guide *24 – Private trusts of land* for further guidance.

12 Execution

WARNING
If you dishonestly enter information or make a statement that you know is, or might be, untrue or misleading, and intend by doing so to make a gain for yourself or another person, or to cause loss or the risk of loss to another person, you may commit the offence of fraud under section 1 of the Fraud Act 2006, the maximum penalty for which is 10 years' imprisonment or an unlimited fine, or both.

Failure to complete this form with proper care may result in a loss of protection under the Land Registration Act 2002 if, as a result, a mistake is made in the register.

Under section 66 of the Land Registration Act 2002 most documents (including this form) kept by the registrar relating to an application to the registrar or referred to in the register are open to public inspection and copying. If you believe a document contains prejudicial information, you may apply for that part of the document to be made exempt using Form EX1, under rule 136 of the Land Registration Rules 2003.

Figure 14.1 (*continued*)

If an express declaration has been made regarding the beneficial interests, this will be presumed to reflect the parties' intentions. If no declaration has been made, or where the parties wish to rebut that presumption, then the parties must adduce evidence as to their respective intentions:

> The time has come to make it clear, in line with *Stack v Dowden* (see also *Abbott v Abbott* [2007] UKPC 53, [2007] 2 All ER 432, [2008] 1 FLR 1451), that in the case of the purchase of a house or flat in joint names for joint occupation by a married or unmarried couple, where both are responsible for any mortgage, there is no presumption of a resulting trust arising from their having contributed to the deposit (or indeed the rest of the purchase) in unequal shares. The presumption is that the parties intended a joint tenancy both in law and in equity. But that presumption can of course be rebutted by evidence of a contrary intention, which may more readily be shown where the parties did not share their financial resources [(Per Lord Walker and Lady Hale SCJJ in *Jones v Kernott* [2012] 1 All ER 1265 at 1273)].

Accordingly, if the parties' intentions have changed, as in the case of *Jones v Kernott*, since the declaration of trust, then the court must either have evidence of that, or infer what would be reasonable as intentions if the parties had thought upon the matter. Lord Walker and Lady Hale continue, by stating:

In a case such as this, where the parties already share the beneficial interest, and the question is what their interests are and whether their interests have changed, the court will try to deduce what their actual intentions were at the relevant time. It cannot impose a solution upon them which is contrary to what the evidence shows that they actually intended. But if it cannot deduce exactly what shares were intended, it may have no alternative but to ask what their intentions as reasonable and just people would have been had they thought about it at the time. This is a fallback position which some courts may not welcome, but the court has a duty to come to a conclusion on the dispute put before it.

In this case, there is no need to impute an intention that the parties' beneficial interests would change, because the judge made a finding that the intentions of the parties did in fact change. At the outset, their intention was to provide a home for themselves and their progeny. But thereafter their intentions did change significantly. He did not go into detail, but the inferences are not difficult to draw. They separated in October 1993. No doubt in many such cases, there is a period of uncertainty about where the parties will live and what they will do about the home which they used to share. This home was put on the market in late 1995 but failed to sell. Around that time a new plan was formed. The life insurance policy was cashed in and Mr Kernott was able to buy a new home for himself. He would not have been able to do this had he still had to contribute towards the mortgage, endowment policy and other outgoings on 39 Badger Hall Avenue. The logical inference is that they intended that his interest in Badger Hall Avenue should crystallise then. Just as he would have the sole benefit of any capital gain in his own home, Ms Jones would have the sole benefit of any capital gain in Badger Hall Avenue. Insofar as the judge did not in so many words infer that this was their intention, it is clearly the intention which reasonable people would have had had they thought about it at the time. But in our view it is an intention which he both could and should have inferred from their conduct.

Accordingly, their Lordships and Ladyship summarised the law as follows:

In summary, therefore, the following are the principles applicable in a case such as there a family home is bought in the joint names of a cohabiting couple who are both responsible for any mortgage, but without any express declaration of their beneficial interests:

(1) The starting point is that equity follows the law and they are joint tenants both in law and in equity.

(2) That presumption can be displaced by showing (a) that the parties had a different common intention at the time when they acquired the home, or (b) that they later formed the common intention that their respective shares would change.

(3) Their common intention is to be deduced objectively from their conduct:

the relevant intention of each party is the intention which was reasonably understood by the other party to be manifested by that party's words and conduct notwithstanding that he did not consciously formulate that intention in his own mind or even acted with some different intention which he did not communicate to the other party (Lord Diplock in *Gissing v Gissing* [1971] AC 886, 906).

Examples of the sort of evidence which might be relevant to drawing such inferences are given in *Stack v Dowden*, at para 69.

(4) In those cases where it is clear either (a) that the parties did not intend joint tenancy at the outset, or (b) had changed their original intention, but it is not possible to ascertain by direct evidence or by inference what their actual intention was as to the shares in which they would own the property, 'the answer is that each is entitled to that share which the court considers fair having regard to the whole course

of dealing between them in relation to the property': Chadwick LJ in *Oxley v Hiscock* [2005] Fam 211, para 69. In our judgment, 'the whole course of dealing . . . in relation to the property' should be given a broad meaning, enabling a similar range of factors to be taken into account as may be relevant to ascertaining the parties' actual intentions.

(5) Each case will turn on its own facts. Financial contributions are relevant but there are many other factors which may enable the court to decide what shares were either intended (as in case (3)) or fair (as in case (4)).

Property in the name of one owner only

Although *Jones v Kernott* was not a case concerned with the situation where the house is in the name of one party only, the Supreme Court did consider how the situation should be dealt with in those circumstances:

> The first issue is whether it was intended that the other party have any beneficial interest in the property at all. If he does, the second issue is what that interest is. There is no presumption of joint beneficial ownership. But their common intention has once again to be deduced objectively from their conduct.

It is the parties' conduct that will also determine the quantification of shares to be distributed to the parties. This will occur in exactly the same way as is described above in relation to land owned by both parties where they either desire to rebut the declaration of trust on the TR1 form or no declaration of trust was ever made.

Again, the starting point is the title deeds to the land, or the Land Register. If the title to the land is in the name of one person, then the law presumes that beneficial ownership is also vested in that person, and the cohabitant must therefore rebut that presumption. In *Oxley v Hiscock*, confirmed in *Stack v Dowden* and *Jones v Kernott*, Chadwick LJ explained:

> It is important to have in mind the underlying requirement, imposed by section 53(1) of the Law of Property Act 1925, (a) that no interest in land can be created orally and (b) that no declaration of trust respecting land can have effect if made orally. But section 53(2) excludes from that requirement 'the creation or operation of resulting, implied or constructive trusts'. It is the requirement in section 53(1) of the 1925 Act – and the saving provision in section 53(2)-which has led to the need, in a case where one former co-habitee asserts against the other (in whose sole name the property is registered) a beneficial interest arising out of some informal arrangement or understanding (not evidenced in writing) or from subsequent conduct, to establish the existence of a constructive trust; or else to rely on a resulting trust arising from contributions . . . [In] 'cases of this nature' [and b]y that, I mean cases in which the common features are: (i) the property is bought as a home for a couple who, although not married, intend to live together as man and wife; (ii) each of them makes some financial contribution to the purchase; (iii) the property is purchased in the sole name of one of them; and (iv) there is no express declaration of trust . . . the first question is whether there is evidence from which to infer a common intention, communicated by each to the other, that each shall have a beneficial share in the property. In many such cases-of which the present is an example-there will have been some discussion between the parties at the time of the purchase which provides the answer to that question. Those are cases within the first of Lord Bridge's categories in *Lloyds Bank plc v Rosset* [1991] 1 AC 107. In other cases-where the evidence is that the matter was not discussed at all-an affirmative answer will readily be inferred from the fact that each has made a financial contribution. Those are cases within Lord Bridge's second

category. And, if the answer to the first question is that there was a common intention, communicated to each other, that each should have a beneficial share in the property, then the party who does not become the legal owner will be held to have acted to his or her detriment in making a financial contribution to the purchase in reliance on the common intention.

In those circumstances, the second question to be answered in cases of this nature is: 'what is the extent of the parties' respective beneficial interests in the property?' Again, in many such cases, the answer will be provided by evidence of what they said and did at the time of the acquisition. But, in a case where there is no evidence of any discussion between them as to the amount of the share which each was to have-and even in a case where the evidence is that there was no discussion on that point-the question still requires an answer. It must now be accepted that (at least in this court and below) the answer is that each is entitled to that share which the court considers fair having regard to the whole course of dealing between them in relation to the property. And, in that context, 'the whole course of dealing between them in relation to the property' includes the arrangements which they make from time to time in order to meet the outgoings (for example, mortgage contributions, council tax and utilities, repairs, insurance and housekeeping) which have to be met if they are to live in the property as their home.

As the cases show, the courts have not found it easy to reconcile that final step with a traditional, property-based, approach. It was rejected, in unequivocal terms, by Dillon LJ in *Springette v Defoe* [1992] 2 FLR 388, 393 when he said: 'The court does not as yet sit, as under a palm tree, to exercise a general discretion to do what the man in the street, on a general overview of the case, might regard as fair.' Three strands of reasoning can be identified.

(1) That suggested by Lord Diplock in *Gissing v Gissing* [1971] AC 886, 909D and adopted by Nourse LJ in *Stokes v Anderson* [1991] 1 FLR 391, 399G, 400B-C. The parties are taken to have agreed at the time of the acquisition of the property that their respective shares are not to be quantified then, but are left to be determined when their relationship comes to an end or the property is sold on the basis of what is then fair having regard to the whole course of dealing between them. The court steps in to determine what is fair because, when the time came for that determination, the parties were unable to agree.

(2) That suggested by Waite LJ in *Midland Bank plc v Cooke* [1995] 4 All ER 562, 574D-G. The court undertakes a survey of the whole course of dealing between the parties 'relevant to their ownership and occupation of the property and their sharing of its burdens and advantages' in order to determine 'what proportions the parties must be assumed to have intended [from the outset] for their beneficial ownership'. On that basis the court treats what has taken place while the parties have been living together in the property as evidence of what they intended at the time of the acquisition.

(3) That suggested by Sir Nicolas Browne-Wilkinson V-C in *Grant v Edwards* [1986] Ch 638, 656G-H, 657H and approved by Robert Walker LJ in *Yaxley v Gotts* [2000] Ch 162, 177C-E. The court makes such order as the circumstances require in order to give effect to the beneficial interest in the property of the one party, the existence of which the other party (having the legal title) is estopped from denying. That, I think, is the analysis which underlies the decision of this court in *Drake v Whipp* [1996] 1 FLR 826, 831E-G.

> For my part, I find the reasoning adopted by this court in *Midland Bank plc v Cooke* to be the least satisfactory of the three strands. It seems to me artificial – and an unnecessary fiction – to attribute to the parties a common intention that the extent of their respective beneficial interests in the property should be fixed as from the time of the acquisition, in circumstances in which all the evidence points to the conclusion that, at the time of the acquisition, they had given no thought to the matter. The same point can be made – although with less force – in relation to the reasoning that, at the time of the acquisition, their common intention was that the amount of the respective shares should be left for later determination. But it can be said that, if it were their common intention that each should have some beneficial interest in the property – which is the hypothesis upon which it becomes necessary to answer the second question – then, in the absence of evidence that they gave any thought to the amount of their respective shares, the necessary inference is that they must have intended that question would be answered later on the basis of what was then seen to be fair. But, as I have said, I think that the time has come to accept that there is no difference in outcome, in cases of this nature, whether the true analysis lies in constructive trust or in proprietary estoppel . . . he right question, in the circumstances of this case, was: 'what would be a fair share for each party having regard to the whole course of dealing between them in relation to the property?'
>
> I think that that is a question to which this court can, and should, give an answer . . . In my view to declare that the parties were entitled in equal shares would be unfair to Mr Hiscock. It would give insufficient weight to the fact that his direct contribution to the purchase price (£60,700) was substantially greater than that of Mrs Oxley (£36,300). On the basis of the judge's finding that there was in this case 'a classic pooling of resources' and conduct consistent with an intention to share the burden of the property (by which she must, I think, have meant the outgoings referable to ownership and cohabitation), it would be fair to treat them as havingmade approximately equal contributions to the balance of the purchase price (£30,000). Taking that into account with their direct contributions at the time of the purchase, I would hold that a fair division of the proceeds of sale of the property would be 60% to Mr Hiscock and 40% to Mrs Oxley.

This approach was endorsed by the Supreme Court in *Stack v Dowden* and *Jones v Kernott*, although the Law Commission did consider that Lord Bridge had set the hurdle rather too high for cohabitants by requiring them to prove either a common intention or a contribution to the purchase price.[16] Nevertheless, the current law is that the parties must establish either that there was a common intention through '*agreement, arrangement or understanding*'.[17] If there is no such agreement, then there must be a reliance on conduct. In *Lloyds Bank v Rosset*, Lord Bridge regarded anything less than direct financial contributions to the purchase price, i.e. payment of either the deposit or the mortgage instalments, as being insufficient. This would seem to be at odds with the later approach in *Stack v Dowden* and *Jones v Kernott,* both of which emphasise the 'whole course of dealing.' Furthermore, in *Stack v Dowden*, Lord Walker viewed the need for the contribution to be referable to the property in some way, rather than being a contribution to the relationship as being problematic.

Accordingly, later cases have accepted indirect contributions as being acceptable. For example, in *Hyett v Stanley* [2003] ECWA Civ 942 for example, a joint mortgage loan was

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[16] Law Commission (2002) *Sharing Homes: A Discussion Paper* (2002, Law Com No 278) at para 4.23.
[17] *Lloyds Bank v Rosset* [1990] 1 All ER 1111 at p.1116 per Lord Bridge.

sufficient to give rise to a common intention regarding the fact that there was an intention for the non-owner to acquire a share. Similarly, an entitlement to a discount,[18] or a contribution to the increase in the value of the property, would be accepted.

Nevertheless, in all the cases where a constructive trust has been found, the contribution made by the non-owner has been related in some way to the value of the land. Therefore in *Burns v Burns* [1984] Ch 317, contributing to the household expenses was not sufficient to give rise to an interest under a constructive trust, unless there is some agreement whereby one person pays the bills in order to enable the other to repay the mortgage loan. Furthermore, the courts have been consistently reluctant to regard personal contributions, e.g. looking after children, to be sufficient[19] because there was no detriment suffered.

The law therefore remains problematic as regards trusts where the house is in the name of one person only. The leading case is still *Lloyds Bank v Rosset*, though *Geary v Rankine* [2012] EWCA Civ 555 has recently confirmed the application of the *Kernott* principles to sole ownership cases. The extent to which this is so is nevertheless problematic because precisely what conduct is sufficient to imply a common intention remains unclear.

Accordingly, if we apply the *Stack v Dowden* judgment to sole ownership cases, then it would be reasonable to look at the whole course of dealing between the parties in order to ascertain whether it is possible to infer a common intention as to each party's interest. The problem then becomes a question of what is sufficient to imply a common intention. Is a common intention to be decided with reference to property-related contributions, or can it include other contributions? Does it relate solely to the whole course of financial dealing, or does it relate to the relationship in its entirety? Can contributions to the relationship be regarded as giving rise to a common intention regarding the acquisition of a share in the land? Accordingly, the law is unlikely to be clarified until the Supreme Court deals specifically with a case where a trust is alleged, where the beneficiary is not also a legal owner of the land, there has been no agreement between the parties, and there has been no contribution that is obviously referable to the purchase price.

Establishing a constructive trust of the family home

Figure 14.2 provides a flowchart that can be used to decide validity.

The inquisitive reader is likely to question the fairness of imposing such precisely delineated requirements for a constructive trust of the family home, while the broader concept of a constructive trust is far more flexible – as shall be demonstrated in Chapter 22. In essence however, the principal question the court asks itself is 'Does the person that the claimant claims is a trustee know that he or she does not own the property for his or her own benefit?' Where a person has acted dishonestly (the thief), this knowledge is easily shown. Where a person has acted, knowing that they are in a position of trust (the company director, the seller of land), again, constructive trusteeship is again easy to show. However, where a person does not appear to know that they do not own the property for their own benefit (such as the testator who wishes to revoke a mutual will, or the owner of land), then the law must consider how their knowledge might be demonstrated. In the case of mutual wills and constructive trusts of the family

[18] *Springette v Defoe* [1992] 2 FLR 388.
[19] *Coombes v Smith* [1986] 1 WLR 808.

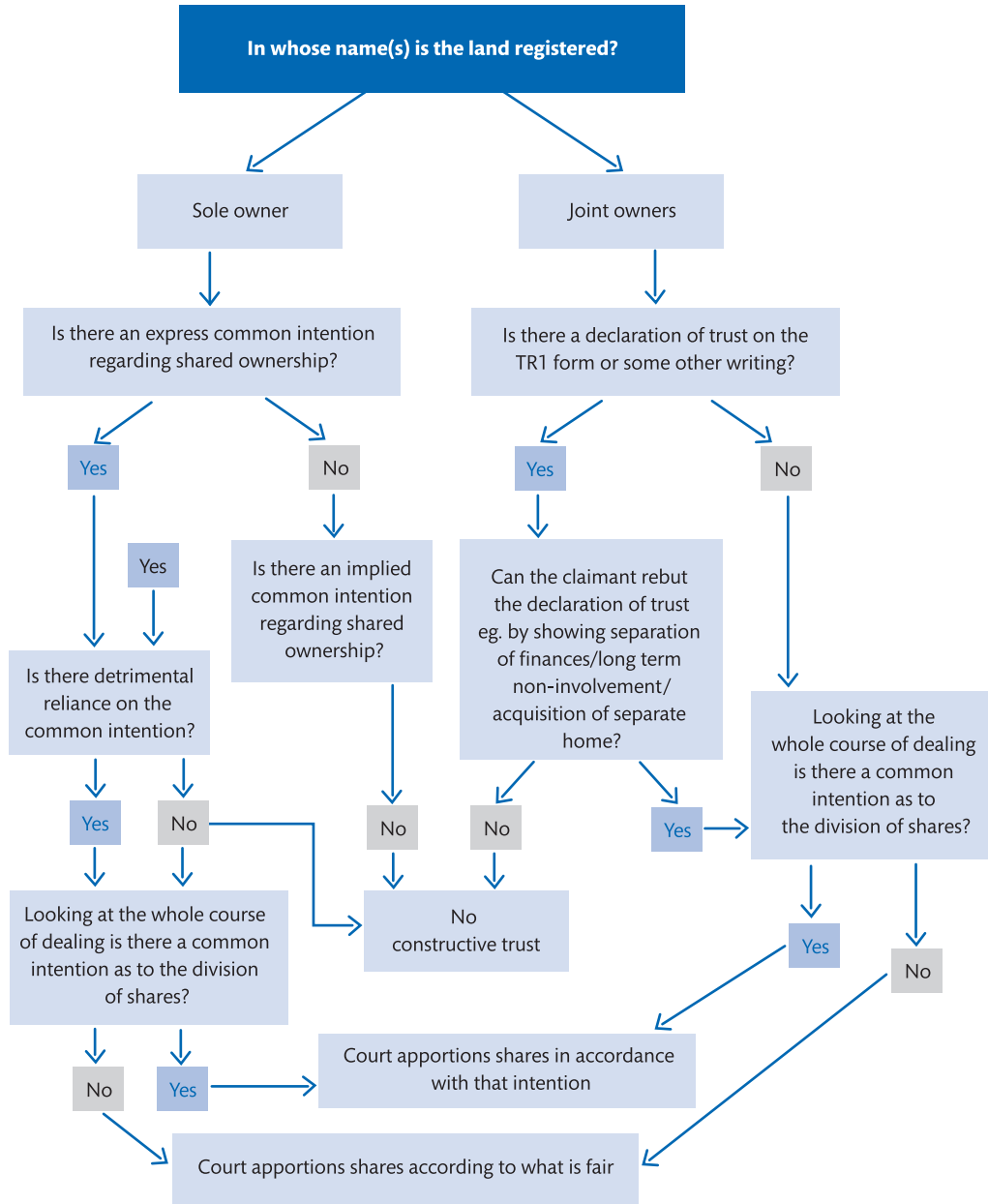

Figure 14.2 A flowchart for deciding validity

home alike, knowledge is derived from the defendant's express agreement through discussion or implied agreement through conduct that, as MacKinnon LJ explained in *Shirlaw v Southern Foundries* [1939] 2 KB 206 at p.227 is 'so obvious that it goes without saying; so that, if, while the parties were making their bargain, an officious bystander were to suggest some express provision for it in their agreement, they would testily suppress him with a common "Oh, of course!"'.

This is an area of law that has generated – and continues to attract – a great deal of academic debate and interest in cases being pursued through the courts system. On the

one hand, there are those who argue that a person should not be entitled to receive that to which they have made no contribution, especially where the defendant has not given them any expectation of an entitlement. On the other hand, there are those who argue that cohabitation is a joint venture, and that therefore all the assets of that venture should be shared. The difficulty then becomes where one should draw the line – should short-term cohabitation allow the claimant an equal share of the defendant's house, especially where the claimant is capable of earning money for themselves and is not regarded as depending on the cohabitant for support. Until a case comes before the courts therefore where the courts delineate the line between conduct sufficient to give rise to a common intention and conduct that is insufficient, as Lord Bridge purported to do in *Lloyds Bank v Rosset*, it would appear that the law on this area is likely to remain unclear. Nevertheless is it a fascinating area for research and study.

Because the resulting and constructive trust is not confined to the family home, the more remedial uses of these types of trust, as well as proprietary estoppel will be considered further later (in Chapter 22). However, the court's approaches in other contexts are less rigid than is encountered in relation to the family home.

Chapter summary

This chapter may be useful for assignments and assessments on:

- Trusts of land
- Implied trusts
- Family trusts
- Trusts of the family home.

Further reading

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Yip, M. (2012) 'The rules applying to unmarried cohabitants' family home' *Conveyancer and Property Lawyer* 159.

15

Succession

Chapter outline

This chapter will cover:

- Intestacy
- Wills
- Secret and half secret trusts
- Mutual wills.

Introduction

A trust is necessary where a person dies because a deceased person can no longer own assets, and the law becomes involved in order to distribute the deceased person's assets to the persons entitled to inherit either under the terms of the deceased's will, or in accordance with the rules of intestacy. It is a fascinating area of the law, as is demonstrated by the frequency with which the terms of a will, or the absence of a will, feature in the plots of novels, television programmes (particularly murder mysteries) and films. In the following chapter extract from Jane Austen's *Sense and Sensibility*, Mr Dashwood's estate is left to his son from his first marriage. The novel's main characters are therefore reduced to a state of the comparative poverty that provides the catalyst for the rest of the novel.

EXTRACT

Austen, J. (1811) *Sense and Sensibility*, Chapter 1

THE family of Dashwood had been long settled in Sussex. Their estate was large, and their residence was at Norland Park, in the centre of their property, where, for many generations, they had lived in so respectable a manner, as to engage the general good opinion of their surrounding acquaintance. The last owner but one, of this estate, was a single man, who lived to a very advanced age, and who, for many years of his life, had a constant companion and housekeeper in his sister. But her death, which happened ten years before his own, produced a great alteration in his home; for, to supply her loss, he invited and received into his house the family of his nephew Mr. Henry Dashwood, the legal inheritor of the Norland estate, and the person to whom he intended to bequeath it. In the society of his nephew and niece, and their children, the old Gentleman's days were comfortably spent. His attachment to them all increased. The constant attention of Mr. and Mrs. Henry Dashwood to his wishes, which proceeded, not merely from interest, but from goodness of heart, gave him every degree of solid comfort which his age could receive; and the cheerfulness of the children added a relish to his existence.

By a former marriage, Mr. Henry Dashwood had one son: by his present Lady, three daughters. The son, a steady respectable young man, was amply provided for by the fortune of his mother, which had been large, and half of which devolved on him on his coming of age. By his own marriage, likewise, which happened soon afterwards, he added to his wealth. His wife had something considerable at present, and something still more to expect hereafter from her mother, her only surviving parent, who had much to give. To him, therefore, the succession to the Norland estate was not so really important as to his sisters; for their fortune, independent of what might arise to them from their father's inheriting that property, could be but small. Their mother had nothing, and their father only seven thousand pounds in his own disposal; for the remaining moiety of his first wife's fortune was also secured to her child, and he had only a life interest in it.

The old Gentleman died; his will was read, and like almost every other will, gave as much disappointment as pleasure. He was neither so unjust, nor so ungrateful, as to leave his estate from his nephew;-but he left it to him on such terms as destroyed half the value of the bequest. Mr. Dashwood had wished for it more for the sake of his wife and daughters than for himself or his son: but to his son, and his son's son, a child of four years old, it was secured, in such a way, as to leave to himself no power of providing for those who were most dear to him, and who most needed a provision, by any division of the estate, or by any sale of its valuable woods. The whole was tied up for the benefit of this child, who, in occasional visits with his father and mother at Norland, had so far gained on the affection of his uncle, by such attractions as are by

no means unusual in children of two or three years old; an imperfect articulation, an earnest desire of having his own way, many cunning tricks, and a great deal of noise, as to outweigh all the value of all the attention which, for years, he had received from his niece and her daughters. He meant not to be unkind however, and, as a mark of his affection for the three girls, he left them a thousand pounds a-piece.

Mr. Dashwood's disappointment was, at first, severe; but his temper was cheerful and sanguine, and he might reasonably hope to live many years, and by living economically, lay by a considerable sum from the produce of an estate already large, and capable of almost immediate improvement. But the fortune, which had been so tardy in coming, was his only one twelvemonth. He survived his uncle no longer; and ten thousand pounds, including the late legacies, was all that remained for his widow and daughters.

His son was sent for, as soon as his danger was known, and to him Mr. Dashwood recommended, with all the strength and urgency which illness could command, the interest of his mother-in-law and sisters.

Mr. John Dashwood had not the strong feelings of the rest of the family; but he was affected by a recommendation of such a nature at such a time, and he promised to do every thing in his power to make them comfortable. His father was rendered easy by such an assurance, and Mr. John Dashwood had then leisure to consider how much there might prudently be in his power to do for them.

He was not an ill-disposed young man, unless to be rather cold hearted, and rather selfish, is to be ill-disposed: but he was, in general, well respected; for he conducted himself with propriety in the discharge of his ordinary duties. Had he married a more amiable woman, he might have been made still more respectable than he was: he might even have been made amiable himself; for he was very young when he married, arid very fond of his wife. But Mrs. John Dashwood was a strong caricature of himself; more narrow-minded and selfish.

When he gave his promise to his father, he meditated within himself to increase the fortunes of his sisters by the present of a thousand pounds a-piece. He then really thought himself self equal to it. The prospect of four thousand a year, in addition to his present income, besides the remaining half of his own mother's fortune, warmed his heart, and made him feel capable of generosity. 'Yes, he would give them three thousand pounds: it would be liberal and handsome! It would be enough to make them completely easy. Three thousand pounds! he could spare so considerable a sum with little inconvenience.' He thought of it all day long, and for many days successively, and he did not repent.

No sooner was his father's funeral over, than Mrs. John Dashwood, without sending any notice of her intention to her mother-in-law, arrived with her child and their attendants. No one could dispute her right to come; the house was her husband's from the moment of his father's decease; cease; but the indelicacy of her conduct was so much the greater, and, to a woman in Mrs. Dashwood's situation, with only common feelings, must have been highly unpleasing; — but in her mind there was a sense of honour so keen, a generosity so romantic, that any offence of the kind, by whomsoever given or received, was to her a source of immoveable disgust. Mrs. John Dashwood had never been a favourite with any of her husband's family; but she had had no opportunity, till the present, of shewing them with how little attention to the comfort of other people she could act when occasion required it.

So acutely did Mrs. Dashwood feel this ungracious behaviour, and so earnestly did she despise her daughter-in-law for it, that, on the arrival of the latter, she would have quitted the house for ever, had not the entreaty of her eldest girl induced her first to reflect on the propriety of going, and her own tender love for all her three children determined her afterwards to stay, and for their sakes avoid a breach with their brother.

Although some institutions offer succession as a discrete module, in many others it may be an element of the equity and trusts course, or an aspect that may be covered in a more generalised way, such as in the context of coursework that addresses the formalities required in the creation of a valid trust. Accordingly, this chapter aims to give an outline of some of the main aspects of the law of succession, while providing guidelines for further reading for those who wish to study the subject more extensively.

Intestacy

Intestacy occurs where a person dies without having made a valid will. The Law Society estimates that two thirds of people die without ever having made a will. However, intestacy may also arise where a will has been made but it is found to be invalid (such as where it has not been signed and witnessed in the manner required by the law), or where a valid will has been made, but some of the legacies contained therein are invalid, such as where a named beneficiary predeceases the testator, with the result that the gift fails because of a lack of certainty of objects. Where a person dies wholly or partially intestate, the law presumes that the deceased's intention would have been for his or her estate to pass to their immediate family. Accordingly, the Administration of Estates Act 1925,[1] s.46 provides a formula for identifying the deceased's family, and distributing the estate between them.

On death, the deceased's estate will pass to his or her personal representatives.[2] Where there is a partially valid will the personal representatives will be the person or persons named as the executor. Where there is no valid will, a person (often but not necessarily a family member) will apply to become the administrator of the deceased's estate. The personal representative's obligation is to liquidate the deceased's assets, pay off any outstanding debts, and then distribute the estate according to the formula contained in s.46.

EXTRACT

Administration of Estates Act 1925, s.46

46 Succession to real and personal estate on intestacy

(1) The residuary estate of an intestate shall be distributed in the manner or be held on the trusts mentioned in this section, namely:-

[(i) If the intestate leaves a [spouse or civil partner], then in accordance with the following Table:

TABLE

If the intestate-	
(1) leaves-	the residuary estate shall be held in trust for the surviving [spouse or civil partner] absolutely.
(a) no issue, and	
(b) no parent, or brother or sister of the whole blood, or issue of a brother or sister of the whole blood	

[1] (1925 c.23).

[2] Administration of Estates Act 1925, s.33.

(2) leaves issue (whether or not persons mentioned in sub-paragraph (b) above also survive)	the surviving [spouse or civil partner] shall take the personal chattels absolutely and, in addition, the residuary estate of the intestate (other than the personal chattels) shall stand charged with the payment of a [fixed net sum], free of death duties and costs, to the surviving [spouse or civil partner] with interest thereon from the date of the death . . . [at such rate as the Lord Chancellor may specify by order] until paid or appropriated, and, subject to providing for that sum and the interest thereon, the residuary estate (other than the personal chattels) shall be held- (a) as to one half upon trust for the surviving [spouse or civil partner] during his or her life, and, subject to such life interest, on the statutory trusts for the issue of the intestate, and (b) as to the other half, on the statutory trusts for the issue of the intestate.
(3) leaves one or more of the following, that is to say, a parent, a brother or sister of the whole blood, or issue of a brother or sister of the whole blood, but leaves no issue	the surviving [spouse or civil partner] shall take the personal chattels absolutely and, in addition, the residuary estate of the intestate (other than the personal chattels) shall stand charged with the payment of a [fixed net sum], free of death duties and costs, to the surviving [spouse or civil partner] with interest thereon from the date of the death . . . [at such rate as the Lord Chancellor may specify by order] until paid or appropriated, and, subject to providing for that sum and the interest thereon, the residuary estate (other than the personal chattels) shall be held- (a) as to one half in trust for the surviving [spouse or civil partner] absolutely, and (b) as to the other half- (i) where the intestate leaves one parent or both parents (whether or not brothers or sisters of the intestate or their issue also survive) in trust for the parent absolutely or, as the case may be, for the two parents in equal shares absolutely (ii) where the intestate leaves no parent, on the statutory trusts for the brothers and sisters of the whole blood of the intestate.]

[The fixed net sums referred to in paragraphs (2) and (3) of this Table shall be of the amounts provided by or under section 1 of the Family Provision Act 1966]

(ii) If the intestate leaves issue but no [spouse or civil partner], the residuary estate of the intestate shall be held on the statutory trusts for the issue of the intestate;

(iii) If the intestate leaves [no [spouse or civil partner] and] no issue but both parents, then . . . the residuary estate of the intestate shall be held in trust for the father and mother in equal shares absolutely;

(iv) If the intestate leaves [no [spouse or civil partner] and] no issue but one parent, then . . . the residuary estate of the intestate shall be held in trust for the surviving father or mother absolutely;

(v) If the intestate leaves no [[spouse or civil partner] and no issue and no] parent, then . . . the residuary estate of the intestate shall be held in trust for the following persons living at the death of the intestate, and in the following order and manner, namely:-

First, on the statutory trusts for the brothers and sisters of the whole blood of the intestate; but if no person takes an absolutely vested interest under such trusts; then

Secondly, on the statutory trusts for the brothers and sisters of the half blood of the intestate; but if no person takes an absolutely vested interest under such trusts; then

Thirdly, for the grandparents of the intestate and, if more than one survive the intestate, in equal shares; but if there is no member of this class; then

Fourthly, on the statutory trusts for the uncles and aunts of the intestate (being brothers or sisters of the whole blood of a parent of the intestate); but if no person takes an absolutely vested interest under such trusts; then

Fifthly, on the statutory trusts for the uncles and aunts of the intestate (being brothers or sisters of the half blood of a parent of the intestate) . . .

(vi) In default of any person taking an absolute interest under the foregoing provisions, the residuary estate of the intestate shall belong to the Crown or to the Duchy of Lancaster or to the Duke of Cornwall for the time being, as the case may be, as bona vacantia, and in lieu of any right to escheat.

The Crown or the said Duchy or the said Duke may (without prejudice to the powers reserved by section nine of the Civil List Act 1910, or any other powers), out of the whole or any part of the property devolving on them respectively, provide, in accordance with the existing practice, for dependents, whether kindred or not, of the intestate, and other persons for whom the intestate might reasonably have been expected to make provision.

[(1A) The power to make orders under subsection (1) above shall be exercisable by statutory instrument subject to annulment in pursuance of a resolution of either House of Parliament; and any such order may be varied or revoked by a subsequent order made under the power.]

(2) A husband and wife shall for all purposes of distribution or division under the foregoing provisions of this section be treated as two persons.

[(2A) Where the intestate's [spouse or civil partner] survived the intestate but died before the end of the period of 28 days beginning with the day on which the intestate died, this section shall have effect as respects the intestate as if the [spouse or civil partner] had not survived the intestate.]

(3) [Where the intestate and the intestate's [spouse or civil partner] have died in circumstances rendering it uncertain which of them survived the other and the intestate's [spouse or civil partner] is by virtue of section one hundred and eighty-four of the Law of Property Act 1925, deemed to have survived the intestate, this section shall, nevertheless, have effect as respects the intestate as if the [spouse or civil partner] had not survived the intestate.

(4) The interest payable on [the fixed net sum] payable to a surviving [spouse or civil partner] shall be primarily payable out of income.]

What this section demonstrates is that the primary beneficiary in intestacy will be the deceased's spouse or civil partner. If a person dies leaving a spouse or civil partner and no other relatives, then the spouse will inherit the residue of the estate in its entirety after all debts have been repaid. Furthermore, where there are other relatives who survive the deceased, again it will be the spouse or civil partner who will inherit the vast majority of the deceased's estate. Indeed, where the estate is comparatively small, it is likely that once the spouse or civil partner has received his or her entitlement, there will be nothing left of the residue for any other family members.

However, with larger estates, once the spouse or civil partner has received their entitlement, the personal representatives will be able to distribute the remainder to other family members. The distribution of the estate will depend upon whether or not the deceased had children. Where the deceased had children, the formula for the distribution of the estate will occur thus. The spouse or civil partner is entitled to inherit a statutory fixed sum of £250,000[3] (or any amount up to that limit where the estate is smaller) with interest accruing from the date of the deceased's death, the deceased's personal chattels as defined in s.55(1)(x) of the Administration of Estates Act 1925, and a life interest over 50 per cent of the remainder. The rest of the estate, namely the interest in remainder after the death of the spouse or civil partner, and the remaining 50 per cent of the residue will be divided equally between any children of the deceased who reach the age of 18, or marry before that age.

SCENARIO 1

Alf dies. After his debts have been paid, his estate is worth £300,000. His wife Beth will inherit £250,000 plus Alf's personal chattels. This leaves £50,000. Beth will receive a life interest over 50 per cent of this sum i.e. a life interest over £25,000. Alf's son Christopher and Alf's daughter Diana will receive an equal share of the residue (£12,500 each). On Beth's death, they will receive the remainder of the sum of Beth's life interest, again in equal shares.

On the other hand, if a person dies leaving no children, but had a spouse or civil partner and parents or full-blood siblings, then the estate will be distributed thus. As with the situation described above where a person dies leaving a spouse and children, the primary beneficiary will be the deceased's spouse or civil partner. Again the spouse or civil partner will inherit the personal chattels as defined in s.55(1)(x) Administration of Estates Act 1925, along with a statutory legacy of up to £450,000[4] with interest from the date of death. The spouse or civil partner will also acquire an absolute interest over 50 per cent of the residue, with the remaining 50 per cent being divided between the deceased's parents if they are still living, or if the parents have predeceased the deceased, between any full-blood siblings, i.e. siblings who share both parents with the deceased.

Where a person dies without leaving a spouse or civil partner, the estate will be divided equally between all those who fall within the first eligible category of beneficiaries identified in the Administration of Estates Act 1925, s.46(1)(ii)–(vi), namely children, parents, full siblings, half siblings, grandparents, full uncles or aunts, then half uncles or aunts. Therefore if a person dies leaving no spouse or civil partner, his or her estate will be divided equally between any children, and remoter relatives will not inherit. If there

[3] Family Provision (Intestate Succession) Order 2009 (SI 2009 No 135), art.2.
[4] Ibid.

are no parents, then the estate will pass to the deceased's parents, and again, any remoter relatives will not be entitled to inherit.

Caveats to the rules

A number of caveats exist however in the application of these rules.

Firstly, in order to inherit under the rules on intestacy, it is necessary for the beneficiary to survive the deceased by at least 28 days.[5] Accordingly, if the survivor dies shortly after the deceased intestate, they will not inherit.

Secondly, the law permits any issue of an eligible beneficiary to inherit in their parent's place if the parent beneficiary has died. Accordingly, where the deceased's children would be eligible to inherit under the intestacy rules, but they themselves have died, the children's children will inherit the share their parent would have been entitled to receive.

SCENARIO 2

Alf dies. He is survived by his two daughters, Belinda and Caroline, and his two grandsons David and Edmund, who are the sons of Alf's son Fred, who died in 1998. The estate will be divided into three equal shares, one portion going to Belinda, one portion going to Caroline, and the third portion (the share to which Fred would have been entitled had he survived) being divided equally between David and Edmund. Any children of Belinda and Caroline could not inherit Alf's estate however, because their mother survives the deceased and is therefore able to inherit in her own right.

The third caveat is that any beneficiaries must reach the age of 18 or marry before that age if they are to inherit. Therefore if a person dies leaving young children, they will not be able to inherit until they reach the age of majority, or marry.

These caveats give rise to the situation where the personal representatives may not know immediately how the deceased's estate ought to be distributed. Accordingly, it will be necessary for them to fulfil the function of trusteeship and invest the estate until such time as it can be distributed. The obligations of duty of care and trustee investments (discussed in Chapter 11) will therefore need to be considered in this situation.

SCENARIO 3

Alf dies. He is survived by his spouse Beth, and his son Charles, who is 10 years old. Although it is clear that Beth will inherit a large part of the estate, Charles's apparent inheritance will need to be invested until his 18th birthday or earlier marriage. It is possible however that Charles may die during this period, and the trustees will have to consider whether other, remoter relatives (parents and full-blood siblings of Alf's) may inherit, and also to increase the share of the estate to which Beth is entitled. If Alf's parents are dead, then it is possible that any siblings, or in the absence of surviving siblings, nephews or nieces, may be under the age of 18, and thus the estate will have to be invested for a further period until they reach an age when they are able to inherit. Even then, it is possible that those beneficiaries may die before they are able to inherit the estate, and therefore the personal representatives will transfer the residue in its entirety to Beth.

[5] Administration of Estates Act 1925, s.46(2A).

If the application of the intestacy rules result in a situation where no eligible beneficiary may inherit, the estate will pass to the Crown.

Wills

For many however, this formulaic distribution of an estate may be regarded as undesirable. An individual may consider for example that the situation where the primary beneficiary is their spouse or civil partner makes insufficient provision for children. Others may consider that the presumption of an equal distribution within a class of beneficiaries will fail to take into account any inequality in individuals' needs and circumstances. Many potentially deserving groups of people have no entitlement under the intestacy rules – cohabitants and those brought up as children of the family (a spouse or cohabitant's children from a previous relationship for example) have no entitlement, and the law of intestacy makes no provision for friends or causes viewed as being worthy. Accordingly, the law of wills permits a person to write a will that permits their estate to be distributed according to their own wishes. A will may be used in order to specify funeral arrangements and to give directions concerning the guardianship of children. A will is ambulatory in its effect until the testator dies. This means that the trust is not complete until the death of the testator, and therefore the testator may revoke or change his or her will once it has been made. It also means that unspecific trust property or beneficiaries may change between the date of writing and the date of death.

For example, if John writes a will in 2013 leaving his money to his children, by the time of his death in 2020, he may well have more (or less) money than he did when the will was written, and the number of children may have increased or decreased since writing the will. However, the will shall dispose of the money John owned at the time of his death by distributing it to all the children who survive him.

The law relating to wills is contained in the Wills Act 1837,[6] although the wording and the provisions of this Act have been amended since the Act was originally passed. Different rules apply in relation to wills made by people serving in the armed forces. However, the formalities applicable regarding these types of wills are beyond the scope of this book.

Capacity

Section 7 of the Wills Act requires that a testator has the necessary capacity to write a valid will. A testator must be over the age of 18 years of age to write a valid will. However, a further requirement is that the testator has the required capacity to write a valid will, with capacity being defined as being of sound mind, memory and understanding. Nevertheless, the extent of the capacity required depends on the complexity of the will and its contents. Therefore a greater degree of understanding will be required in order to ensure that a very complex will is valid than will be the case where the will is relatively uncomplicated. The issues to be considered when deciding upon testamentary capacity are explained by Cockburn CJ in the case of *Banks v Goodfellow* (1870) LR 5 QB 549.

[6] (1837 c.26).

EXTRACT

Banks v Goodfellow (1870) LR 5 QB 549

Case facts

The testator was a person who suffered from delusions, and had at one time in the past been detained in an asylum as a lunatic. The evidence presented to the court was contradictory on the question of whether he could manage his own affairs. The issue for the court therefore was whether he was able to manage his own affairs.

Sir Alexander Cockburn CJ (at p.564)

It is essential to the exercise of such a power that a testator shall understand the nature of the act and its effects; shall understand the extent of the property of which he is disposing; shall be able to comprehend end appreciate the claims to which he ought to give effect; and with a view to the latter object that no disorder of the mind shall poison his affections, pervert his sense of right, or prevent the exercise of his natural faculties; that no insane delusion shall influence his will on disposing of his property, and bring about a disposal of it which would not have been made otherwise.

Outcome

Having regard to these considerations therefore, the testator did have the required capacity to write a will. Despite the delusions from which he had been suffering he understood the purpose of a will, the extent of his estate and an awareness of who he ought to consider benefiting.

Validity

A will shall only be valid if it complies with the requirements of s.9 Wills Act 1837. Section 9 requires wills to be in writing and signed by the testator, with the signature being intended to give effect to the will. The signature must either be made or acknowledged in the presence of two witnesses, and the witness must attest and sign or acknowledge his or her signature in the presence of the testator.

EXTRACT

Wills Act, s.9

9 Signing and attestation of wills

No will shall be valid unless-

(a) it is in writing, and signed by the testator, or by some other person in his presence and by his direction; and

(b) it appears that the testator intended by his signature to give effect to the will; and

(c) the signature is made or acknowledged by the testator in the presence of two or more witnesses present at the same time; and

(d) each witness either-

  (i) attests and signs the will; or

  (ii) acknowledges his signature,

in the presence of the testator (but not necessarily in the presence of any other witness), but no form of attestation shall be necessary.]

The courts have adopted a very broad approach to some of these provisions. Writing for example is very broadly defined. The courts have accepted that a broad range of media and implements may be used in order to write a will, with the cases of *Re Barnes, Hodson v Barnes*[7] and *Re Slavinskyj's Estate*[8] perhaps representing the most unusual examples of what is acceptable as writing. In the former case, the will was written on an eggshell, while the latter case concerned a will written on a wall. The courts also accept that a will need not be written in a language that may be used by a party in court proceedings. In addition to wills written in English or Welsh, the courts have accepted that wills written in bad Ukrainian[9] and wills written in the code used by a jeweller in the course of his business[10] have all been regarded as valid forms of writing. The courts' approach therefore appears to be to accept that anything that is a written manifestation of the testator's intentions concerning the disposition of his or her estate on death may be regarded as a will.

The courts have also accepted that a signature does not necessarily mean a full signature, and that it can include any mark or marks intended to represent a signature, from initials[11] or a partial signature[12] to a thumb print[13] or a stamp[14], that have all been regarded as being sufficient. The emphasis is on whether the testator's actions were intended to give effect to the will. Therefore if what was done is interpreted as having been in order to execute the will, the act of signature will be regarded as valid. A leading case on this point is the case of *In the Goods of Chalcraft*.[15]

EXTRACT

In the Goods of Chalcraft [1948] P 222

Case facts

This case concerned a death bed will, where the testatrix was extremely frail and in considerable pain. The will she had drafted was given to her to sign, but she was only able to complete a partial signature. The will was therefore signed E. Chal, rather than E. Chalcraft. Shortly afterwards, the testatrix became unconscious and died.

Judgment

I come to the next point, whether what the deceased wrote can be accepted as her signature within the provisions of the Wills Act, 1837. As I have said, there is no question of it being acknowledged as her mark. Reliance was placed by counsel for the defendants on three cases in relation to this point. He referred, first, to *In the Goods of Maddock*. That was a case where the signature in question was that of a witness, not of a testator, the particular witness being old and infirm. As a result he was unable to complete his signature legibly, and desisted having only written a part of his christian name, and no surname at all. It was held that, in those circumstances, that was not a proper attestation of the will.

The next case relied on by the defendants was *In the Goods of Blewitt*. The question there was whether initials placed alongside certain interlineations in a will were acceptable as a signature.

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[7] (1926) 43 TLR 71.
[8] (1989) 53 SASR 221.
[9] *Re Slavinskyj's Estate* (1989) 53 SASR 221.
[10] *Kell v Charmer* (1856) 23 BEAV. 196.
[11] *Re Savory* (1851) 15 Jur 1042.
[12] *Re Chalcraft, Chalcraft v Giles* [1948] P 222.
[13] *Re Finn* (1935) 105 LJP 36.
[14] *Jenkins v Gaisford and Thring, Re Jenkins* (1863) 3 Sw & Tr 93.
[15] *Re Chalcraft, Chalcraft v Giles* [1948] P 222.

It was held that they were. In the course of the learned President's judgment in that case he cited the language of members of the House of Lords in the earlier case of *Hindmarsh v. Charlton* [[1861–73] All ER Rep 186], which, he said, seems 'equally applicable to the testator's signature as to the witnesses' subscription.' Then, quoting from the Lord Chancellor in *Hindmarsh v. Charlton*, he goes on: 'I will lay down this as to my notion of the law: that to make a valid subscription of a witness there must either be the name or some mark which is intended to represent the name.' In the same case Lord Chelmsford says: 'The subscription must mean such a signature as is descriptive of the witness, whether by a mark or by initials, or by writing a name in full.' What is said on behalf of the defendants in this case is that here you have not any of those three things; this is not a case of a mark, it is not a case of initials, and it is not a case of writing the name in full. Instead of that it is the initial followed by half the surname.

The third case to which I was referred was an Irish case, *In the Goods of Kieran, decd* [[1933] IR 222]. That was a case in which the facts are much more similar to those of the present case. It was a case of a testator who was in bed very ill, and who tried to write his name but did not succeed in doing more than write two more or less indecipherable initials. The similarity with this case, ceases after that, because in that case a solicitor was present, and he then asked the testator whether what the testator had written could be accepted as his mark, and the testator accepted what he had written as his mark; it was so endorsed on the will by the solicitor, and was so attested by the witnesses. In that case it was decided that although the mark did not take the usual form of a cross, nevertheless it was a mark acknowledged by the testator as his own in the presence of witnesses and, therefore, sufficient to amount to a signature under the Act. But the learned judge in that case does, I think, go a little wider than was necessary for the decision of the case in giving his reasons. I think it valuable to read the last few sentences of his judgment. He says this: 'What is the test that I am to apply? It is, in my opinion, whether I am satisfied that the two scrawls were placed there by the testator as a personal act or acknowledged as such by him, animo testandi, to verify the making of the will as his own act. If a testator cannot, or does not, sign his name, or place legible initials on the will, but, on the other band, places on it or acknowledges something upon it as his mark, in my opinion the court should not be concerned as to the particular character or shape of the mark. It may be the time-honoured cross, that has been referred to, or it may be some other character. I am satisfied on the evidence here that not only did the testator commence to make his signature animo testandi but continued in the same state of mind until the termination of the execution of his will, and accordingly I admit this will to probate.'

I find this a very difficult point to decide. What is said for the defendants is that if a testator sets out with the intention of signing his name, but never succeeds in completing a signature, and never develops any intention to execute the document in any other way, then it is not a signature. He can if he chooses, and if he forms the intention of doing so, execute the document by putting his initials on it; and he can, if he wishes to do so, and forms the intention of doing so, execute a document by making his mark and acknowledging his mark in the presence of witnesses. But what is said is that if he starts out with the intention of doing any one of these things, and never departs from that intention, but yet never completes that which he sets out to do, then there can in law be no execution of the document. *In the Goods of Maddock* [[1874–80] All ER Rep 367], if what was said about witnesses is to apply to testators, certainly seems to go a long way towards establishing that proposition. The Irish case to which I have referred does not help very much, partly because it did ultimately turn on the testator's acknowledgment of his mark, and partly because of the rather wider grounds on which the learned judge put his judgment in the last few sentences, which I have read. Indeed, if one took those last few sentences by themselves, it could be read as an authority to the contrary of what has been contended on behalf of the defendants. It seems to me that there must necessarily be some question of degree involved in this. I put in argument the case of the man who signs his name (a practice which we all know very well) by making the first few letters of his signature

fairly distinct, and the last few letters of his signature completely indecipherable. Supposing, for the sake of argument, in this case the deceased instead of stopping at the 'l' in 'Chalcraft' had followed it by a few, or even one, indecipherable line. What would be the effect then? Would that be a completed signature? It seems to me that one ought to give a broad interpretation to the words used by the Lord Chancellor in the case of *Hindmarsh v. Charlton* in the passage which I have read. There must either be the name or some mark which is intended to represent the name. It seems to me that I must have regard to all the facts of this case: the fact that this lady was in an extremely weak condition; that she was lying, if not quite on her back, very nearly on her back, in a position in which it must have been very difficult to write at all. I must ask myself the question whether on all the facts I can draw the inference that what she wrote was intended by her to be the best that she could do by way of writing her name. It seems to me that if I come to that conclusion, then I ought to accept this writing of 'E. Chal' as being in law the signature of the deceased. Bearing in mind all the circumstances of the case – the weakness of the deceased, the difficulty of writing in that position – I come to the conclusion that this mark 'E. Chal' on this document does amount, in all the circumstances, to a signature on the part of the deceased. I think *In the Goods of Maddock* is distinguishable, because in that case there was no question of writing any surname at all; the writing stopped short at a part only of the christian name. Here we have something a good deal better than that and, in all the circumstances, I am satisfied that I ought to accept it as the signature of the deceased.

Outcome

On this basis, the testatrix' will was found therefore to be valid.

However, if the signature was completed for some other purpose, such as preventing additional pages from being added to the document, the signature, although apparent on the face of the will shall not be regarded as valid for the purposes of validating the will.[16] Similarly, if the testator had not completed all that he had intended to do in order to give effect to the will, then the will shall not be valid. In the case of *Re Colling*[17] for example, the testator began to write his signature, but one of the witnesses was called out of the room before the act of signature could be completed. Accordingly only the partial signature appeared on the will, and because the testator had not completed all that he had intended, the will was held not to be valid.

EXTRACT

In the Goods of Dilkes (1874) LR 3 P & D 164

Case facts

The testatrix wrote a will that covered two sheets of paper. She signed both sheets, but the witnesses only signed the first page.

Sir J Hannen

If the holograph part of this document be taken as the will, there is no attested signature at the foot or end of it. The signature on the first page was made merely to authenticate what was written thereon, and it was intended to execute the will by the subsequent signature; but such intention was not formally carried out. The mark at the end was made as an execution of the will, but then it was not attested by the witnesses. I must reject the application.

[16] *In the Goods of Dilkes* (1874) LR 3 P & D 164.
[17] [1972] 3 All ER 729.

As an alternative to signature, a will may be signed by another person 'at the testator's direction and in his presence'. This may be necessary where the testator, owing to some illness or disability, is unable to make *any* mark on the document. However, as Borkowski explains, this seems unnecessarily broad in situations where the testator has the physical ability to put a mark on the will that represents a signature.[18] Nevertheless, it again suggests the courts' emphasis on interpreting s.9 as broadly as possible in order to give effect to the testator's wishes.

The signature must also be witnessed by two witnesses who are present at the same time, and they must sign or attest their signatures in the presence of the testator. The order of the signature is important. The testator must sign the will in the presence of the witnesses, and then the witnesses must sign in order to attest to the fact that they have witnessed the act of signature. Accordingly, the will is not valid if the witnesses sign the will before there has been anything for them to witness.

Presence (in the sense that the testator must sign in the presence of both the witnesses, and the witnesses must sign in the presence of the testator) has been interpreted as meaning more than physical presence, in that there is also a need for the witnesses to be aware of the event that is taking place. A 'line of sight' test has been promulgated,[19] with the result that physical presence is evaluated with reference to whether the witness(es) *could have* seen the act of signature had they been looking in the right direction at the right time. This creates a number of anomalies in the law. On the one hand, it means that a will is not valid if the circumstances of its execution are re-enacted in such a way that it appears that it would have been impossible for the witness to see the act of signature (*Brown v Skirrow* – below). It also means that a will is not valid where the witness is unable actually to see the act of signature, but within the confines of a small space is fully aware that the act of signature is taking place.[20] However, a will is valid where it is not clear whether the witness saw the act of signature, but it appears that he or she could have done so had he or she chosen to look in the right direction at the appropriate time.[21]

EXTRACT

Brown v Skirrow [1902] P 3

Case facts

The testatrix took her will into a shop for signature. One witness saw the act of signature take place but the other witness – the shopkeeper's view – was impeded by another customer who was standing between him and the testatrix.

Gorell Barnes J

It appears that the testatrix prepared the second will herself and then took it to a shop, a photograph of which was produced with a variety of groceries and other things shewn therein,

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[18] Borkowski, A. (2000) 'Reforming Section 9 of the Wills Act' *Conveyancer and Property Lawyer* 31–42 at p.37.

[19] In *Causer v Causer* [1996] 3 All ER 256 Judge Colyer QC considers the authorities on the requirements of witnessing a will and concludes that none of them emphasise whether the act of signature WAS actually seen, merely that it COULD HAVE been seen from the witness' vantage point.

[20] *Tribe v Tribe* (1849) 1 Rob Eccl 775.

[21] *Shires v Glascock* (1685) 2 Salk 688.

and in particular two counters, one on the left and the other on the right hand side of the shop. The two witnesses, or people exceedingly like them, are shewn standing behind the respective counters. The testatrix appears to have proceeded straight to the left-hand counter, where Miss Jeffery was, and asked her to witness her will. She stood with her back towards the other counter, and behind her was a commercial traveller doing business with Mr. Read, the other witness in the case. It appears, as far as I understand the evidence, that the testatrix signed her name at the left-hand counter, over which Miss Jeffery was leaning, and then Miss Jeffery signed her name as it appears on the document. Up to this time Mr. Read had been engrossed with the commercial traveller, and had not the slightest idea of what was going on at the other counter. It is urged that, even if he were conscious that the testatrix was there, he did not see anything of the transaction at the other counter; he says so himself. In fact, he did not know, and had no opportunity of knowing, what was going on there. The witness, Miss Jeffery, having completed her signature, marched round the shop and asked Mr. Read to come from his counter and go round to where the testatrix still was, Miss Jeffery taking up the position which Mr. Read vacated. Mr. Read accordingly went round, and the testatrix said to him, 'This is my will.' Mr. Read then signed his name to the document. The question for me to determine is whether that was a good execution and attestation. It is not suggested that it was a good acknowledgment in the presence of the two witnesses, because, at the moment when she said to Mr. Read 'This is my will,' the first witness, Miss Jeffery, had already signed her name; and, according to the decided cases, the acknowledgment must be made in the presence of the two witnesses, who must afterwards attest it: see especially *Wyatt* v. *Berry* [[1893] P 5]. Mr. Priestley, however, contends that it was a good execution; but I fail to see how the testatrix's signature can be said to have been affixed to the document in the presence of Mr. Read, when, although he was in the shop, he had no idea and saw nothing of what was going on at the time, and, moreover, had no opportunity of seeing, there being, as I have said, another person in the shop between him and the testatrix. In some cases it would be most unfortunate that such a result should arise; but, happily, in the present instance it is not very serious, because the earlier will is very much to the same effect as the later one. The Wills Act is very precise, and must be applied with strictness.

Outcome

Accordingly, the will was found not to be valid.

An interesting issue that this case demonstrates about wills, and about the operation of the law more generally, is that the judgment was delivered on the basis of not what actually happened, but on the basis of how the scenario was reconstructed by the court. Had the customer or the shopkeeper been positioned slightly differently it is entirely possible that the court would have judged the case on the basis that the witness could have seen the act of signature had he looked in the appropriate direction at the correct time, and is therefore likely to have arrived at a different conclusion. The law of wills therefore raises a number of interesting questions concerning the law's contingent character. Perhaps if the situation that had come before the court had been presented and reconstructed slightly differently, or if the situation had been slightly different, the outcome – and the precedent – would have been different. Accordingly, when presenting an argument there may be considerable advantage in considering the material ways in which the current case may be distinguished from the relevant precedents.

Section 9 permits the signature either to be made or acknowledged by the testator in the presence of the witnesses. Accordingly, even though the witnesses do not see the act of signature itself the will may nevertheless be valid if it is acknowledged either expressly,

or by implication. In *Re Davies*[22] for example, gestures made by the testatrix in the context of the words she used were regarded as sufficient acknowledgement of her signature.

Once the testator has signed or acknowledged their signature, then the witnesses must attest and either sign the will or acknowledge their signature in the presence of the testator. However, each witness does not have to be in the presence of the other witness when they attest and sign or acknowledge their signature, although a prudent solicitor would be advised to ensure that each witness signs or acknowledges their signature in the presence of the other witness as well as the testator. Attestation means that the witness is confirming that they have witnessed the testator's act of signature or acknowledgement. Therefore in order for the will to be valid, the testator's signature must be made before that of the witnesses. Otherwise, there are no specific form of words that must be used in order for a will to be validly attested, although an attestation clause of some form is advised, in order to channel the witnesses minds to ensuring that their behaviour complies with the requirements of s.9.

Surprisingly perhaps, there are no statutory requirements regarding the capacity of witnesses, and therefore a child or a person who lacks capacity may be a valid witness to a will. Nevertheless, a witness who lacks the necessary capacity may be regarded as lacking the necessary mental element of 'presence' for the purposes of s.9. As Dr Lushington explains in *Hudson v Parker*,[23] presence must meant that '*the witnesses should see and be conscious of the act done and be able to prove it by their own evidence: if the witnesses are not to be mentally as well as bodily present, they might be asleep or intoxicated or of unsound mind*.' The prudent solicitor, and indeed the prudent testator or testatrix, should however have regard to the purpose of attestation, and the reason for requiring witnesses. The witnesses may be required in the future to testify as to the validity of the will both as regards the testator's capacity and that the formalities of section 9 have been complied with. It is therefore advisable that the testator chooses witnesses who are likely to be able to give credible evidence if called upon to testify.

The case of *Re Gibson*[24] indicates however that a blind person cannot ordinarily act as a witness to a will purely because the element of sight involved in terms of seeing the act of signature would not be present. This is problematic however, because a person who is blind is not prevented from making a valid will, and the fact that the blind testator would equally need to witness the witness's act of signature does not appear to have been regarded as problematic by the courts. Again, there is a sense that what the law becomes is contingent upon the cases that have come to be decided.

A further point to note in relation to the selection of witnesses is that although an executor, a creditor or a beneficiary, or the spouse or civil partner of such a person, may validly act as a witness to a will, s.15 Wills Act 1837 prevents them, or their spouse or civil partner from deriving any benefit under the will. Therefore, if the executor witnesses a will, he or she will not be able to benefit from any clause in the will that allows remuneration for the work undertaken. By the same principle, the spouse or civil partner of the executor cannot benefit from the will as a beneficiary, and the witnessing of a will by the spouse or civil partner of the executor will mean that the executor will not be able to benefit from a remuneration clause in the will. Similarly, a creditor or a beneficiary who witnesses a will cannot then benefit from a legacy in their favour contained in a will. As with the situation with executors, if the spouse or civil partner of a creditor or a beneficiary witnesses the will, the creditor or beneficiary cannot claim the legacy that purports to benefit them.

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[22] (1850) 2 Rob Eccl 337.
[23] (1844) 1 Rob Eccl 14 at p24.
[24] [1949] P 434.

Although the need for formalities is generally accepted as being important, as a way of preventing fraud and of ensuring that the testator's wishes are fulfilled, concerns have been expressed regarding their unintended consequences, and the situation whereby a strict adherence to the requirement of formality has led to the courts to act in a way that goes against the testator's wishes. Furthermore, it may be argued that some of the formalities were appropriate for 1837, but that they may not be as suitable in modern times.

Writing

Although it is generally conceded that there is a need to record the terms of a will in a permanent form, it is possible to argue that writing may not be the most appropriate mechanism. The requirement of writing in s.9 for example precludes wills made in other permanent forms such as recording. The advantages of recording a will may however be considerable, in that it may be easier to determine the testator's capacity, as well as enabling the testator to indicate specifically which items of property are to be given to which beneficiary.

Signature

The requirement of signature is generally regarded as being extremely important. However, Borkowski (below) advocates a stricter application of the rules regarding signature at the testator's direction, in that allowing a will to be signed by a person other than the testator provides greater opportunity for fraud, rather than mitigating it. Nevertheless, Borkowski concedes that a will would need to be signed by another person at the testator's direction in situations where the testator is physically incapable of doing so. His argument however is that this should be the only exception, and that otherwise the will ought to be signed by the testator in person.

EXTRACT

Borkowski, A. (2000) 'Reforming Section 9 of the Wills Act' *Conveyancer and Property Lawyer* 31

Section 9(a) allows 'some other person' to sign on behalf of the testator providing this is done in the presence and by the direction of the testator. The person signing can sign in his own name or that of the testator. The possibility that the testator's will can be signed by some person other than the testator is patently a worrying one: there is obvious potential for fraud and undue influence in such a case. These possibilities, especially the latter, may seem to be denied by the insistence on the testator's 'direction', but as that term too is not defined by section 9, nor clarified in the case law, they cannot be discounted.

What is the point of allowing a person to sign on the testator's behalf, given that the latter need only make a mark in order to sign? The original justification for this provision was to provide for the case of the illiterate testator, but the main purpose now must be to help the testator who cannot sign because of illness or disability (although he must be at least capable of giving 'direction'). This is entirely justifiable but, if that is the *raison d'être* for the rule, section 9 should make that clear. As it is, there would appear to be nothing to invalidate a will signed by some other person on behalf of a perfectly fit testator. Is it desirable to allow this? I think not, and it is difficult to envisage the circumstances in which such a possibility could be justified. It should be ended by amending section 9(a) so as to confine the signing of a will by an amanuensis to cases where the testator cannot sign his will by reason of illness or disability (which would include illiteracy). I would thus amend the relevant part of section 9(a) to read 'or by some other person in his presence and by his direction *where the testator is unable to sign the will because of illness or disability*'.

Witnessing

It is generally conceded that witnesses are extremely important in terms of ensuring the validity of a will. However, s.9 reveals inconsistencies in the law's expectations concerning the gravity of the role. For example, the fact that no requirements are imposed concerning the capacity of the witnesses means that the law does not adequately emphasise the need to ensure that the witnesses are capable of being called upon to testify should the will later be disputed. Borkowski also argues that the number of witnesses should be increased. Two witnesses could easily be so intimately connected as to be able to collude in their evidence – as may be the situation with 'the friendly couple next door'.[25] Insisting on three witnesses however would make it more likely that at least one of the witnesses has no connection with the others, and therefore may be a way of mitigating the risk that witnesses may collude in their evidence.

EXTRACT

Tilly, E. (2005) '*Sherrington v Sherrington*: lessons in the execution of wills' *Conveyancer and Property Lawyer* 306

To choose witnesses on the basis of their not surviving the testator completely flies in the face of the purposes of the formalities and hinders the evidence that can be obtained regarding the execution of the will after the testator has died. The testator is the only one who really knows what happens, but as his testimony is unavailable the witnesses take on an important role after his death. As such, witnesses should be selected on the basis of their competence to observe and participate in the execution ceremony and their ability to give evidence once the testator has died. In *Sherrington v Sherrington* [[2006] EWCA Civ 1784] this was not done. Although both survived the deceased, Mr Thakkar had only 'a very limited understanding of English' so he was not an ideal witness. The rather surreal situation occurred during the execution of the deceased's will whereby Mrs Butt had to translate for Mr Thakkar what he was being asked to do by the deceased.

Furthermore the presumption of due execution may act as a major stumbling block to those challenging the will where witness evidence is not available. If the witnesses in *Sherrington v Sherrington* had not been able to give evidence, then it would have been very difficult to rebut the presumption. On the contrary, the presumption would have been strengthened by the fact that the deceased was a solicitor, as Lightman J. indicated. The only intrinsic evidence that would have assisted the claimants in challenging the will, and raised their suspicions in the first place, would have been the unusual provisions and the surprising typographical errors. Neither of these would have been sufficient to prove lack of due execution, but instead the claimants would have had to rely solely upon the plea of lack of knowledge and approval, a plea which is even harder to prove. Without the witnesses it could not have been proved in *Sherrington v Sherrington*, let alone discovered, that the deceased did not acknowledge his signature before the attesting witnesses.

The purposes of the Wills Act formalities have been widely discussed, particularly by Gulliver and Tilson in 'Classification of Gratuitous Transfers' and in Professor J. H. Langbein's seminal article on the subject, 'Substantial Compliance with the Wills Act'. The purposes have been

[25] Borkowski, A. (2000) 'Reforming Section 9 of the Wills Act' *Conveyancer and Property Lawyer* 31 at p.39.

identified as: the ritual function, the evidential function, the channelling function and, finally, the protective function. The formalities, contained largely in s.9 of the Wills Act 1837, are designed to serve these functions.

The ritual and protective functions of the Wills Act formalities are relevant to the facts of *Sherrington v Sherrington*. The ritual function stresses that the formalities required to make a will should be such as to impress upon the testator the importance of what he is doing. It should not be so easy to make a will that it can be done flippantly. The testator must be made to think seriously about his testamentary dispositions and to realise the importance (financially and morally) of his actions through the solemnity of the execution ceremony. Furthermore the formalities must also serve a protective function; to protect the testator from fraud and undue influence and from making a will that does not reflect his genuine testamentary wishes.

In an execution ceremony 'lasting at most 5 minutes' it is hard to see how these functions can be served consistently with all testators. The execution of a will is a relatively simple process and the formalities can be carried out efficiently in five minutes. More often than not the will executed will be a genuine expression of the testator's testamentary intentions. However some testators require more protection than others, depending upon their vulnerability. A choice has to be made. The formalities may be strengthened to protect these more vulnerable testators but risk more wills failing to comply with the more stringent execution requirements. Alternatively the formalities may be left as they are, with the risk that they may fail to protect some testators.

ACTIVITY

What do you consider to be the advantages and disadvantages of s.9? Should s.9 be reformed?

Commentary

This type of question is a common format for an examination or essay question. One way to approach this essay is to begin by listing the advantages of s.9. Consider what s.9 seeks to achieve and why these formalities are important. The material in this chapter may provide you with some ideas, but you will also need to conduct further research. Try looking for books or journal articles where s.9 is discussed. What advantages do the authors suggest?

Then consider listing the disadvantages. Again this chapter has suggested some possible problems that arise with s.9, but these should only be treated as a starting point for your own research.

You may then want to begin writing the essay. One approach may be to address each subsection of s.9 in turn, and within that paragraph to outline both the advantages and then the disadvantages. One of your arguments may be that the formality of writing prevents fraud. You then need to explain how it does this – an essay requires you to convince your reader of your point of view, therefore it is imperative that you demonstrate how the argument you put forward is substantiated. You can then conclude whether or not the continued existence of the current law on each paragraph is merited.

You can then go on to consider the second part of the question, and address whether the law ought to be reformed. Your conclusions to the first part of the essay will inform the argument you present in the second part of the essay.

Revocation

After being made, a will may be revoked. The Wills Act 1837 envisages four ways in which a will may be validly revoked. These are: marriage or civil partnership (s.18); by another will or codicil (s.20); by some other writing (s.20); and by destruction (s.20). Marriage or civil partnership revokes a will because it is considered that marriage or civil partnership causes the testator to have different financial considerations and responsibilities. Other changes to one's family structure, such as divorce or the dissolution of a civil partnership, the death of one's spouse or civil partner, or the birth of children will not revoke an earlier will. However any will made before marriage or civil partnership will be revoked by marriage or civil partnership, with the result that the testator will have to write a new will if he or she wishes to continue to leave legacies to specific individuals (children from a previous relationship for example) or causes. One exception to s.18 is that a will made in contemplation of marriage or civil partnership will not be revoked by that marriage or civil partnership. The will must have been made in contemplation of marriage or civil partnership to a particular person, and there must be an intention that the marriage or civil partnership will not revoke the will.

The methods of voluntary revocation of a will contained in s.20 require that there must be an intention for the will to be revoked. It is presumed that an act that effects the revocation of a will is intentional, but this presumption may be rebutted by evidence to the contrary. For example, if the testator's will is inadvertently destroyed, then the will is not revoked because the destruction is not coupled with an intention to revoke.

In order for a will to be revoked by some later instrument, it is necessary for that later will or codicil,[26] or the document that revokes the earlier will without disposing of the testator's estate, to comply with the validity requirements of s.7 and s.9. The later will or codicil may expressly revoke earlier wills, or parts of earlier wills. Alternatively, a later will may impliedly revoke an earlier will, because its clauses are inconsistent with the earlier will. For example, if a later will disposes of the same property as the earlier will, then the later will shall be presumed to revoke the earlier will.

EXTRACT

Cadell and Another v Wilcocks and Others [1898] P 21

Case facts

The testatrix had been left money by her father, coupled with a power of appointment – a power to decide which of the testatrix's own children should receive that money on her death. In a will made in 1890 she gave the money to her daughter Gertrude. In 1894 she made another will, which made no reference to the power of appointment, and in 1895 she made a third will. Neither of the latter wills expressly revoked the earlier will. The question for the court to consider therefore was whether the power of appointment had been validly exercised under the testatrix's first will, or whether it had been revoked by her later wills.

[26] A codicil is a document that is similar in effect to a will but is used in order to make minor amendments to a will. For example, if Jane writes a will leaving specific items of jewellery to named beneficiaries, and then provides that the rest of the jewellery is to be given to her sister, Anne, a codicil may be a useful mechanism for conferring a further specific item of jewellery on another named beneficiary. More substantial amendments to a will should however be made by drafting a new will.

Sir F.H. Jeune

The question in this case is, which of three wills made respectively on April 26, 1890, July 5, 1894, and September 5, 1895, by the testatrix, Mrs. Lucy Biddulph, should be admitted to probate.

The father of the testatrix, Robert Bickerstaffe, left 16,000l. among his four daughters in equal shares for life, with power of appointment to each of them by will amongst her children, and, in default of appointment, to her children equally.

At the time of the will of 1890, the testatrix had two daughters, Anne, then married, and Gertrude, then a widow, and three sons, Middleton, Assheton, and Franc. By the will of 1890 the testatrix, after revoking all previous wills, gave her daughter Gertrude 'the sum of 4000l. absolutely for her sole use and benefit,' describing it as 'being the sum left to me by the will of my father the late Robert Bickerstaffe.'

. . . By her will of 1894 the testatrix bequeathed to her daughter Gertrude 'the sum of 4000l. for her own absolute use and benefit, and to dispose of as she may think fit.' She then gave 50l. to her steward, Finton McDonald, and the residue of her property to her children Franc and Gertrude equally, and appointed Franc Gertrude and Dr. Nevil Cadell executors.

Between the wills of 1894 and 1895, Franc, the son of the testatrix, and also the steward died. A letter of the testatrix containing her instructions for the will of 1895 was produced to me, but I do not think it material. By the will of 1895 the testatrix made a bequest to her daughter Gertrude in these terms: 'All the property real freehold or personal wheresoever situate of which I may die seised or possessed for her own absolute use and benefit and to dispose of as she may think fit,' and gave the same, in case of her daughter predeceasing her, to her daughter's husband, Dr. Nevil Cadell, and appointed her daughter and Dr. Cadell executrix and executor.

Neither the will of 1894, nor the will of 1895, contained any words of revocation; and it was not disputed before me, that neither the terms of the will of 1894, nor those of the will of 1895, were sufficient to effect a valid execution of the limited power of appointment vested in the testatrix.

I think that this case is governed by the familiar principle of law stated in *Williams on Executors*, 9th ed. p. 138, and approved by Lord Penzance in , that the mere fact of making a subsequent testamentary paper does not work a total revocation of the prior one, unless the latter expressly or in effect revoke the former, or the two be incapable of standing together, and if a subsequent testamentary paper, whether will or codicil, be partially inconsistent with one of earlier date, then such latter instrument will revoke the former as to those parts only where they are inconsistent.

In this case there was clearly no express revocation, in whole or in part, of the will of 1890 by either the will of 1894 or the will of 1895. I assent to Mr. Inderwick's contention that, had there been a general clause of revocation in either the will of 1894 or that of 1895, it would have revoked the whole will of 1890, including the execution of the power contained in it. The opinion indeed of the Delegates in the case of *Hughes v. Turner* [(1835) 40 ER 254], if correctly reported, would appear to be to the effect that a clause of revocation per se does not revoke the portion of an earlier will which has executed a power; and in *In the Goods of Merritt* [(1858) 4 Jur NS 1192] and in *In the Goods of Joys* [(1860) 4 Sw & Tr 214] Sir Cresswell Cresswell expressed a similar opinion. It might be considered doubtful whether the case of *Sotheran v. Dening* [(1881) 20 Ch D 99] in the Court of Appeal overruled those authorities, because weight

was given to the consideration, which arose in that case, that by virtue of the 27th section of the Wills Act a general bequest operated on the subject-matter of the power of appointment, and so strengthened the evidence in favour of an intention to revoke its previous execution. But in *In re Kingdon* [(1886) 32 Ch D 604] the question of revocation by a general revocatory clause arose simpliciter, there being no subsequent provision relating to the subject-matter of the power in question, and Kay J. clearly considered that he was justified by the authority of *Sotheran* v. *Dening* in holding that a will executing a power was revoked in toto by general words of revocation in a subsequent will. The effect of his decision is, I venture to think, that on this point of law common sense at last prevailed. I cannot understand why express words, revoking all previous wills, should be supposed to spare an execution of a power contained in one or more of them from the fate inflicted on all the rest of their contents. But, in the present instance, there are no express words to revoke the will of 1890. Next, is there anything in the wills of 1894 or 1895 inconsistent with the execution of the power in the will of 1890, or, in other words, is there anything that by implication effects a revocation of that execution? It is not necessary to consider whether, if the power of appointment in this case had been general and not, as it was, limited, the general bequests in the wills of 1894 and 1895 would have been not only, by virtue of the 27th section of the Wills Act, effectual to execute the power, but also sufficient to revoke a previous execution of it. It is, I think, clear that these general words of bequest, which do not execute the limited power, as the 27th section of the Wills Act has no application, cannot revoke or affect its previous execution. The wills of 1890 and 1895 can, therefore, stand together; and, subject to proof in common form, there should be probate of both of them. The will of 1894 I regard as revoked by that of 1895, as both wills profess to deal with the whole of the testatrix's own property.

Outcome

In this case, the will of 1895 revoked the will made in 1894 because the later will disposed of the same property as the earlier will. On the other hand, neither of the later wills revoked the earlier will as regards the legacy left by the testatrix's father.

Finally a will will be revoked by being destroyed. Section 20 Wills Act 1837 provides that the destruction of a will must be accompanied by an intention to revoke the will. Section 20 states:

> no will or codicil, or any part thereof, shall be revoked otherwise than as aforesaid, . . . or by the burning, tearing, or otherwise destroying the same by the testator, or by some person in his presence and by his direction, with the intention of revoking the same.

Therefore a will that is torn up in error by being mistaken for another piece of paper will not be revoked, because the destruction was not intended to effect the revocation. In order for a will to be destroyed there must be an act that either destroys a will or renders it invalid. Clearly therefore the complete destruction of a will shall revoke it. However, lesser acts may also suffice as revocation of a will. For example, in the case of *Hobbs v Knight* (1838) 1 Curt 769, the testator cut his signature off the bottom of the will, leaving the rest of it intact. Because this affected the validity of the will, it was deemed to have been a sufficient manifestation of the testator's intention to revoke his will.

EXTRACT

Hobbs v Knight (1838) 1 Curt 769

Case facts

In this case the testator had written a will, and had later cut the signature off the bottom of the document. The question for the court was whether the will had therefore been revoked in the manner envisaged by s.20.

Sir Herbert Jenner

[T]he next question is, does the cutting out of the signature of the testator, the rest of the paper remaining entire, amount to a revocation of the will? In order to determine the effect of this act (the excision of the name of the testator) we must consider what is necessary to create a valid will under the statute. The ninth section of the statute is to this effect, 'That no will shall be valid unless it shall be in writing and executed in manner hereinafter mentioned (that is to say), it shall be signed at the foot or end thereof by the testator, or by some other person in his presence and by his direction; and such signature shall be made or acknowledged by the testator, in the presence of two or more witnesses present at the same time, and such witnesses shall attest, and shall subscribe the will in the presence of the testator; but no form of attestation shall be necessary.' It appears, then, that the signature of the testator is necessary to the validity of a will; that no will is valid without it, so that it is not only a material part, but an essential part, without which a will cannot exist.

A will being so executed, the next question is, How is it to be revoked? The 20th section provides 'that no will or codicil, or any part thereof, shall be revoked, otherwise than as aforesaid' (that is, by marriage, under the 18th section) 'or by another will, &c,' which does not apply to this case, 'or by the burning, tearing, or otherwise destroying the same by the testator, or by some person in his presence, and by his direction, with the intention of revoking the same.' Assuming, then, that this act was done by the deceased, it must be taken to have been deliberately done; the effect of that act is now to be considered. The signature of the testator being, as I before said, an essential part of a will, it is difficult to comprehend when that which is essential to the existence of a thing is destroyed, how the thing itself can exist. There can be no doubt that if the name of the testator had been burnt or torn out, the revocation would have been as complete as if the will had been torn into twenty pieces. If this were not the case, it would lead to many absurd consequences. But it has been argued that, as the present act of Parliament has pointed out certain modes with regard to the revocation of wills, the Court cannot go beyond the express terms of the act; that the words being confined to burning, tearing, or otherwise destroying, omitting the terms 'obliterating' and 'cancelling' used in the statute of frauds; there must be an actual burning or tearing, or as to ' otherwise destroying,' that the whole instrument must be destroyed; that the cutting, in the present case, is not tearing (burning is out of the question), and, the instrument not being destroyed, that there is no revocation; and upon this part of the argument the case of *Doe dem. Reed* v. *Harris* (6 Ad.& Ell. 209. 1 Nev.& P. 405) in the Queen's Bench was referred to, in which the testator had thrown his will on the fire, with the intention of destroying it, and a part of the cover was burnt, but there being no burning on the instrument itself, the judges of that Court held that the will was not revoked; that the words of the statute of frauds had not been complied with. But that case is not applicable to the present point, for here a part of the will, the most essential part, is removed, and if in that case the name of the testator had been burnt or torn off, I think the Court of Queen's Bench would have held that to be an effectual revocation by burning or tearing, for, according to the judgment in that case, it was not required that the whole will

should be burnt or torn. The learned judges do not say how much it is necessary should be burnt, but Mr. Justice Coleridge says it is sufficient if the entirety of the will is destroyed; his expressions are these, 'We were pressed with the argument; must the whole of the document be destroyed? I say no: but there must be a destruction of so much as to impair the entirety of the will, so that it may be said that the will does not exist in the manner framed by the testator.' So I say here, is not the entirety of the will destroyed by the removal of the signature of the testator? It is true this is not an act of tearing in the strict sense of that term; but, if the circumstances of this case required it, I think it would not be difficult to shew that a will might be revoked by cutting with an instrument as well as by tearing, if a corresponding effect be produced by the one act as by the other . . . Suppose a will were torn into two or more pieces, the will, no doubt, would be revoked; but if it were cut into twenty pieces with a knife, that would be no revocation, and if the pieces could be collected and pasted together, the will must be pronounced for by the Court. I cannot conceive it possible that it was the intention of the legislature to leave the law in that state. The question then comes to this: whether this be or be not a destruction of the will. I consider the name of the testator to be essential to the existence of a will, and that, if that name be removed, the essential part of the will is removed and the will is destroyed; otherwise the statute does certainly not deserve the title it bears, namely, 'An act to amend the laws with respect to wills.'

Similarly, in the case of *Re Adams* [1990] 2 All ER 97, the testatrix had scribbled over her own signature and the signatures of the witnesses in heavy pen marks, with the result that the signatures were no longer visible. Again this meant that the will was no longer valid and had therefore been effectively revoked. These cases may be compared with that of *Cheese v Lovejoy* (1877) 2 PD 251, where the testator had drawn a line through the pages of his will, leaving the writing still clearly visible underneath. He had then thrown the will among a heap of other papers and documents. Here, the testator's acts were deemed to have been insufficient to manifest an intention to revoke – the will had not been damaged in any way, and there was no effect on the crucial parts that indicated its validity.

EXTRACT

Cheese v Lovejoy (1877) 2 PD 251

Case facts

The testator had drawn lines through various parts of his will. He had written 'This is revoked' on the back of the document, and had then thrown it among a pile of wastepaper. A servant had retrieved the document and had kept it until the testator's death. Had the will been revoked?

James LJ's judgment on this issue was brief to the point of terseness.

James LJ

We cannot allow the appeal in this case. It is quite clear that a symbolical burning will not do, a symbolical tearing will not do, nor will a symbolical destruction. There must be the act as well as the intention. As it was put by Dr. Deane in the Court below, 'All the destroying in the world without intention will not revoke a will, nor all the intention in the world without destroying: there must be the two.'

This case represents what may be seen as an unduly strict application of s.20. Perhaps drawing single lines through the clauses of the will may be regarded as insufficient to destroy a will. However, this act coupled by the fact that the testator had expressly written that the will was to be revoked, and the fact that it was discovered among a pile of wastepaper shows a clear manifestation of the testator's intention to revoke the will. It may however be that the court was reluctant to allow the will to be revoked on the basis that although on the facts of the case at hand it was clear that the written statement of revocation had been made by the testator, this might create a dangerous precedent for regarding other wills as being revoked where the written indication of revocation did not comply with s.9. It is also unclear from the facts of the case whether the testator was aware that the will had not been destroyed – the evidence suggests that the will was seen in various prominent places around the house since the time of its apparent revocation. Accordingly, it may be considered that the testator had the opportunity to do more to manifest the revocation of his will and that he had not taken sufficient steps in order to ensure that the will was destroyed. Therefore, although *Cheese v Lovejoy* may be viewed as illogical on its own facts, the judgment may be more readily justified if one considers more broadly what types of actions should be sufficient to destroy a will.

Other examples of acts insufficient to destroy a will can be seen in the cases of *In the Estate of Nunn* [1936] 1 All ER 555, and *Perkes v Perkes* (1820) 3 B & A 489. *In the Estate of Nunn* concerned a testatrix who had cut out a clause of her will, and had sewn the remainder back together. As the missing section did not affect the validity of the remainder, the will was held not to have been revoked by her act. In *Perkes v Perkes*, the testator had torn his will into four pieces in a fit of anger towards one of the intended beneficiaries of the will. However, a bystander grabbed hold of him and prevented him from tearing the will any further. The intended beneficiary and the testator apologised to each other for their conduct and the testator said that he was glad therefore that he had not been able to tear the will into smaller pieces. It was held in this case that the will had not been destroyed, because the testator had not completed the act of destruction he had intended, i.e. he had intended to tear the will into small pieces, but had only cut it into quarters. This was explained by Best J in his judgment where he states (p.742):

> The real question . . . is whether the act be complete. If the testator here after tearing it [i.e. the will] twice through, had thrown the fragments on the ground, it might have been properly considered, that he intended to go no further, and that the cancellation was complete; but here there is evidence that he intended to go further . . .

It is important to note that what must be intended is the revocation. It is possible therefore that there may be an intention to destroy a will, but no intention for it to be revoked. This may be illustrated with reference to the case of *Scott v Scott* (1859)1 Sw & Tr 258. Here the testator destroyed his will mistakenly believing that it would have been revoked by his later will. It transpired however that the later will had not been executed properly, with the effect that it did not revoke the older will. Accordingly, the older will was deemed not to have been revoked, and a copy was accepted as being a valid version of the older will.

One difficulty of course where there has been intentional destruction of the will but no intention to revoke it is how it may be proved to be a person's unrevoked will. This will of course depend on the circumstances. As with *Scott v Scott*, it may be possible to provide a copy of the original will, or it may be possible to send the fragments of the will, as with *Perkes v Perkes*. However, if the only copy of the original will has been completely destroyed but there was no intention to revoke it, then although the will is conceptually valid, the evidence of the testator's intention may be difficult to ascertain evidentially,

and therefore the testator is well advised to draw up a new will. However, a draft copy of a will may be used as evidence of what was contained in a destroyed but unrevoked will, as may oral evidence from those who saw it prior to its destruction, from, for example, the solicitor who drew up the will, or those who witnessed it. In the case of *Re Webb* [1964] 2 All ER 91, a testatrix's original will had been destroyed when the solicitor's office where it was lodged was bombed. She had kept a copy of a draft of the will, and the witnesses gave evidence that they had witnessed the original will. Accordingly the draft coupled with the evidence given by the witnesses was sufficient evidence to conclude that the will had been destroyed but not revoked, and the draft was accepted as a valid version of the will.

EXTRACT

Re Webb, Smith v Johnston and others [1964] 2 All ER 91

Case facts

The testatrix had written a will in 1940. Shortly after it was written the solicitor's office where the will was lodged was damaged, and the will was destroyed. Shortly before the testatrix's death a copy of the will was discovered in the testatrix's house, and identified by her as her will. Although it was many years out of date, the testatrix regarded it as her only will, but intended to write another. She died before the later will could be drawn up. The question for the court was firstly whether destruction had revoked the earlier will, and if not, could the copy be admitted as evidence of what the original will contained.

Faulks J

Counsel for the defendants says that where a will is lost and the copy is relied on, there must be some sufficient evidence of the due execution of the original and that, assuming that I am prepared to allow the plaintiff to rely on this completed draft, that is not enough, for Mrs Mackins, the witness in question, does not give sufficient evidence of the execution of the original. So one must approach the matter in two stages. First of all, in order to decide whether it is proper for the plaintiff to rely on the completed draft, the first matter to which the court has to turn its attention is the well known presumption of law that if a will is lost, which has been in the custody of the testatrix during her lifetime, it has been destroyed by the testatrix animo revocandi. Here, however, the plaintiff herself can supply an answer for she tells me – and I accept her evidence – that shortly before the death of the deceased, a conversation took place between the sisters, as a result of the completed draft having been unearthed by the plaintiff in a tin trunk on the premises of the deceased, which went in this wise: the deceased said: 'Don't throw that away; it's my will.' Her sister replied: 'Well it's very out of date', and apparently indeed it was because it referred to dispositions in favour of a number of people who were already dead. At that the deceased said: 'Well, you take it with you and have it re-done for me', and the plaintiff, very properly, answered: 'I don't know about that, but I'll bring a form for you to sign next time I come.' Unhappily two days before she came 'next time' the deceased died. If anything is clear from that, it must be that the will, the original will, had not been destroyed animo revocandi or the deceased would not have said of the completed draft that it was her will. The deceased accordingly having said that that was her will, and the absence of the original being reasonably accounted for, as in my judgment it is, when one has regard to the bombing of the offices of Mr Warrington Rogers, I think that it is right in this case for the court to have regard to the completed draft. That is in application of the principle laid down in *Sugden v Lord St Leonards* [[1874–80] All ER Rep 21], and in a case, to which counsel for

the defendants referred me, called *In the Estate of Phibbs* [[1917] P 93]. In the former case, however, the execution of the will that was lost was duly proved by the evidence of persons who were in attendance at the time and saw it executed in accordance with the provisions of the Wills Act, 1837. The question here is whether the court is entitled to say that although there is no such affirmative evidence, the completed draft being used as secondary evidence to prove the contents of the last will, the maxim omnia praesumuntur rite esse acta allows the court to say that there being an attestation clause in the completed draft, which speaks to the regularity of the execution of the document, that in the absence of cogent negative evidence is enough. In my view that is enough.

Revival

Unless a will has been destroyed, a revoked will can also be revived. This is contained in s.22 Wills Act 1837, and allows a revoked will to be revived either by being re-executed, or by a codicil that manifests an intention to revive an earlier will. Re-execution requires compliance with s.9 Wills Act 1837. Another possibility is that the will remains unaltered but that a codicil gives effect to the revocation. In the case of *In the Goods of Davis* [1952] P 279, a testator made a will leaving his estate to a woman who later became his wife. The act of marriage effected the revocation of the earlier will, even though the sole beneficiary of the will was the testator's wife. However, the testator had signed and executed a codicil to his will explaining that the beneficiary was now the testator's wife. This was held to be sufficient to revive the earlier will. However, in order for a will to be revived it must still be in existence. In the case of *Rogers v Goodenough* (1862) 2 Sw & Tr 342, the testator burned his first will having made a second will. However, he later wished to revive the first will but this was held to be ineffective as the first will no longer existed. It must also be borne in mind that there must be an intention to revive the first will – merely revoking a later will shall not cause the revival of the earlier will, as is seen in *In the Goods of Hodgkinson* [1893] P 339.

Interpreting a will

One of the difficulties with the law of wills is that the words used may be ambiguous in their meaning. In the same way as the words contained in a statute are interpreted, so too must the words of a will be interpreted in a way that is consistent both with the testator's intentions and with the need for the courts to provide an objective evaluation of what a will means. The difference between wills and statutes is that statutes are drafted by professional draftspeople who envisage that the texts they produce will need to be read and interpreted. A will on the other hand is not necessarily drafted in this way. Many people will of course consult a solicitor in order to write a will, and the solicitor is likely to refer to a series of will precedents in order to draft the document. Such will precedents provide accepted forms of wording for the most commonly used clauses. *Williams on Wills* for example provides the following precedents for, respectively, a clause revoking earlier wills, a clause appointing trustees, and a clause that leaves the entire estate to an individual person (a common beneficiary where one leaves the entirety of one's estate to a sole beneficiary would be the testator's spouse or civil partner).

EXTRACT

Williams on Wills Vol. 2

Wills precedents

I [testator] of [address] hereby revoke all former testamentary dispositions made by me and declare this to be my last will.

I appoint my wife [name] sole executrix and trustee of this my will but if my wife shall die in my lifetime or shall refuse or be unable to act as such executrix and trustee[2] then I appoint [name] of [address] and [name] of [address] to be the executors and trustees of this my will and I declare that in this will the expression 'my trustee' shall where the context so admits include my personal representatives or personal representative for the time being and the trustees or trustee for the time being of this will.

Subject to the payment of my debts funeral and testamentary expenses, inheritance tax legacies and annuities I devise and bequeath all my real and personal estate whatsoever and wheresoever of which I have any power of disposition by will whatsoever not hereby or by any codicil hereto specifically disposed of unto [name] absolutely.

However, it is entirely permissible for a will to be drawn up without professional advice by the testator him- or herself. Accordingly, the words used by the testator may have a meaning that he or she did not contemplate, and therefore the Chancery division of the High Court often has to guess what the testator intended from the words used in his will, and to attempt to give effect to that, while at the same time maintaining consistency in how words are used across different areas of law. Clearly, when the courts come to interpreting a will, the person who knew what his intentions were, namely the testator, will not be available to give evidence. Accordingly, the main source of information the court has to go by will be the will itself and the words contained in that will. Therefore, the law's role is not to consider what the testator actually intended when he or she made the will, but rather to consider what he or she intended by the words that were used – the court is not able to guess what the testator did not express. What becomes apparent is that what is intended from the words contained in the will may be different from what the court concludes must have been the testator's actual intention.

A leading modern authority on the interpretation of legal documents is the case of *Mannai Investment Co Ltd v Eagle Star Life Assurance Co Ltd* [1997] AC 749. Although the case deals primarily with the interpretation of contracts, many of the principles it outlines are equally applicable in the context of wills. Here it is acknowledged that words may have broader or narrower meanings, and different words may have different meanings according to the context in which they are used. Accordingly, it is necessary for the court to decide what meanings of the terms used are the most appropriate to give effect to the testator's intentions.

EXTRACT

Mannai Investment Co Ltd v Eagle Star Life Assurance Co Ltd [1997] AC 749

Lord Hoffmann

I propose to begin by examining the way we interpret utterances in everyday life. It is a matter of constant experience that people can convey their meaning unambiguously although they have used the wrong words. We start with an assumption that people will use words and grammar in a conventional way but quite often it becomes obvious that, for one reason or another, they are not doing so and we adjust our interpretation of what they are saying accordingly. We do so in order to make sense of their utterance: so that the different parts of the sentence fit together in a coherent way and also to enable the sentence to fit the background of facts which plays an indispensable part in the way we interpret what anyone is saying. No one, for example, has any difficulty in understanding Mrs. Malaprop. When she says 'She is as obstinate as an allegory on the banks of the Nile,' we reject the conventional or literal meaning of allegory as making nonsense of the sentence and substitute 'alligator' by using our background knowledge of the things likely to be found on the banks of the Nile and choosing one which sounds rather like 'allegory.'

Mrs. Malaprop's problem was an imperfect understanding of the conventional meanings of English words. But the reason for the mistake does not really matter. We use the same process of adjustment when people have made mistakes about names or descriptions or days or times because they have forgotten or become mixed up. If one meets an acquaintance and he says 'And how is Mary?' it may be obvious that he is referring to one's wife, even if she is in fact called Jane. One may even, to avoid embarrassment, answer 'Very well, thank you' without drawing attention to his mistake. The message has been unambiguously received and understood.

If one applies that kind of interpretation to the notice in this case, there will also be no ambiguity. The reasonable recipient will see that in purporting to terminate pursuant to clause 7(13) but naming 12 January 1995 as the day upon which he will do so, the tenant has made a mistake. He will reject as too improbable the possibility that the tenant meant that unless he could terminate on 12 January, he did not want to terminate at all. He will therefore understand the notice to mean that the tenant wants to terminate on the date on which, in accordance with clause 7(13), he may do so, i.e. 13 January.

Why, then, do cases like *Hankey v. Clavering* [1942] 2 K.B. 326 arrive at a different answer? I want first to deal with two explanations which seem to me obviously inadequate. First, it is sometimes said that the examples which I have given from ordinary life are concerned with what the speaker meant to say. He may subjectively have intended to say something different from what he actually said and it may be possible, by the kind of reasoning which I have described, to divine what his subjective intentions were. But the law is not concerned with subjective intentions. All that matters is the objective meaning of the words which he has used.

It is of course true that the law is not concerned with the speaker's subjective intentions. But the notion that the law's concern is therefore with the 'meaning of his words' conceals an important ambiguity. The ambiguity lies in a failure to distinguish between the meanings of words and the question of what would be understood as the meaning of a person who uses words. The meaning of words, as they would appear in a dictionary, and the effect of their syntactical arrangement, as it would appear in a grammar, is part of the material which we use to understand a speaker's utterance. But it is only a part; another part is our knowledge of the

background against which the utterance was made. It is that background which enables us, not only to choose the intended meaning when a word has more than one dictionary meaning but also, in the ways I have explained, to understand a speaker's meaning, often without ambiguity, when he has used the wrong words.

When, therefore, lawyers say that they are concerned, not with subjective meaning but with the meaning of the language which the speaker has used, what they mean is that they are concerned with what he would objectively have been understood to mean. This involves examining not only the words and the grammar but the background as well. So, for example, in *Doe d. Cox v. Roe*, 4 Esp. 185 the landlord of a public house in Limehouse gave notice to quit 'the premises which you hold of me . . . commonly called . . . The Waterman's Arms.' The evidence showed that the tenant held no premises called The Waterman's Arms; indeed, there were no such premises in the parish of Limehouse. But the tenant did hold premises of the landlord called The Bricklayer's Arms. By reference to the background, the notice was construed as referring to The Bricklayer's Arms. The meaning was objectively clear to a reasonable recipient, even though the landlord had used the wrong name. We therefore will in due course have to answer the question: if, as long ago as 1803, the background could be used to show that a person who speaks of The Waterman's Arms means The Bricklayer's Arms, why can it not show that a person who speaks of 12 January means 13 January?

The immediate point, however, is that the fact that the law does not have regard to subjective meaning is no explanation of the way *Hankey v. Clavering* [1942] 2 K.B. 326 was decided. There was no need to resort to subjective meaning: the notice would objectively have been understood to mean that the landlord wanted to terminate the tenancy on the day on which he was entitled to do so.

I pass on to a second explanation which also seems to me inadequate. Lord Greene M.R. said, at pp. 329–330, that because such notices have unilateral operation, the conditions under which they may be served must be strictly complied with. I have already said that this principle is accepted on both sides. But, as an explanation of the method of construction used in *Hankey v. Clavering*, it begs the question. If the clause had said that the notice had to be on blue paper, it would have been no good serving a notice on pink paper, however clear it might have been that the tenant wanted to terminate the lease. But the condition in clause 7(13) related solely to the meaning which the notice had to communicate to the landlord. If compliance had to be judged by applying the ordinary techniques for interpreting communications, there was strict compliance. The notice clearly and unambiguously communicated the required message. To say that compliance must be strict does not explain why some other technique of interpretation is being used or what it is.

A variation of this explanation is to say that the language of the notice must be strictly construed. But what does it mean to say that a document must be 'strictly' construed, as opposed to the normal process of ascertaining the intentions of the author? The expression does not explain itself. If it operates merely by way of intensification, so that the intention must be clear, unambiguous, incapable of misleading, then I think that the notice in this case satisfied the test at that level. Likewise, as Lord Greene M.R. acknowledged when he said that the whole thing was obviously a slip, did the notice in *Hankey v. Clavering*. So the concept of strict construction does not explain the decision.

A more promising clue to the explanation is Lord Greene's statement, in two places, that the notice must 'on its face' comply with the terms of the lease. What does 'on its face' mean? Clearly, the face of the document is being contrasted with the background, in law sometimes called the 'extrinsic evidence,' against which the language is ordinarily construed. But Lord Greene cannot have meant that the document must always be read without any background,

because (even if, which I doubt, it were conceptually possible to interpret the use of language without the aid of any background) cases like the *Cox* case, 4 Esp. 185, show that some background, at least, can be used. It appears, therefore, that Lord Greene is referring to some principle whereby background can be used to show that a person who speaks of The Waterman's Arms means The Bricklayer's Arms, but not that a person who speaks of 12 January means 13 January. What principle is this?

It is, I think, to be found in an old rule about the admissibility of extrinsic evidence to construe legal documents. In its pure form, the rule was said to be that if the words of the document were capable of referring unambiguously to a person or thing, no extrinsic evidence was admissible to show that the author was using them to refer to something or someone else. An extreme example is in *In the Goods of Peel* (1870) L.R. 2 P.& D. 46, in which the testator appointed 'Francis Courtenay Thorpe, of Hampton . . . Middlesex' to be his executor. There was a Francis Courtenay Thorpe of Hampton, Middlesex. He was however only 12 years old and his father Francis Corbet Thorpe, of Hampton, Middlesex, was an old friend of the testator. Lord Penzance said, at p. 47, that these facts were inadmissible: 'The testator makes use of a description which applies in fact to one person, and not to any other.' A variation on this rule was *In re Fish; Ingham v. Rayner* [1894] 2 Ch. 83 in which the testator left his residuary estate to his 'niece Eliza.' He had no niece called Eliza but his wife had an illegitimate grandniece called Eliza, to whom the evidence of their relationship showed that he must have intended to refer, and also, as it happened, a legitimate grandniece called Eliza. The Court of Appeal said that the estate went to the legitimate grandniece and that evidence of the relationship between the testator and the illegitimate grandniece was inadmissible. Lindley L.J. said, at p. 85:

> 'where the person most nearly answering the description is the legitimate grandniece of the testator's wife . . . no evidence can be admitted to prove that her illegitimate grandniece was intended.'

On the other hand, if there was no one to whom the description accurately applied, there was said to be a 'latent ambiguity' and evidence of background facts which showed what the testator must have meant, notwithstanding that he had used the wrong words, was admitted.

Let us compare this rule with ordinary common sense interpretation of what people say. If someone has gone to great pains, well in advance, to secure tickets for himself and a friend for a Beethoven concert at the Royal Festival Hall by a famous visiting orchestra on 13 January and says to the friend a week earlier 'I'll see you at the Festival Hall concert on 12 January' it will be obvious that he is referring to the concert on 13 January. According to the old rules of construction, the law will agree if there is no concert at the Festival Hall on 12 January. In that case there is a latent ambiguity. But if there is a concert on that date (Stockhausen, say, played by a different orchestra) he will be taken to have referred to that concert.

This extraordinary rule of construction is, as it seems to me, the only explanation for the decisions in *Hankey v. Clavering* [1942] 2 K.B. 326 and *Cadby v. Martinez*, 11 A.& E. 720. The *Cox* case, 4 Esp. 185, was distinguished by counsel in the Cadby case, at p. 723, as involving a latent ambiguity: there was no Waterman's Arms in Limehouse, so evidence that the landlord would have been understood by a reasonable tenant as intending to refer to The Bricklayer's Arms was admissible. But Midsummer 1837, or 21 December 1941 (in *Hankey v. Clavering*) or 12 January 1995 (in this case) are all real dates to which the notices could have referred. Therefore evidence of background which showed that a reasonable recipient would have understood the person giving the notice as having intended to refer to a different date had to be disregarded. The effect is that apart from the exceptional case in which the date is obviously impossible on the face of the notice (as in *Carradine Properties Ltd. v. Aslam* [1976] 1 W.L.R. 442) the intention which the notice would convey as to date has to be determined without regard to the terms of

the lease (or anything else) as background. There is an artificial assumption that the reasonable recipient does not know what would be the correct date. On this basis, the interpretation of the notices as referring to the wrong dates and therefore being invalid is, of course, inescapable.

It is clear that this rule of construction has been applied to the interpretation of notices for at least 200 years and it is hardly surprising that Lord Greene M.R. and Lord Clauson felt obliged to apply it in *Hankey v. Clavering* and that the Court of Appeal applied it in this case. It is, however, highly artificial and capable of producing results which offend against common sense. Lord Penzance began his decision that the testator had appointed a 12-year-old boy as his executor by saying:

> 'If I am at liberty to look at the facts stated in the affidavits, I may possibly have no difficulty in deciding that the person meant is the father, but the question is, whether I am at liberty to do so:' In the Goods of Peel, L.R. 2 P.& D. 46.

In *In re Fish* [1894] 2 Ch. 83, 84, Lindley L.J. began his judgment by saying: 'This is one of those painful cases in which it is probable that the testator's intention will be defeated' and A.L. Smith L.J. said, at p. 86, that if he could have admitted the evidence about the testator's relationship with his wife's illegitimate grandniece he would gladly have done so.

I think that the rule is not merely capricious but also, for reasons which I need not develop at length, incoherent. It is based upon an ancient fallacy which assumes that descriptions and proper names can somehow inherently refer to people or things. In fact, of course, words do not in themselves refer to anything; it is people who use words to refer to things. The word 'allegory' does not mean a large scaly creature or anything like it, but it is absurd to conclude, as judges sometimes do, that this is not an 'available meaning' of the word in the interpretation of what someone has said. This is simply a confusion of two different concepts; as we have seen, a person can use the word 'allegory,' successfully and unambiguously, to refer to such a creature.

Even in its natural habitat, the construction of wills, the rule has not been (and, I think, cannot be) applied with any consistency. In *National Society for the Prevention of Cruelty to Children v. Scottish National Society for the Prevention of Cruelty to Children* [1915] A.C. 207 Earl Loreburn refused to accept that there was 'a rigid rule' that 'once a persona is accurately named in a will' there is not to be 'any further inquiry or consideration in regard to the person who is to take the benefit.' The true rule, he said, was that 'the accurate use of a name in a will creates a strong presumption against any rival who is not the possessor of the name.' This demotes the rule to the common sense proposition that in a formal document such as a will, one does not lightly accept that people have used the wrong words. I doubt whether anyone would dissent from this principle, which would present no obstacle to a conclusion that the tenant in this case must have used the wrong words.

If your Lordships are to follow this path, it will be necessary to say that *Hankey v. Clavering* and the older cases which it followed are no longer good law. It would be wrong, I think, to distinguish them on narrow grounds and leave them as wrecks in the channel, causing uncertainty and litigation in the future. Furthermore, the old rule of construction has been applied not only to notices exercising break clauses but also to notices to terminate periodic tenancies: *Doe d. Spicer v. Lea* (1809) 11 East 312. In his admirable submissions on behalf of the landlord,

Mr. Patten warned that a departure from the old rule would cause great uncertainty in the daily construction of notices to quit in county courts throughout the land. I confess that this prospect has caused me some anxiety and I think that it must be given serious consideration.

The rule as applied to wills, which restricts the use of background in aid of construction, reflects a distrust of the use of oral evidence to prove the background facts. The people who could give

evidence about the background to a will would in most cases be members of the family interested in the outcome of the case and until 1843, persons with an interest in the litigation were not even competent witnesses. No doubt the exclusion of background makes, in a somewhat arbitrary way, for greater certainty in the sense that there is less room for dispute about what the background was and the effect which it has upon the intention to be attributed to the testator. But, as the cases mournfully show, this certainty is bought at the price of interpretations which everyone knows to be contrary to the meaning which he intended.

There are documents in which the need for certainty is paramount and which admissible background is restricted to avoid the possibility that the same document may have different meanings for different people according to their knowledge of the background. Documents required by bankers' commercial credits fall within this category. Article 13(a) of the Uniform Customs and Practice for Commercial Credits (1993 revision) says (echoing Lord Greene M.R.'s phrase in *Hankey v. Clavering*) that the documents must 'upon their face' appear to be in accordance with the terms and conditions of the credit. But the reasons of policy which require the restriction of background in this case do not apply to notices given pursuant to clauses in leases. In practice, the only relevant background will be, as in this case, the terms of the lease itself, which may show beyond any reasonable doubt what was the intention of the person who gave the notice. There will be no question of the parties not being privy to the same background – both of them will have the lease – and no room for dispute over what the relevant background is.

In the case of commercial contracts, the restriction on the use of background has been quietly dropped. There are certain special kinds of evidence, such as previous negotiations and express declarations of intent, which for practical reasons which it is unnecessary to analyse, are inadmissible in aid of construction. They can be used only in an action for rectification. But apart from these exceptions, commercial contracts are construed in the light of all the background which could reasonably have been expected to have been available to the parties in order to ascertain what would objectively have been understood to be their intention: *Prenn v. Simmonds* [1971] 1 W.L.R. 1381, 1383. The fact that the words are capable of a literal application is no obstacle to evidence which demonstrates what a reasonable person with knowledge of the background would have understood the parties to mean, even if this compels one to say that they used the wrong words. In this area, we no longer confuse the meaning of words with the question of what meaning the use of the words was intended to convey. Why, therefore, should the rules for the construction of notices be different from those for the construction of contracts? There seems to me no answer to this question.

All that can be said is that the rules for the construction of notices, like those for the construction of wills, have not yet caught up with the move to common sense interpretation of contracts which is marked by the speeches of Lord Wilberforce in *Prenn v. Simmonds* [1971] 1 W.L.R. 1381 and *Reardon Smith Line Ltd. v. Yngvar Hansen-Tangen* [1976] 1 W.L.R. 989. The question is therefore whether there is any reason not to bring the rules for notices up to date by overruling the old cases.

There can, I think, be no question of anyone having acted in reliance on the principle of construction used in *Hankey v. Clavering* [1942] 2 K.B. 326. The consequence of such a construction is only to allow one party to take an unmeritorious advantage of another's verbal error, an adventitious bonus upon which no one could have relied. In this respect, the case for rejecting the old authorities is at least as strong as it was in *Sudbrook Trading Estate Ltd. v. Eggleton* [1983] 1 A.C. 444, in which this House overruled cases going back to the early 19th century on the construction of contracts for sale at a valuation.

> Nor do I think that a decision overruling the old cases will create uncertainty as to what the law is. In fact I think that the present law is uncertain and that only a decision of this House, either adopting or rejecting the *Hankey v. Clavering* rule of construction, will make it certain. So, for example, in *Carradine Properties Ltd. v. Aslam* [1976] 1 W.L.R. 442, 444, Goulding J. said that the test for the validity of a notice was: 'Is the notice quite clear to a reasonable tenant reading it? Is it plain that he cannot be misled by it?' and he went on to say that the reasonable tenant must be taken to know the terms of the lease. This test was approved by the Court of Appeal in *Germax Securities Ltd. v. Spiegal* (1978) 37 P.& C.R. 204, 206 and, as will be apparent from what I have already said, I think that it was the right test to adopt. It is, however, absolutely impossible to reconcile the application of such a test with the decision in *Hankey v. Clavering*, in which no reasonable tenant who knew the terms of the lease could possibly have mistaken the landlord's meaning. It is therefore not surprising that in *Micrografix v. Woking 8 Ltd.* [1995] 2 E.G.L.R. 32 Jacob J. felt free to dismiss *Hankey v. Clavering* as 'much distinguished' and to ignore it, or that Rattee J. in *Garston v. Scottish Widows' Fund and Life Assurance Society* [1996] 1 W.L.R. 834 should be puzzled as to why the Court of Appeal in this case considered, as I think rightly, that they were bound by *Hankey v. Clavering*.
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> In my view, therefore, the House should say unequivocally that the test stated by Goulding J. in *Carradine Properties Ltd. v. Aslam* [1976] 1 W.L.R. 442 was right and that *Hankey v. Clavering* and the earlier cases should no longer be followed. The notice should be construed against the background of the terms of the lease. Interpreted in this way, the notice in the present case was valid and I would therefore allow the appeal.

The essence of Lord Hoffmann's judgment is that the law's role is to interpret meaning objectively. Its primary evidence, particularly in the context of wills, is the words the testator used, and the court cannot guess whether a person has used those words correctly or whether the words that have been used accurately convey what he or she intended to convey. Nevertheless, this does not mean that the testator's subjective intentions are irrelevant; the court must look at the words the testator used within the context of their usage, and therefore it is possible to construe which of a range of possible meanings the testator was intending when he or she used a specific word, as well as to interpret what was intended when the wrong words were used.

For example, there are regional and cultural differences in what people mean when they use a particular word, and therefore the word should not be construed solely with reference to its usual meaning, but also its usual meaning in the context of the testator's habitual usage or the usage within a particular geographical region/culture/profession. Construing meaning with reference to such aspects of the testator's background means that the court's role is to identify what would be a reasonable person's interpretation of the words used.

Lawyers for example use words in a different way to laypersons, and terms such as trust, consideration, company, redemption, property have specific meanings for lawyers, while non-lawyers use these terms in different ways. Accordingly, the use of legal terminology by a non-lawyer will be interpreted in accordance with its popular meaning, while on the other hand, the use of legal terminology by a lawyer, or within the context of a professionally drafted will, will be interpreted according to its legal meaning. Viscount Simon explains this in the case of *Perrin v Morgan*:[27]

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[27] [1943] AC 399 at p.405.

My Lords, the fundamental rule in construing the language of a will is to put upon the words used the meaning which, having regard to the terms of the will, the testator intended. The question is not, of course, what the testator meant to do when he made his will, but what the written words he uses mean in the particular case-what are the 'expressed intentions' of the testator. In the case of an ordinary English word like 'money,' which is not always employed in the same sense, I can see no possible justification for fixing upon it, as the result of a series of judicial decisions about a series of different wills, a castiron meaning which must not be departed from unless special circumstances exist, with the result that this special meaning must be presumed to be the meaning of every testator in every case, unless the contrary is shown. I agree, of course, that, if a word has only one natural meaning, it is right to attribute that meaning to the word when used in a will, unless the context or other circumstances which may be properly considered show than an unusual meaning is intended. But the word 'money' has not got one natural or usual meaning. It has several meanings, each of which in appropriate circumstances may be regarded as natural. In its original sense, which is also its narrowest sense, the word means 'coin.' Moneta was an appellation of Juno and the temple of Moneta at Rome was the mint. Phrases like 'false money' or 'clipped money' show the original use in English. But the conception very quickly broadens into the equivalent of 'cash' of any sort. The question 'Have you any money in your purse?' refers presumably to bank notes or treasury notes, as well as to shillings and pence. A further extension would include not only coin and currency in the possession of an individual, but debts owing to him and cheques which he could pay into his banking account, or postal orders, or the like. Again, going further, it is a matter of common speech to refer to one's 'money at the bank,' although in a stricter sense the bank is not holding one's own money and what one possesses is a chose in action which represents the right to require the bank to pay out sums held at the call of its customer. Sums on deposit, whether with a bank or otherwise, may be included by a further extension. But this is by no means the limit to the senses in which the word 'money' is frequently and quite naturally used in English speech. The statement that I have my money invested on mortgage or in debentures, or in stocks and shares, or in savings certificates, is not an illegitimate use of the word 'money,' upon which the courts are bound to frown, though it is a great extension from its original meaning to interpret it as covering securities. In considering the various meanings of the word 'money' in common speech, one must go even further, as any dictionary will show. The word may be used to cover the whole of an individual's personal property-sometimes, indeed, all of a person's property, whether real or personal. 'What has he done with his money?' may well be an inquiry as to the general contents of a rich man's will. Horace's satire at the expense of the fortune-hunter, who attached himself to childless Roman matrons, has its modern equivalent in the saying, 'It's her money he's after.' When St Paul wrote to Timothy that the love of money is the root of all evil, he was not warning him of the risks attaching to one particular kind of wealth, but was pointing to the dangers of avarice in general. When Tennyson's northern farmer counselled his son not to marry for money, but to go where money is, he was not excluding the attractiveness of private property in land. These wider meanings of 'money' are referred to in some of the reported cases as 'popular' meanings, in contrast to the 'legal' meaning of the term, but for the purpose of construing a will and especially a home-made will, a popular meaning may be the more important of the two. The circumstance that a skilled draftsman would avoid the use of so ambiguous a word only confirms the view that, when it is used in a will, the popular as opposed to the technical use of the word 'money' may be important.

> I protest against the idea that, in interpreting the language of a will, there can be some fixed meaning of the word 'money,' which the courts must adopt as being the 'legal' meaning as opposed to the 'popular' meaning. The proper meaning is the correct meaning in the case of the particular will and there is no necessary opposition between that meaning and the popular meaning. The duty of the court, in the case of an ordinary English word which has several quite usual meanings which differ from one another, is not to assume that one out of several meanings holds the field as the correct meaning until it is ousted by some other meaning regarded as 'non-legal,' 'but to ascertain without prejudice as between various usual meanings which is the correct interpretation of the particular document.'

Lord Hoffmann therefore advocates going beyond a dictionary definition of words used, and looking at how words are understood in their context. His example of the character of Mrs Malaprop in Sheridan's *The Rivals*[28] is an example. If one looks in a dictionary for the term 'allegory', the character's use of the word to describe a creature living on the river Nile would be nonsensical. However, by looking at the context in which she uses the word, she does not use the word allegory in its strict sense as a 'Description of a subject under the guise of some other subject of aptly suggestive resemblance'[29] but rather as a word meaning 'A genus of saurian reptiles of the crocodile family, also called Caymans, of which the various species are found in America; popularly the name is extended to all large American Saurians, some of which are true crocodiles'.[30]

Accordingly, in the context of wills it is necessary to consider how the words used by the testator are employed in the context of the document as a whole and in the context of the testator's background and the circumstances in which the will was written. For example, people might refer to their cohabitant as their wife/husband as a more convenient shorthand than unmarried cohabitant, or to their children as all the children living with them (their spouse's children from a previous relationship as well as their own biological children). Accordingly, in the case of *Perrin v Morgan* [1943] AC 399 Lord Atkin argued that one's style of writing, and the meaning attributable to particular words is socially determined – in other words dependent on one's individual circumstances and background including age, education and relationship to the beneficiary. He states:

> the construing court has to ascertain what was meant being guided by the other provisions of the will and the other relevant circumstances, including the age and education of the testator, his relations to the beneficiary chosen, whether kinship or friendship, the provision for other beneficiaries, and other admissible circumstances. Weighing all these, the court must adopt what appears to be the most probable meaning. To decide on proven probabilities is not to guess but to adjudicate. If this is to decide according to the context, I am content, but I cannot agree that the court is precluded from looking outside the terms of the will. No will can be analysed in vacuo. There are material surroundings such as I have suggested in every case and they have to be taken into account. The sole object is of course to ascertain from the will the testator's intentions (p.414).

Accordingly, the case of *Perrin v Morgan* considered that the term money could be interpreted more broadly than simply meaning cash, and was deemed to include stocks and

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[28] Sheridan R.B. (2004) *The Rivals*. London: Methuen Drama.
[29] OED definition.
[30] OED definition.

shares, rent owed to her by tenants on property she owned, an income tax rebate she was owed and dividends. During the 19th century, the court's tendency was to consider that words should be given a narrow meaning – in other words that terms such as money should only include those forms of money upon which there could be no disagreement. In the case of *Lowe v Thomas* (1854) 5 DE GM & G 315 for example, money was deemed to refer only to cash, even though the particular circumstances of the case suggested that the testatrix had probably intended for the term money to be used more widely, as she had only a small amount of cash that was to be divided between a large number of beneficiaries, and a significant number of stocks and shares that were not included in the bequest.

There are however more recent examples of its being used, for example the case of *Re Rowland* [1963] Ch 1. In this case, a testator had made a will leaving everything to his wife, or to other beneficiaries if his wife's death preceded or coincided with his. Both the testator and his wife died in an accident, and the other beneficiaries therefore attempted to claim that they were entitled to inherit the estate, as the wife's death had coincided with that of her husband. The high court declined this interpretation, as it coincided with was deemed to mean 'occurring simultaneously', i.e. that the other beneficiaries were entitled to benefit under the will if the testator and his wife died at exactly the same second as each other. It is more likely however that what the testator meant was if he and his wife died as a consequence of the same event (even if the wife survived her husband by a short time) – as was the case in this situation, the other beneficiaries should inherit. However, the court took the view that as coincided meant 'at exactly the same time' the will did not countenance the possibility that the wife might survive her husband by a very short period of time (seconds, minutes or a few hours) before dying herself. Accordingly, the other beneficiaries named in the testator's will were unable to inherit.

Nevertheless, cases that have come before the courts in the 20th century have tended to take a rather more liberal approach to the interpretation of wills – looking more to how the testator intended his words to be interpreted, rather than considering the literal interpretation of the words used. The broader approach to the construction of wills considers what the words mean in the context of the will itself, and where appropriate with reference to extrinsic evidence, such as other examples/contexts in which the testator used the words he used, or the evidence of witnesses regarding how he came to the decision to use a specific word or phrase.

Lord Denning was a particularly strong advocate of the contextual approach to the interpretation of wills. In his dissenting judgement in the case of *Re Rowland* he states:

> the whole object of construing a will is to find out the testator's intentions so as to see that is property is disposed of in the way he wished. True it is that you must discover his intention from the words he used: but you must put on his words the meaning which they bore to him . . . and in order to discover the meaning which he intended, you will not get much help by going to a dictionary. It is very unlikely that he used a dictionary, and even less likely that he used the same one as you. What you should do is to place yourself as far as possible in his position, taking note of the facts and circumstances known to him at the time: and then say what he meant by his words.

Thus in the case of *Re Lynch* [1943] 1 All ER 168, the testator left his estate to his wife, and then to his sons after his wife's death or remarriage, but it was proved that the term wife referred to his unmarried cohabitant (as the testator had never married), and that

the term remarriage was used to mean marriage for the first time to a person other than the deceased (as the beneficiary had never been married before).

Nevertheless, the courts' primary text is the will and therefore it is only able to interpret what the testator expressed in the will, and cannot speculate on what would have been the testator's intention when the circumstances are different from those envisaged by the deceased testator. For example in *Jones v Midland Bank* [1998] 1 FLR 246 a testatrix left the entirety of her estate to her son, but if the son should 'predecease' her, her nephews should inherit the estate. What actually occurred was that the son was convicted of his mother's manslaughter, a consequence of which was that he forfeited any claim to her estate. Could the nephews inherit? The court held that they could not – to predecease means to die before the testatrix. The son was still alive at the time of the testatrix's death, and had not therefore predeceased her. Accordingly, as the nephews could only inherit in the event of the son predeceasing his mother, they were not entitled to inherit if the son was not entitled to the estate for some other reason . . . such as his conviction for manslaughter. Of course it may be that, had she considered that possibility, the testatrix would have wished for the nephews to inherit, but the court felt that it was not its role to speculate upon what the testatrix might have wished in such circumstances.

The general approach therefore appears to be that the courts will presume that words are given their ordinary, usual meaning (e.g. that wife does not ordinarily mean 'unmarried cohabitant') and that technical terminology is used correctly. An example of the latter point can be seen in the case of *Re Cook* [1948] Ch 212, where the testatrix had bequeathed all her personal estate. It may be that she meant to give everything she owned, but it was held that the clause only referred to personalty, and did not therefore dispose of any land that she owned. A lawyer would be expected to know what such a term as 'personal estate' meant, and would therefore only have used it if personalty was what was intended. Nevertheless, the courts are often willing to show a greater degree of leniency where a will has been drawn up without the benefit of legal advice. By contrast however, where a will has been drawn up as a consequence of legal advice having been given, the courts are less willing to countenance a broader interpretation than the strict technical meaning of the term. However if there is more than one possible meaning of a word (such as money for example, which could be interpreted very narrowly so as only to amount to cash, or could be interpreted more broadly so as to encompass other assets that represent money, such as stocks and shares, dividends and savings bonds) to give the word the interpretation that is most appropriate in the circumstances of the case. However, where the ordinary meaning is inappropriate, or where the testator has supplied some evidence of his or her intended meaning (such as where he or she provides definitions of particular words), then the court will consider interpreting the will more broadly. An example where the ordinary meaning of a word was inappropriate in the circumstances of the case may be encountered in the case of *Thorn v Dickens* [1906] WN 54 where the testator had left everything to a person referred to as mother. Again the ordinary meaning of the phrase mother would be to mean one's female parent. However, it was shown that the person the testator referred to as mother was in fact the testator's wife, and as the testator's own mother had died long before the will was drawn up, the will was construed so as to mean that the testator wished to give his estate to his wife.

Extrinsic evidence

Further support to the notion that the court's function is to give effect to the testator's intention is encountered in s.21 Administration of Justice Act 1982 which allows a court

to consider extrinsic evidence in order to determine what a testator intended by his or her will.

EXTRACT

Administration of Justice Act 1982, s.21

21 Interpretation of wills – general rules as to evidence

(1) This section applies to a will-

(a) in so far as any part of it is meaningless;

(b) in so far as the language used in any part of it is ambiguous on the face of it;

(c) in so far as evidence, other than evidence of the testator's intention, shows that the language used in any part of it is ambiguous in the light of surrounding circumstances.

(2) In so far as this section applies to a will extrinsic evidence, including evidence of the testator's intention, may be admitted to assist in its interpretation.

That being so, it is not however the role of the court to speculate as to what the testator has given no thought to, or which he or she may have considered but which is not evident from the will. Therefore, while a court is willing to presume that by writing a will the testator did not intend to die intestate, and is therefore willing to find an interpretation of the will that permits testacy rather than intestacy, the court cannot construe into a will what was not there in the first place.

In the case of *Miller v Travers* (1832) 8 Bing 244 for example the testator had disposed by will of all his land in county Limerick (this was before Irish independence). In fact he had very little land in County Limerick, but had a considerable amount of land in County Clare that was not referred to at all in the will. An attempt was made to argue that extrinsic evidence should be accepted to confirm that the testator had intended to include the land in County Clare with the land in County Limerick. However, there was no basis for arguing this, as the will was silent in relation to the land in County Clare, and therefore the reference to County Limerick could not be construed as meaning County Limerick and County Clare, because there was no suggestion that that should be the case. All extrinsic evidence can do therefore is to confirm which of several possible intentions expressed in the will accords most closely with the testator's true intention. This is explained by Nicholas J in *Re Williams* [1985] 1 All ER 964 where he states:

> The evidence may assist by showing which of two or more possible meanings a testator was attaching to a particular word or phrase. 'My effects' and 'my money' are obvious examples. That meaning may be one which without recourse to the extrinsic evidence would not really have been apparent at all. So long as that meaning is one which the word or phrase read in its context is capable of bearing, then the court may conclude that, assisted by the extrinsic evidence, that is its correct construction. But if, however liberal may be the approach of the court, the meaning is one which the word or phrase cannot bear, I do not see how . . . the court can declare that meaning to be the meaning of the word or phrase.

Further scope to resolve ambiguity is provided by s.20 Administration of Justice Act 1982, which allows a court to rectify wills by adding or removing words.

EXTRACT

Administration of Justice Act 1982, s.20

20 Rectification

(1) If a court is satisfied that a will is so expressed that it fails to carry out the testator's intentions, in consequence-

(a) of a clerical error; or

(b) of a failure to understand his instructions,

it may order that the will shall be rectified so as to carry out his intentions.

(2) An application for an order under this section shall not, except with the permission of the court, be made after the end of the period of six months from the date on which representation with respect to the estate of the deceased is first taken out.

(3) The provisions of this section shall not render the personal representatives of a deceased person liable for having distributed any part of the estate of the deceased, after the end of the period of six months from the date on which representation with respect to the estate of the deceased is first taken out, on the ground that they ought to have taken into account the possibility that the court might permit the making of an application for an order under this section after the end of that period; but this subsection shall not prejudice any power to recover, by reason of the making of an order under this section, any part of the estate so distributed.

(4) In considering for the purposes of this section when representation with respect to the estate of a deceased person was first taken out, a grant limited to settled land or to trust property shall be left out of account, and a grant limited to real estate or to personal estate shall be left out of account unless a grant limited to the remainder of the estate has previously been made or is made at the same time.

However, this is very limited. A will will not be altered by a court unless it is considered necessary to do so. Furthermore, a will will not be altered to give effect to the supposed intention of the testator if the will itself is unambiguous. Furthermore, it must be clear what is extraneous or what is omitted so that there is no ambiguity in terms of what the court could do in order to rectify the error. In other words, it will not rewrite the will, but merely correct it so that it achieves what is apparent on the will what it intended to achieve.

Accordingly, words might be added where you have a number of clauses giving the same type of legacy to a number of beneficiaries, but a typographical error has meant that some words are excluded from one of the clauses which appear in all the other clauses. In the case of *Re Cory* [1955] 2 All ER 630 for example, a testator left his residuary estate to be distributed equally between his four daughters and his son. Each of the daughters was to have a share of the estate for her lifetime, and thereafter the estate was to be given to each daughter's children. The will made it clear that the estate could be divided equally between the testator's grandchildren, and that in the absence of a selection being made, the trustees could decide how to divide the estate. The clause stated that the estate was held 'upon trust for all or such one . . . of the children . . . of such daughter and in default of and subject to any such appointment in trust . . .'. As it is, this clause does not make a great deal of sense – there is reference to what happens in the event of a default (i.e. if something does not happen) but no explanation of what will not

have happened in order for the default provisions to be effective. What was omitted from the clause however was that it was the daughters who were to decide how to divide the estate between their children, and that the trustees could only decide this where one of the daughters had not decided on the distribution of the estate before her death. Accordingly, the court was able to insert into the clause that it was the daughters who were to decide which of the children should receive her estate after her death, so that the clause read 'upon trust for all or such one . . . of the children . . . of such daughter AS SHE SHALL APPOINT and in default of and subject to any such appointment in trust . . .'. Words have also been changed where they have led to ambiguity. Again, this often involves the correction of typographical errors rather than more significant reinterpretations of meaning. Other potential errors for the court to correct are irreconcilable gifts being given in the same will, the residuary estate being disposed of more than once, and gifts of the same subject matter being made twice. Again, the approach taken will depend on the context of the case, and in all likelihood the persuasiveness of the witnesses' evidence. One approach is where the gifts are irreconcilable, the later one is deemed to prevail, although where possible, the court will tend to favour an equal division of the legacy, either as concurrent or consecutive interests.

Where the ambiguity cannot be resolved, then it is likely that a gift will fail for uncertainty of intention, subject matter or beneficiary. If there is a clause in the will dealing with the residue of the deceased's estate, then the failed gift will become part of the residue. If on the other hand there is no residuary clause, or the ambiguity in the construction of the will refers to the residuary clause itself, then the gift will not pass by will, but by the deceased's intestacy.

Secret trusts, mutual wills and *donatio mortis causa*

There are three areas concerning the law of succession which seem to blur the distinction between express trusts and implied trusts. These are secret trusts (and by extension half-secret trusts), mutual wills and *donatio mortis causa*. On the one hand these may be regarded as express trusts in that they are intentionally and voluntarily created. On the other hand, their relationship with express trusts is created because they do not follow the formalities of the Wills Act 1837 concerning the need for trusts that arise on death to be made in writing. Accordingly, it may be argued that their existence is justified because the trustee has placed him- or herself in a situation where it would be inequitable to deny that a trust exists, as is the case with constructive trusts. Whatever one's view may be on this issue, the law nevertheless upholds these types of trusts as being valid, but only in certain prescribed circumstances.

Secret trusts

A secret and a half-secret trust are both trusts that arise behind a will. In relation to a fully secret trust, a testator will write a will naming certain beneficiaries. However, he or she will inform one (or more) of those beneficiaries that the legacy they will receive is to be held on a trust for another person. The will itself does not reveal this trust, and therefore it enables the testator to benefit people he or she might not wish to openly acknowledge.

A half-secret trust is a similar concept. Here the will identifies that property is to be held on a trust, but the beneficiaries are not identified on the face of the will.

Why therefore are secret and half-secret trusts employed? Historically, their significance was to enable people to provide for family members who were not openly acknowledged,

for example mistresses and illegitimate children. Nowadays, this may still be a concern for people in the public eye, such as politicians who may wish to be seen to uphold family values. It may also be useful for people to be able to donate to a particular cause which they may not wish to be seen to associate with, or with which their family may disapprove.

Why are secret trusts and half-secret trusts enforced?

On the face of it, secret and half-secret trusts conflict with the provisions of s.9 Wills Act 1837, which requires the will to be in writing, signed by the testator and witnessed. This will not occur with secret and half-secret trusts. They are therefore upheld because equity will not allow a statute to be an instrument of fraud. A strict interpretation of the Wills Act would enable the secret trustee to take the property absolutely, and deny the secret trust beneficiary what is rightfully his or hers as was shown in *McCormick v Grogan* (1869) LR 4 HL 82. This argument is not valid in relation to half-secret trusts, as it is then obvious that the property is held on trust. Accordingly the other reason given for enforcing secret and half-secret trusts is to ensure that the interests of the beneficiaries are not extinguished, as with *Re Fleetwood* (1880) 15 Ch D 594. Here Hall VC, the settlor, writes his will in a particular manner, or does not revoke because he is relying on the trustee's promise.

Another justification is that a secret trust is not a will trust, it operates outside the will, and is in effect an *inter vivos* trust rather than a trust that arises on death. Accordingly, a beneficiary under a secret trust may even witness a will that ultimately will benefit him – as was seen in *Re Young* [1951] Ch 344 in relation to half-secret trusts. A beneficiary under a will cannot do this, as is provided in s.15 Wills Act 1837.

A different situation might arise if a fully secret trustee attests the will. A fully secret trustee would be caught by the provisions of s.15, because on the face of the will he or she is the beneficiary and therefore the purported legacy to him or her would be invalid. On the other hand, in the case of a half-secret trust it is clear that the person named in the will is a trustee, and therefore it is probable there can be no objection to him or her witnessing the will.

Another problem is what happens if the secret trustee predeceases the testator. According to *Re Maddock* [1902] 2 Ch 220, if a fully secret trustee predeceases the testator, then the gift will lapse and the secret trust will fail because there is no subject matter for the trust, as the subject matter is the purported legacy to the secret trustee. However, because a half-secret trust, in the same way as any other trust, will not be allowed to fail for want of a trustee, the predecease of the half-secret trustee should not affect the trust. One problem however might relate to certainty – how are we to identify the beneficiary if the trustee has died and the testator, although still alive, is unable to communicate this?

What happens if the beneficiary dies before the testator? One authority is the case of *Re Gardner (No 2)* [1923] 2 Ch 230. Here the court was of the opinion that the beneficiary acquires an interest when the trust is created as an *inter vivos* trust. The property will pass to anyone who is entitled to it under the beneficiary's will or intestacy. However, this case is generally accepted to have been wrongly decided, because although the trust has been created, the trust property is not transferred to the trustee until the testator's death. In other words the trust is not fully constituted until the testator's death, and therefore the beneficiary cannot benefit until the trust property has been transferred to the trustee.

The three certainties are also relevant to the institution of the secret and half-secret trust. Again there needs to be certainty of intention (*Kasperbauer v Griffith* [2000] WTLR

333), certainty of subject matter (*Ottaway v Norman* [1972] Ch 698) and certainty of beneficiaries. Certainty of intention is fairly straightforward, but Ottaway suggests that subject matter could be more problematic as a residue of what the trustee did not herself use could validly be the subject of the trusts. This turned on the facts of the case, but in practical terms, it is rare for a secret trust to operate on this basis. No cases have addressed beneficiaries, and therefore it is presumed that the same rules apply as with all other trusts.

Communication of trust – secret trusts

The testator must, before his or her death ask the legatee to hold the property on trust for a third party, as was shown in *Wallgrave v Tebbs* (1855) 2 K & J 313. This can take place before or after the execution of the will however. Nevertheless communication by letter received after the death of the testator is not sufficient as this does not give the legatee the opportunity to refuse to act. However, although the existence of the trust must be communicated before the testator's death, its precise terms (e.g. the identity of the beneficiaries) can remain a secret. However, it seems that the communication needs to be in the possession of the trustee before the settlor's death, or that he or she knows where to find it (e.g. in the form of a sealed envelope that has been given to the trustee or one that he or she has been told where to find, as with *Re Keen* [1937] Ch 236). In the case of *Re Boyes* (1884) 26 Ch D 531 however, the letter communicating the precise terms of the trust were not found until after the testator's death. Communication of the intended beneficiaries' identity was not held to have been validly made and the trust failed for uncertainty of objects.

The question of who receives the communication is also important where there are multiple trustees, and communication is only made to some of them. If the property is transferred to the trustees as tenants in common, then those who have not been told about the trust will not be bound by it, as is shown in *Tee v Ferris* (1856) 2 K & J 357. This is also true in relation to property that is to be held by the trustees as a joint tenancy, if communication occurs after the will has been written – the authority here is *Moss v Cooper* (1861) 1 John & H 352. If communication of the trust to the trustees occurs before the will is written, all the trustees will be bound even if communication of the trust was only made to some trustees – *Re Stead* [1900] 1 Ch 237. The reason for this is that where the trustees do not accept the obligation until after the will is made, their promise has not induced the will to be written. Where the promise is made before the will is made, then it may be argued that it was the trustee's promise (on behalf of themselves and others) that induced the testator to draw up his or her will in the way that he or she did.

Communication – half-secret trusts

In relation to half-secret trusts on the other hand, the testator must ask the intended trustee to hold the legacy on trust for a third party before or contemporaneously with the making of the will. This is based on the view of the courts in *Blackwell v Blackwell* [1929] AC 318, *Re Keen* [1937] Ch 236 and *Re Bateman's Will Trusts* [1970] 1 WLR 1463. A further requirement in relation to half-secret trusts is that the form of communication made must not be contrary to the express provisions of the will. In *Re Keen*, the testator left £10,000 to two persons '*to be held on trust and disposed of them to such person . . . as may be notified by me to them or either of them during my lifetime*'. Before executing the will, the testator handed a sealed envelope to the legatees, which contained the name of the beneficiary which was not to be opened until after the testator's death. The Court of

Appeal held that the will provided that communication of the beneficiary's identity should occur in the future, i.e. after execution of the will, whereas by his actions the testator had communicated the identity of the beneficiary before executing the will. In this case however, communication in accordance with the will, i.e. after execution, would have been ineffective as communication before execution of the will is required. It appears from *Re Bateman* that the terms of the trust must be communicated before the date of the will, and not merely the fact of its existence. A similar scenario can be seen in the case of *Re Spence* [1949] WN 237. Here the will suggested that the testator would have communicated his intention to all the legatees, whereas in fact his intention had only been communicated to some of them. Again, the trust failed. As with secret trusts, if communication of the trust is only made to some of the trustees, then if they are tenants in common, the ones who have not been informed will not be bound. If they are joint tenants, acceptance by one will bind them all.

Finally, it is necessary to consider what happens if the fully secret or the half-secret trust fails. It is clear on the will that there was no intention for the half-secret trustee to acquire the property beneficially. This means that it will revert back to the testator's estate.

In relation to a fully secret trust, it will depend on whether the legatee knows that he or she is to hold the property on trust. As has been shown, this does not need to be communicated before executing the will, provided it is communicated before the testator's death. As in the case of *Re Boyes* therefore, the legatee knew that he was supposed to hold the property on trust. When the trust failed, the legatee held the property on a resulting trust for the testator's estate. However if at the time of the testator's death, the legatee has not been informed that he is to hold the property on trust, then he will take the property absolutely.

Mutual wills

A particularly knotty problem in the context of wills is the law relating to mutual wills. A mutual will arises where two people write wills leaving their joint estate to an agreed third party, such as where a husband and wife agree to leave their estate to their child. Each writes a will to this leaving their estate to the other, with a proviso that after the spouse's death, the joint estate of husband and wife will be given to the child. Therefore, John writes a will leaving his estate to his wife Jane, and specifying that should Jane predecease him, the estate will go to John and Jane's daughter Mary on John's death. Jane writes an identical will. John dies, and his entire estate passes to Jane. On Jane's death, provided that Jane does not revoke her will, Jane (and John's) estate will pass to Mary. The problem for the law to resolve therefore is whether Jane is permitted to revoke her will after John's death, and if so, what should happen to her estate on her death – should it pass to Mary under the terms of the original will, which Jane agreed not to revoke, or should it pass under the terms of her new will?

The law's solution to this problem has been to identify a trust as having been created when the will is made. Accordingly, if a mutual will is revoked by one of the parties after the death of the other, those who inherit under the later will, or the survivor's intestacy, will stand as trustees for the original beneficiary. However, clear evidence is needed of the intention to create a mutual will, and it is rare that cases where a mutual will is alleged have been upheld. In the case of *Ollins v Walters* [2007] EWHC 3060 (Ch), Norris J emphasises the need for there to be a contractual agreement between the two testators that they will not revoke their wills in order for the courts to construe that the will constitutes a lifetime *inter vivos* constructive trust, as well as a trust that arises on death:

> In my judgement its irreducible core is that there must be a contract between T1 and T2 that in return for T1 agreeing to make a will in form X and not to revoke it without notice to T2, then T2 will make a will in form Y and agree not to revoke it without notice to T1. If such facts are established then upon the death of T1 equity will impose upon T2 a form of constructive trust (shaped by the exact terms of the contract that T1 and T2 have made). The constructive trust is imposed because T1 has made a disposition of property on the faith of T2's promise to make a will in form Y, and with the object of preventing T1 from being defrauded. So much is established by *Re Dale* [1994] Ch 31, [1993] 4 All ER 129, [1993] 3 WLR 652 in passages from the judgement of (and citations by) Morritt J at pp 38B–C and D–E, 41A-B, 41H–42B, 46E, and 48E–49B. There is no need to refer to the decisions that precede *Re Dale*, but I should refer to *Re Goodchild* [1997] 3 All ER 63, [1997] 3 FCR 601, [1997] 1 WLR 1216 for its confirmation of the need (a) for an underlying contract (at p 1224E–G per Leggatt LJ and at 1229C–E per Morritt LJ) and (b) for agreement on the irrevocability of the intended disposition after the death of the first to die (at p 1225F-G per Leggatt LJ). (In my formulation, and particular by the use of the expression 'a form of constructive trust', I have tried to avoid entering upon the controversy of whether the trust is a 'floating trust' during the survivorship of T2 and a more conventional constructive trust only upon the death of T2: for this point is not in the event material to the case I have to decide).

The concept of the mutual wills is problematic in the law of trusts because on the one hand it is a form of trust that deals with the distribution of property on death. However, if that is the case, the survivor is entitled to revoke the will at any point before their death. On the other hand, if the mutual will is a form of *inter vivos* trust, then it is an incomplete trust in that there is no intention for the subject matter of the trust to be transferred until the testator dies. Furthermore, the concept of the mutual will is problematic because it cannot easily be classified either as an express trust or as an implied trust. On the one hand, there is a clear manifestation of an intention to create a trust in the will document – it cannot therefore be said to be a trust that arises because it would be inequitable to deny its existence. On the other hand, necessity requires the trust to be constructive, because once the will has been revoked, there is no intention to confer a benefit on the original beneficiary, and therefore the law only imposes a trust because otherwise it would be inequitable to allow the surviving testator to revoke his or her will, when this opportunity was not available to the deceased testator.

Donatio mortis causa

Another area of the law that fails to fit neatly into textbook categorisations is the concept of *donatio mortis causa*. A *donatio mortis causa* is a lifetime gift made in contemplation of death. However, the gift only takes effect in the event of the donor's death. In one sense therefore, a *donatio mortis causa* has the attributes of a lifetime trust. However, the fact that is contingent upon the donor's death means that it also shares the attributes of a will. It is also necessary for the gift to be given to the donee – if there is no transfer of the property, there can be no valid *donatio mortis causa*. *Donatio mortis causa* is often problematic for the law for a number of reasons. Firstly, there is the problematic issue that the only evidence of the donation is likely to come from the donee him- or herself. Much therefore depends on the donee's credibility. Secondly, the concept of *donatio mortis causa* interferes with the law's need for formality – the requirements of s.9 of the Wills Act 1837 for example do not need to be complied with, with the result that although

the Wills Act was enacted as a means of preventing fraud, the allowance of *donatio mortis causa* undermines this in a significant way. What is also problematic is that *donatio mortis causa* undermines a lot of the law's other formalities. The transfer of land usually needs to be by deed, and the creation of a trust over land must be in writing – Law of Property Act 1923, s.53 – the only exception being the constructive trust. However, given that there is a deliberate manifestation of an intention, coupled by a deliberate transfer of the trust property to a specific beneficiary, it is difficult to see how a *donatio mortis causa* might be regarded as a constructive trust. It is therefore surprising that *donationes mortis causa* continue to be upheld. Nevertheless, where there is clear evidence that a donation was made, the courts cannot easily dismiss its existence.

Inheritance (Provision for Family and Dependants) Act 1975

Despite these rules on wills and intestacy, it may also be possible to make a claim against a deceased person's estate on the basis that his or her will or the terms of intestacy does not make reasonable financial provision for family and dependants on the deceased's death. This is governed by the Inheritance (Provision for Family and Dependants) Act 1975 (IPFDA).[31] On intestacy, family members are likely to benefit under the intestacy rules. However, they may be prevented from inheriting because of another person having a prior claim. For example, the amount one's children may inherit may be limited (or excluded entirely when the deceased's estate is comparatively small) by the existence of a surviving spouse. However, one's spouse may be wealthy in their own right, whereas one's children (not necessarily the children of the wealthy spouse if the intestate person remarried before death) may be poorer. Similarly, dependants may not be one's family members and may include cohabitants, children of the family or former spouses. The persons entitled to claim are the deceased's spouse, former spouses who have not remarried, children, children of the family (e.g. stepchildren), cohabitants and other persons who may have been dependent on the deceased. The court can make orders allowing for payments to be made either on a periodical basis or as a lump sum, as well as ordering the transfer or acquisition of property (IPFDA, s.2), and the court has the power to decide how to divide the estate between those entitled under the Act, and those entitled under the terms of the deceased's will or the intestacy rules – s.2(4).

The law of succession is therefore a fascinating and multifaceted area of the law. It places great significance on social expectations regarding who ought to benefit from a deceased person's estate, but nevertheless allows the testator to circumvent these. Nevertheless, the law of wills is often an extremely contentious area of litigation, and often results in families being split because some members dispute the entitlement of others, or of perceived outsiders, to inherit.

[31] (1975 c.63).

Chapter summary

This chapter may be useful for assignments and assessments on:

- Express trusts and constructive trusts
- Succession
- The validity of wills.

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16

Commercial trusts

Chapter outline

This chapter will cover:

- Securing customers' payments
- Ring-fencing company assets
- Fiduciary duties
- Loans
- Retention of title clauses
- Intermediaries in arm's-length transactions
- Solicitors' clients' accounts
- Employee incentives.

Introduction

Earlier we dealt primarily with trusts in a domestic context and their significance for families and couples. This (and the following) chapter will consider some of the primary commercial uses of the trust. Trusts have become increasingly common in commercial contexts. In the past there was a great deal of reluctance to use the trust in commercial contexts, with the lack of certainty inherent in a trust being cited as the main objection. There was a tendency to view equity as being primarily remedial, and therefore the restitutionary focus of equity, and the finding of a trust where otherwise there would be inequity, was viewed as being in conflict with the need for certainty in commercial transactions, and the perceived importance of giving effect to what the parties agreed. Gradually however it was acknowledged that a trust is not solely remedial in focus, and that the agreement to hold property under a trust can be just as much the subject of negotiation and precise requirements as a contract. More recently it has been recognised that trusts do not equate with uncertainty, and that they may be used in a myriad of different ways to protect commercial property.

EXTRACT

Millett, P.J. (1998) 'Equity's Place in the Law of Commerce' *Law Quarterly Review* 214

Even twenty years ago there was still a widely held belief, by no means confined to common lawyers, that equity had no place in the world of commerce. Businessmen need speed and certainty; these do not permit a detailed and leisurely examination of the parties' conduct. Commerce needs the kind of bright line rules which the common law provides and which equity abhors. Resistance to the intrusion of equity into the business world is justified by concern for the certainty and security of commercial transactions. Such considerations led Lindley L.J. over a century ago to give his well-known warning against the extension of the equitable doctrine of constructive notice to commercial transactions. This is often repeated like a mantra. But it is inaccurate and its influence has been harmful. The purchase of land and the giving of a bank guarantee are both commercial transactions; yet the doctrine of constructive notice applies to both. In fact Lindley L.J. was speaking of the doctrine of constructive notice as it was developed by the Court of Chancery in relation to land . . .

When the question is concerned with the imposition of fiduciary duties, the distinction is not between commercial and non-commercial transactions, a distinction which Lehane has described as 'a red herring', but between commercial and non-commercial relationships.

It is of course far too late to suppose that the body of law which owes its origin to family and friendship cannot be introduced into the market place without making some kind of category mistake. It is no longer possible to dispute Sir Anthony Mason's extrajudicial observation that the concepts, doctrines, principles and remedies developed by the old Court of Chancery

> 'have extended beyond the old boundaries into new territory where no Lord Chancellor's foot has previously left its imprint . . . Equitable doctrines and reliefs have penetrated the citadels of business and commerce long thought, at least by common lawyers, to be immune from the intrusion of such principles.'

Three things have combined to bring about this development. First, there is the growing complexity and professionalisation of commercial life which have accompanied the change

from an industrial to a service economy and the growth of the financial services industry. Much commerce today is based on trust; on each side of a commercial arms' length transaction there are likely to be relationships of trust and confidence. As a result, the modern fiduciary is usually a professional. He expects to be paid for his services, and he expects to be liable (and to be covered by appropriate insurance) if he performs his duties negligently. The picture of the trustee or fiduciary as an old friend of the family who has gratuitously volunteered his services is long obsolete. Principles of equity designed to mitigate the severity of its rules as they bore on the well-meaning amateur are incongruous when applied to the paid professional.

We ought to stop repeating the inaccurate incantation that equity does not permit a trustee to profit from his trust. Of course it does. What it forbids is his making a secret or uncovenanted profit from his trust. We also need to reconsider the propriety of including the standard form of trustee exemption clause which exempts the trustee from liability for loss or damage not caused by his own dishonesty. The view is widely held that these clauses have gone too far, and that trustees who charge for their services and who, as professional men, would not dream of excluding liability for ordinary professional negligence, should not be able to rely on a trustee exemption clause which excludes liability for gross negligence. Jersey introduced a law in 1989 which denies effect to a trustee exemption clause which purports to absolve a trustee from liability for his own 'fraud, wilful misconduct or gross negligence'. The subject is presently under consideration in this country by the Trust Law Committee under the chairmanship of Sir John Vinelott and its proposals will be awaited with interest.

Secondly, there has never been a greater need to impose on those who engage in commerce the high standards of conduct which equity demands. The common law insists on honesty, diligence, and the due performance of contractual obligations. But equity insists on nobler and subtler qualities: loyalty, fidelity, integrity, respect for confidentiality, and the disinterested discharge of obligations of trust and confidence. It exacts higher standards than those of the market place, where the end justifies the means and the old virtues of loyalty, fidelity and responsibility are admired less than the idols of 'success, self-interest, wealth, winning and not getting caught'. It is unrealistic to expect that employees can be given incentives through enormous bonuses without undermining their business ethics. It is hardly necessary to say more on this subject in a year in which we have seen employees in the financial services industry, enticed by the prospect of even larger bonuses, threaten not only to leave their employer for a competitor but to take their entire teams of junior staff with them; and in which we have seen a takeover bidder make use, possibly of stolen documents, but certainly of confidential information belonging to the target company, with major City firms apparently regarding such conduct as acceptable.

Thirdly, plaintiffs and their advisers have discovered the apparent advantages of alleging breach of trust or fiduciary duty, with the result that a statement of claim is considered to be seriously deficient if it does not contain inappropriate references to these concepts which are often scattered throughout the pleadings with complete abandon.

At first equity lawyers looked with disdain at their common law colleagues who were obviously using equitable concepts without any understanding of their proper scope. More recently, however, we have been challenged to define these expressions, and to our dismay have realised that we cannot agree on their meanings. We have been forced to re-examine our terminology and reconsider our own concepts. The process is a continuing one and is marked by considerable controversy. It has, however, been greatly assisted by a number of academic monographs on particular concepts such as subrogation, fiduciary obligations, and constructive and resulting trusts, which are required reading for anyone seriously interested in the concepts on which the development of equity into the next century depends.

At one level of course, the trust is used in commercial contexts in exactly the same way as in a domestic relationship. Commercial partners may co-own land and other assets in just the same way as domestic partners. Accordingly, trusts such as those imposed by s.34 and s.36 Law of Property Act 1925 will affect commercial co-owners in precisely the same way as domestic co-owners, and the discussion of the rules relating to trusts of land under the Trusts of Land and Appointment of Trustees Act 1996 will be applicable to commercial land just as much as to domestic land.

Nevertheless, there has been an increasing recognition of the usefulness of trusts in a commercial setting in ways that are distinct from domestic trusts for a number of reasons.

- providing a fund for customers in the event of a company going into administration;
- ring-fencing company assets;
- explaining the nature of the duties owed by a company director to the company;
- providing loans;
- allowing businesses to retain title to goods until payment has been received;
- providing a trusted intermediary in arm's-length transactions;
- enabling solicitors and others to hold money for their clients in conveyancing transactions and the administration of estates;
- employee incentives such as pensions.

In this chapter therefore, the operation of the trust in a purely commercial context will be considered.

Providing funds for customers

A number of cases have demonstrated that where a company is concerned about the likelihood of it going into administration, it may decide to create a trust of customers' money in order to ensure that the customers may be repaid in the event that the company does go into administration. The original authority for this principle is *Barclays Bank Ltd v Quistclose Investments Ltd* [1970] AC 567. However, a similar approach was taken in the case of *Re Kayford* [1975] 1 All ER 604.

EXTRACT

Barclays Bank Ltd v Quistclose Investments Ltd [1970] AC 567

Case facts

A company named Rolls Razor was in financial difficulties, but succeeded in making an arrangement for further finances, provided that Rolls Razor could raise £209,719 8s 6d to pay a dividend to the shareholders. Rolls Razor proposed to fulfil this requirement by obtaining a loan from Quistclose Investments. The loan was issued, and paid into a separate account at Barclays Bank. Barclays Bank was aware of the fact that this money was a loan, and that its purpose was to pay a dividend to the shareholders. Before the dividend was paid however, Rolls Razor went into liquidation. The respondents sought to claim the money back arguing

that it was held on a resulting trust for them because the purpose of the loan (the payment of the dividend) had not been fulfilled. The appellants argued however that Quistclose Investments were merely an unsecured creditor, and would therefore only be repaid if there were sufficient funds remaining after all the other prior creditors had been repaid.

Lord Wilberforce

Two questions arise, both of which must be answered favourably to the respondents if they are to recover the money from the bank. The first is whether as between the respondents and Rolls Razor Ltd. the terms upon which the loan was made were such as to impress upon the sum of £209,719 8s. 6d. a trust in their favour in the event of the dividend not being paid. The second is whether, in that event, the bank had such notice of the trust or of the circumstances giving rise to it as to make the trust binding upon them.

It is not difficult to establish precisely upon what terms the money was advanced by the respondents to Rolls Razor Ltd. There is no doubt that the loan was made specifically in order to enable Rolls Razor Ltd. to pay the dividend. There is equally, in my opinion, no doubt that the loan was made only so as to enable Rolls Razor Ltd. to pay the dividend and for no other purpose. This follows quite clearly from the terms of the letter of Rolls Razor Ltd. to the bank of July 15, 1964, which letter, before transmission to the bank, was sent to the respondents under open cover in order that the cheque might be (as it was) enclosed in it. The mutual intention of the respondents and of Rolls Razor Ltd., and the essence of the bargain, was that the sum advanced should not become part of the assets of Rolls Razor Ltd., but should be used exclusively for payment of a particular class of its creditors, namely, those entitled to the dividend. A necessary consequence from this, by process simply of interpretation, must be that if, for any reason, the dividend could not be paid, the money was to be returned to the respondents: the word 'only' or 'exclusively' can have no other meaning or effect.

That arrangements of this character for the payment of a person's creditors by a third person, give rise to a relationship of a fiduciary character or trust, in favour, as a primary trust, of the creditors, and secondarily, if the primary trust fails, of the third person, has been recognised in a series of cases over some 150 years.

In *Toovey v. Milne* (1819) 2 B. & A. 683 part of the money advanced was, on the failure of the purpose for which it was lent (viz, to pay certain debts), repaid by the bankrupt to the person who had advanced it. On action being brought by the assignee of the bankrupt to recover it, the plaintiff was non suited and the non suit was upheld on a motion for a retrial. In his judgment Abbott C.J. said, at p. 684:

> 'I thought at the trial, and still think, that the fair inference from the facts proved was that this money was advanced for a special purpose, and that being so clothed with a specific trust, no property in it passed to the assignee of the bankrupt. Then the purpose having failed, there is an implied stipulation that the money shall be repaid. That has been done in the present case; and I am of opinion that that repayment was lawful, and that the non suit was right.'

The basis for the decision was thus clearly stated, viz., that the money advanced for the specific purpose did not become part of the bankrupt's estate. This case has been repeatedly followed and applied: see *Edwards v. Glynn* (1859) 2 E. & E. 29; *In re Rogers, Ex parte Holland and Hannen* (1891) 8 Morr. 243; *In re Drucker (No. 1)* [1902] 2 K.B. 237; *In re Hooley, Ex parte Trustee* [1915] H.B.R. 181. *In re Rogers*, 8 Morr. 243 was a decision of a strong Court of Appeal. In that case, the money provided by the third party had been paid to the creditors before the bankruptcy. Afterwards the trustee in bankruptcy sought to recover it. It was held that the money was advanced to the bankrupt for the special purpose of enabling his creditors to be paid, was

impressed with a trust for the purpose and never became the property of the bankrupt. Lindley L.J. decided the case on principle but said (at p. 248) that if authority was needed it would be found in *Toovey v. Milne*, 2 B. & A. 683 and other cases. Bowen L.J. said (8 Morr. 243, 248) that the money came to the bankrupt's hands impressed with a trust and did not become the property of the bankrupt divisible amongst his creditors, and the judgment of Kay L.J., at p. 249, was to a similar effect.

These cases have the support of longevity, authority, consistency and, I would add, good sense. But they are not binding on your Lordships and it is necessary to consider such arguments as have been put why they should be departed from or distinguished.

It is said, first, that the line of authorities mentioned above stands on its own and is inconsistent with other, more modern, decisions. Those are cases in which money has been paid to a company for the purpose of obtaining an allotment of shares (see *Moseley v. Cressey's Co.* (1865) L.R. 1 Eq. 405; *Stewart v. Austin* (1866) L.R. 3 Eq. 299; *In re Nanwa Gold Mines Ltd.* [1955] 1 W.L.R. 1080). I do not think it necessary to examine these cases in detail, nor to comment on them, for I am satisfied that they do not affect the principle on which this appeal should be decided. They are merely examples which show that, in the absence of some special arrangement creating a trust (as was shown to exist in *In re Nanwa Gold Mines Ltd.*), payments of this kind are made upon the basis that they are to be included in the company's assets. They do not negative the proposition that a trust may exist where the mutual intention is that they should not.

The second, and main, argument for the appellant was of a more sophisticated character. The transaction, it was said, between the respondents and Rolls Razor Ltd., was one of loan, giving rise to a legal action of debt. This necessarily excluded the implication of any trust, enforceable in equity, in the respondents' favour: a transaction may attract one action or the other, it could not admit of both.

My Lords, I must say that I find this argument unattractive. Let us see what it involves. It means that the law does not permit an arrangement to be made by which one person agrees to advance money to another, on terms that the money is to be used exclusively to pay debts of the latter, and if, and so far as not so used, rather than becoming a general asset of the latter available to his creditors at large, is to be returned to the lender. The lender is obliged, in such a case, because he is a lender, to accept, whatever the mutual wishes of lender and borrower may be, that the money he was willing to make available for one purpose only shall be freely available for others of the borrower's creditors for whom he has not the slightest desire to provide.

I should be surprised if an argument of this kind – so conceptualist in character – had ever been accepted. In truth it has plainly been rejected by the eminent judges who from 1819 onwards have permitted arrangements of this type to be enforced, and have approved them as being for the benefit of creditors and all concerned. There is surely no difficulty in recognising the co-existence in one transaction of legal and equitable rights and remedies: when the money is advanced, the lender acquires an equitable right to see that it is applied for the primary designated purpose (see *In re Rogers*, 8 Morr. 243 where both Lindley L.J. and Kay L.J. recognised this): when the purpose has been carried out (i.e., the debt paid) the lender has his remedy against the borrower in debt: if the primary purpose cannot be carried out, the question arises if a secondary purpose (i.e., repayment to the lender) has been agreed, expressly or by implication: if it has, the remedies of equity may be invoked to give effect to it, if it has not (and the money is intended to fall within the general fund of the debtor's assets) then there is the appropriate remedy for recovery of a loan. I can appreciate no reason why the flexible

interplay of law and equity cannot let in these practical arrangements, and other variations if desired: it would be to the discredit of both systems if they could not. In the present case the intention to create a secondary trust for the benefit of the lender, to arise if the primary trust, to pay the dividend, could not be carried out, is clear and I can find no reason why the law should not give effect to it.

I pass to the second question, that of notice. I can deal with this briefly because I am in agreement with the manner in which it has been disposed of by all three members of the Court of Appeal. I am prepared, for this purpose, to accept, by way of assumption, the position most favorable to the bank, i.e., that it is necessary to show that the bank had notice of the trust or of the circumstances giving rise to the trust, at the time when they received the money, viz., on July 15, 1964, and that notice on a later date, even though they had not in any real sense given value when they received the money or thereafter changed their position, will not do. It is common ground, and I think right, that a mere request to put the money into a separate account is not sufficient to constitute notice. But on July 15, 1964, the bank, when it received the cheque, also received the covering letter of that date which I have set out above: previously there had been the telephone conversation between Mr. Goldbart and Mr. Parker, to which I have also referred. From these there is no doubt that the bank was told that the money had been provided on loan by a third person and was to be used only for the purpose of paying the dividend. This was sufficient to give them notice that it was trust money and not assets of Rolls Razor Ltd.: the fact, if it be so, that they were unaware of the lender's identity (though the respondent's name as drawer was on the cheque) is of no significance. I may add to this, as having some bearing on the merits of the case, that it is quite apparent from earlier documents that the bank were aware that Rolls Razor Ltd. could not provide the money for the dividend and that this would have to come from an outside source and that they never contemplated that the money so provided could be used to reduce the existing overdraft. They were in fact insisting that other or additional arrangements should be made for that purpose. As was appropriately said by Russell L.J., ([1968] Ch. 540, 563F) it would be giving a complete windfall to the bank if they had established a right to retain the money.

In my opinion, the decision of the Court of Appeal was correct on all points and the appeal should be dismissed.

EXTRACT

Re Kayford [1975] 1 All ER 604

Case facts

Kayford was a mail-order business in financial difficulties. It was advised that in order to protect the customers' money in the event that the company became insolvent, it should open a separate bank account called a 'customers' trust deposit account'. Money received from customers should be paid into this account, which would mean that it could be repaid to the customers if Kayford went into liquidation. However, the managing director did not follow this advice. Instead, he put the customers' money into an existing account in the company's name, but the day after the company resolved to go into liquidation, it sent a letter to the bank requesting that the name of the account be changed to 'customer trust deposit account'. The question for the court was whether a trust had been created for the benefit of the customers.

Megarry J

This case arises on a summons taken out on 10 October 1973 by the joint liquidators of Kayford Ltd which is in voluntary liquidation: I shall call it 'the company'. The summons relates to a sum of £37,872.45, with interest thereon, standing to the credit of the company in a deposit account at a bank. A further £47.80, with interest thereon, is also in that bank account. The company carried on a mail-order business in bedding quilts, stretch covers for chairs and so on. The customers either paid the full price in advance, or paid a deposit. In January 1972 the company was experiencing difficulties in getting supplies, and it entered into an arrangement with a manufacturing company named Monaco Manufacturing (Household Textiles) Ltd, which I shall call 'Monaco'.

After an advertising campaign by the company in August 1972, similar to previous campaigns, money came in for goods, but the company found itself unable to obtain supplies to meet all the orders. By November 1972 Monaco, which by then was the company's chief supplier, was in serious difficulties, after the company had already provided financial support to Monaco to the extent of some £80,000. Mr Kay, the managing director of the company, was becoming concerned for the customers of the company who had sent and were sending money for goods. On 22 November Monaco told the company that Monaco would have to go into liquidation unless it received further financial support. If this happened it would affect not only the company's ability to deliver the goods but also its solvency. The next day, 23 November, Mr Kay saw the company's accountants, who advised him to consult accountants specialising in matters of insolvency; and the same day Mr Wainwright of such a firm was consulted. He advised that a separate bank account should be opened by the company, to be called a 'Customers' Trust Deposit Account', and that all further moneys paid by customers for goods not yet delivered should be paid into this account and withdrawn only when the goods had been delivered. The object of doing this was so that if the company had to go into liquidation, these sums of money could and would be refunded to those who had paid them. This advice was accepted. On Monday, 27 November, Mr Kay gave instructions to the bank manager by telephone. He and the manager agreed that a dormant deposit account in the company's name, with £47.80 to its credit, should be used for this purpose: and this was done. The £37,872.45 with which I am concerned consists of money thus received, together with the interest on it.

There is not much more to relate. On 6 December Monaco ceased to make deliveries. On 8 December Mr Kay saw the company's solicitors to consider putting the company into liquidation. On 11 December he saw Mr Wainwright, who then discovered that his advice had not been precisely carried out. Mr Wainwright suggested that Mr Kay should at once write to the bank confirming the oral arrangements that had been made; and on 12 December Mr Kay did this. On the day before, 11 December, the company had resolved to go into voluntary liquidation, and meetings were convened for 9 January 1973.

The question for me is whether the money in the bank account (apart from the dormant amount of £47.80 and interest on it), is held on trust for those who paid it, or whether it forms part of the general assets of the company. Counsel for the joint liquidators, one of whom is in fact Mr Wainwright, has contended that there is no trust, so that the money forms part of the general assets of the company and so will be available for the creditors generally. On the other hand, there is a Mr Joels, who on 12 December paid the company £32.20 for goods which have not been delivered; and counsel for him seeks a representation order on behalf of all others whose moneys have been paid into the bank account, some 700 or 800 in number. I make that order. Counsel for the representative beneficiary, of course, argued for the existence of an effective trust. I may say at the outset that on the facts of the case counsel for the joint liquidators was unable to contend that any question of a fraudulent preference arose. If one leaves on one side any case in which an insolvent company seeks to declare a trust in favour of

creditors, one is concerned here with the question not of preferring creditors but of preventing those who pay money from becoming creditors, by making them beneficiaries under a trust. I should add that I had some initial doubts about whether Mr Joels was the most suitable representative beneficiary, in view of the date when he paid his money, and whether counsel for the joint liquidators, in representing Mr Wainwright (as well as the other joint liquidator), was not to some degree committed to arguing against the efficacy of the course that Mr Wainwright had advised; but discussion has allayed these doubts.

Now there are clearly some loose ends in the case. Mr Kay, advised to establish a 'Customers' Trust Deposit Account', seems to have thought that it did not matter what the account was called so long as there was a separate account; and so the dormant deposit account suggested by the bank manager was used. The bank statement for this account is before me, and on the first page, for which the title is simply 'Deposit account Kayford Limited', nearly £26,000 is credited. The second and third pages have the words 'Customer Trust Deposit account' added after the previous title of the account; and Mr Joels's payment was made after these words had been added. Mr Kay also left matters resting on a telephone conversation with the bank manager until he wrote his letter of 12 December to the bank. That letter reads: 'We confirm our instructions regarding the opening of the Deposit account for customer deposits for new orders'; and he then makes some mention of other accounts with the bank. The letter goes on: 'Please ensure the Re-opened Deposit account is titled "Customer Trust Deposit account".' Then he gives the reference number and asks for confirmation that this has been done. Nevertheless, despite the loose ends, when I take as a whole the affidavits of Mr Wainwright, Mr Kay and Mr Hall (the bank manager) I feel no doubt that the intention was that there should be a trust. There are no formal difficulties. The property concerned is pure personalty, and so writing, though desirable, is not an essential. There is no doubt about the so-called 'three certainties' of a trust. The subject-matter to be held on trust is clear, and so are the beneficial interests therein, as well as the beneficiaries. As for the requisite certainty of words, it is well settled that a trust can be created without using the words 'trust' or 'confidence' or the like: the question is whether in substance a sufficient intention to create a trust has been manifested.

In *Re Nanwa Gold Mines Ltd* [[1955] 3 All ER 219] the money was sent on the faith of a promise to keep it in a separate account, but there is nothing in that case or in any other authority that I know of to suggest that this is essential. I feel no doubt that here a trust was created. From the outset the advice (which was accepted) was to establish a trust account at the bank. The whole purpose of what was done was to ensure that the moneys remained in the beneficial ownership of those who sent them, and a trust is the obvious means of achieving this. No doubt the general rule is that if you send money to a company for goods which are not delivered, you are merely a creditor of the company unless a trust has been created. The sender may create a trust by using appropriate words when he sends the money (though I wonder how many do this, even if they are equity lawyers), or the company may do it by taking suitable steps on or before receiving the money. If either is done, the obligations in respect of the money are transformed from contract to property, from debt to trust. Payment into a separate bank account is a useful (though by no means conclusive) indication of an intention to create a trust, but of course there is nothing to prevent the company from binding itself by a trust even if there are no effective banking arrangements.

Accordingly, of the alternative declarations sought by the summons, the second, to the effect that the money is held in trust for those who paid it, is in my judgment the declaration that should be made. I understand that questions may be raised as to resorting to the interest on the moneys as a means of discharging the costs of the summons; on that I will, of course, hear argument. I should, however, add one thing. Different considerations may perhaps arise in relation to trade creditors; but here I am concerned only with members of the public, some of

whom can ill afford to exchange their money for a claim to a dividend in the liquidation, and all of whom are likely to be anxious to avoid this. In cases concerning the public, it seems to me that where money in advance is being paid to a company in return for the future supply of goods or services, it is an entirely proper and honourable thing for a company to do what this company did, on skilled advice, namely, to start to pay the money into a trust account as soon as there begin to be doubts as to the company's ability to fulfil its obligations to deliver the goods or provide the services. I wish that, sitting in this court, I had heard of this occurring more frequently; and I can only hope that I shall hear more of it in the future.

However, it appears that, although the courts were willing to countenance such trusts being created in these cases, there has been an increasing realisation that they may be problematic. Desirable though it may be to ensure that a company's customers do not suffer from the non-delivery of the goods they have ordered, if the company goes into administration, it does mean that customers are put in a preferential position over other creditors. Furthermore, what the courts have discovered is that it is sometimes difficult to identify that a trust has been created – there may be uncertainty as to the fact that a trust was intended, and uncertainty as to the subject matter of the trust. Therefore unlike the cases of *Barclays Bank v Quistclose Investments*, and *Re Kayford*, in the case of *Re Goldcorp Exchange* [1995] 1 AC 74, no trust was found to have been created because there was no certainty as to the subject matter of the trust. In *Re Farepak Food and Gifts* [2006] All ER (D) 265 the uncertainty arose because there was no clear intention that the company's directors had intended to create a trust, and what property was to be the subject of the trust. Accordingly, in the *Farepak* case, no trust was identified.

EXTRACT

Re Farepak Food and Gifts [2006] All ER (D) 265

Case facts

Farepak was a Christmas savings scheme, whereby people paid money to agents, in order to save up to buy hampers and gifts for Christmas. The company was in financial difficulties, and therefore, in the three days before the company went into administration, its directors sought to ring-fence the money the customers had paid into the fund. A trust document was created, but the document mistakenly identified the wrong account as being the subject matter of the trust. A further difficulty was that there was ambiguity in the trust document regarding who exactly the purported beneficiaries of the trust were.

Mann J

The basis on which it is submitted that moneys be returned to customers is that the moneys are held on trust for them, or if they are not then the rule in *ex parte James* [[1803–13] All ER Rep 78] is relied on. The trust is said to arise from three possible sources:

- A *Quistclose* resulting trust (*Barclays Bank v Quistclose Ltd* [1970] AC 567, [1968] 3 All ER 651, [1968] 3 WLR 1097; *Twinsectra Ltd v Yardley* [2002] UKHL 12, [2002] 2 AC 164, [2002] 2 All ER 377).
- A constructive trust arising out of the unconscionability of retaining customer moneys received after the decision to cease trading and the attempts to stop receipt of customer moneys.
- The express declaration of trust, or an implied declaration arising out of the related facts.

I shall deal with those claims in turn. However, before doing so I need to deal with the basis on which moneys were received by the Agents, because it has a potentially important bearing on all ways in which the trust claim is sought to be maintained . . .

The *Quistclose* trust

Mr Trace argued this point. He argued that an analysis of the facts and the customer conditions showed that there was a payment for a specific purpose, and that since that purpose had not been fulfilled the customer money was held on resulting trust. The purpose in question was the provision of vouchers (or other products elected by the customer). So far as the customer conditions are concerned he relied on a term which provided that payments must be 'completed in full' before any entitlement arose, and that as between categories of goods ordered the payment would be allocated in a given priority – first vouchers, the frozen hampers, then grocery hampers and so on down the line. He pointed out that if the price were altered the customer has the right to the return of the contributions in full, and the same was true if there were a substitution.

This argument, if good, would work to the theoretical benefit of all customers of Farepak in the 2006 Farepak year, and not just those whose payments were received at the time under consideration in this application (though there is no practical benefit to most of them because most of the money has gone anyway). Unfortunately, on the material that I have had the argument fails. I have already held that the money is taken by the Agents as agent for Farepak. That of itself does not militate against the existence of a *Quistclose* trust. However, there is no suggestion that the Agent was expected to keep the money separate from other money (or indeed his or her own), and it is indeed known that it was mixed with the money of others and paid over to Farepak with the money of others. Again, that of itself it not inconsistent with a *Quistclose* trust, but it does not help. But crucially, there is no suggestion that the money ought to have been put on one side by Farepak pending the transmutation from credited money to goods or vouchers. If there were a *Quistclose* trust then that obligation would have been inherent in it, but the business model would have made no sense. It would have required Farepak to have kept all the customer moneys in a separate account from January until November, untouched until the time when the goods or vouchers were acquired and then sent out. That is completely implausible. It would turn Farepak into a very odd savings organisation. Even banks do not have to do that. Mr Trace urged on me that the description of this as a savings scheme (which is how it was described in some publicity) indicated that there was a trust until the vouchers/goods were provided, and pointed to an OED definition which he said supported him. I am afraid it gives him no support at all. The concept of a trust is not inherent in the use of the word 'savings'; indeed, most savings organisations do not operate via a trust at all. They operate at the level of contract and debt.

On analysis it is apparent enough that what the customer was making was advance payments towards the purchase price of goods or vouchers. The payments were noted on the relevant cards. When the price had been paid the customer was entitled to the chosen goods or vouchers. That describes, and is, a contractual relationship. The provision for the return of money if the price went up, or if acceptable goods were not provided, are contractual terms for the return of an equivalent amount of money, not money held on trust.

This argument therefore fails.

The constructive trust

Both Miss Hilliard and Mr Trace sought to make this point. Their starting point was the decision in *Neste Oy v Barclays Bank* [1983] 2 Lloyd's Rep 658 at 666, [1983] Com LR 185, 133 NLJ 597. In that case a company decided that it should cease trading on 22 February. On the same date a payment was made to it of moneys to enable it to discharge its function as shipowner's agent

by discharging certain liabilities. The payment was made by inter-bank transfer on that day (see p. 662). It was found that this money was paid and received at a time when the recipient company had resolved to cease trading immediately, when it had not itself paid for the services which it was entitled to discharge with the remitted moneys and when there was no chance it would pay for those services. In those circumstances Bingham J held there was a constructive trusteeship of the moneys . . . the parallels between what is said there and the present case are obvious. If one looks at the date of receipt into the Natwest current account for the moment, or the date of receipt into the A & L account, then from 11 October Farepak received sums at a time when it had decided to cease trading, and at a time when it was clear that there would be a total failure of consideration – the goods and vouchers were not going to be provided. It is said that that makes it unconscionable for Farepak and its unsecured creditors to have the benefit of this money in the same way as it was unconscionable in *Neste Oy*, with the same sort of constructive trust arising as a result.

It is, however not that simple. So far as the law is concerned, the reasoning of Bingham J has been criticised by Lord Browne-Wilkinson in *Westdeutsche Landesbank v Islington LBC* [1996] AC 669, [1996] 2 All ER 961, [1996] 2 WLR 802 as apparently being premised on reasoning which smacks of a remedial constructive trust which is not recognised by English law . . .

Mr Lopian pointed out (using different terminology) that we are somewhere close to the frontiers of the law of constructive trusts and that if I decided that there were one in this case then I would be deciding new law because I would be creating a remedial constructive trust of a type which is still unknown to English law. I think I can accept that the criticisms of *Neste Oy* mean that the position in a case like that one, where moneys are paid in the nature of an advance payment to be applied in acquiring goods or services which the company has already decided will not be provided, is not as clear as one would wish, but despite that I think that the decision in that case is clear enough and can be reconciled with principle. If and insofar as it could be established that moneys were paid to Farepak by customers at a time when Farepak had decided that it had ceased trading, and indeed at a time when it had indicated that payments should not be received, then there is a strong argument for saying that those moneys would be held by the company as constructive trustee from the moment they were received. As I have said, it may well be possible to justify this conclusion on the basis of a mistake, to bring it into line with Lord Browne-Wilkinson's views. So I would be minded to follow the result in *Neste Oy*, with modified reasoning . . . However, I am afraid that I cannot determine that all the moneys in relation to which I am asked to make a decision fall within that line of argument. If I am to apply the underlying principles which are demonstrated by *Neste Oy* then I have to apply them by reference to the time at which the moneys should be taken to have been paid to and received by Farepak. That is not necessarily the same date as the credit appeared in the current account, and that is for two reasons. First, in the case of items with a three day clearing cycle, some of the items credited on 11 October will be items which were 'paid into' the HOCA on 9 October (outside the period) and some items credited on 12 October will be items 'paid into' HOCA on 10 October (again outside the period). It is not clear on the citation of authorities that I have referred to that it is right to take the date at the end of the clearing cycle as being the date of receipt for these purposes. If the correct analysis is a mistake analysis, at the time when the payment was made in the sense of moneys being paid to the bank there was no relevant mistake because the company had not yet decided to cease trading. The same is true of payments directly into the current account – some of those credited on 11 and 12 October will represent moneys paid in on 9 and 10 October though probably not much money falls into this category. But second, it is in fact even more complicated than that. All the money thus credited is money that had been paid, by some mechanism or another, to Agents before they ever got anywhere near a Natwest account. Since the Agents are agents of the company, receipts by those Agents fall to be treated as receipts by the company. If, as is possible on a scale unknown

to me at present, those Agents received cash but paid in with their own cheques, then in a real sense the company has already received the money. Much of that money is likely to have been collected by the Agents outside the hiatus period . . .

The same is true of moneys paid into the A & L account. Any cash paid in is likely to have been collected outside the hiatus period, to an extent which is simply unknown. Any cheques credited to that account will, in large part, have been 'paid in' before the hiatus period (assuming the same clearance periods apply to that account as apply to the Natwest accounts), representing money or cheques collected from customers even earlier.

Accordingly, an application of the result of *Neste Oy* (which is the high water mark of the constructive trust case) does not justify the distribution of all the money. Payment and receipt of the money were, in that case, effectively simultaneous. Payment and receipt of the moneys in the present case were not necessarily simultaneous. That creates factual and legal problems. The factual problems lie in ascertaining how moneys arrived at the Agents and at HOCA (and A & L). The legal problems lie in analysing how the constructive trust principles that survive from *Neste Oy* apply to those facts. The overall position is of sufficient uncertainty that I am unwilling to decide them on the basis of the material that I have.

I very much regret coming to this decision. Had it been possible to arrive at a firmer conclusion, applying an appropriate degree of robustness, I would very much have liked to have done so. However, I consider that even allowing for the desirability of distributing now, if at all possible, the material does not exist which makes it sufficiently clear for present purposes that the sums which are said to come within the constructive trust do in fact do so. It is not clear to me whether it is possible to determine that at least some relevant sums do come within the possible trust. I suspect that that will take some work to ascertain that, and that work will be difficult.

The express trust

Miss Hilliard's first point in relation to this is that, without the deed of trust, the facts demonstrate an effective declaration of trust over all the customer moneys which the company had or received as at or after the date of the creation of the trust (ie after 10 October). This includes moneys paid in prior to 11 October. I do not think that this argument can succeed. The directors clearly manifested an intention to create a trust, but they have to do something in the nature of a declaration in order actually to create it. What they did was execute the deed of trust. There is no evidence of any other act going beyond a mere declaration of intention, apart from the execution of the deed, that is even a candidate. Accordingly an express trust arises out of the deed or not at all.

The main problem with the declaration of trust is that on its terms it does not apply to any moneys because the account referred to is empty. On the facts as placed before me there is a strong case for saying that the problem is one of misdescription which can be cured by a process of construction, but I do not think that it is necessary to agonise over that because it is clear to me on the evidence that the deed was executed as a result of a mistake and falls to be rectified. The mistake is plain – Mr Fowler intended to refer to the account with money in it, and identified the wrong one. His prime purpose was not to declare a trust over the account referred to in the deed. His purpose, and the purpose of the directors, was to declare trusts over real money. He merely misdescribed where it was. That is rectifiable. The directors who executed the deed were told what it was thought the effect was, repeating the mistake. They were similarly mistaken.

A unilateral document can be rectified – see *Re Butlin's Settlement* [1976] Ch 251, [1976] 2 All ER 483, [1976] 2 WLR 547. In my view the declaration of trust should be rectified to bring it into line with the intention of the company. The relevant intention is the intention of the board to

protect customers whose money was still being received, as refined by Mr Fowler who implemented the intention by giving instructions for the trust deed. His intention was, in substance if not in terms, to declare a trust over the current account. His own evidence is that he did not go further and intend to declare one over any other account or money – the HOCA (if relevant) or the A & L account. The appropriate form of rectification would be to substitute the name and number of the current account for the account identified in the deed.

Mr Lopian says that that does not necessarily remove all the problems, however. It is said that cl 1 presents a problem in that it goes further than intended. It states that the moneys in the account are held on trust for the payors, and not merely the customers. The intention of the directors was to protect the customers, not others, and to a limited extent the money of others was also credited to the current account. Thus, says Mr Lopian, the deed does not coincide with the intention of the company even if the name of the account is rectified.

That does not seem to me to be a bar to rectification, or treating the deed as if rectified, for two reasons. First, I consider that the deed as rectified only covers customer money on its true construction. The first recital refers to moneys being paid into the account by customers. In that context the word 'payors' in recital 3 would quite naturally mean the payors just referred to, namely the customers. There is no reason why a wider class than those just referred to should be intended at this point. That inference is strengthened by the circumstance that anyone else paying money into the account would be someone who intended the company to have the money on any footing – persons other than customers who owed the company money. If that is right then the words 'relevant payors' is reference back to the people thus described in the recitals. That means that the deed does indeed refer to a trust over moneys paid in by customers, which is to be held in trust for those customers paying it in.

Second, even if the deed does go further than apparently intended (on extrinsic evidence) so far as the apparent beneficiaries are concerned, then that is no reason for saying it has no effect vis-à-vis customers. As a matter of construction it still catches money paid in by customers.

The fact that it is actually the agents who pay the money in, and not customers, does not make any difference. It is quite clear what money is being talked about, and who the beneficiaries are said to be.

The deed can therefore be treated as rectified to cover the account and moneys it was intended to cover. At this point, however, another problem arises. If and insofar as the money has already been paid to the company (via the Agents) the relevant customers are already creditors. By declaring this trust those customers are apparently given a preference. The whole purpose of this deed is to do just that, though the chain of reasoning is not articulated because no thought was given at the time to the legal route by which the company acquired the money. I do not see at the moment that there is any obvious answer to this, though the point was not argued before me (probably because there was not much focus on the true status of the Agents). If it is possible to treat any customers as paying the money in direct then there may not be a preference so far as those customers are concerned, because they are not creditors at the moment of the creation of the trust over their money, but filtering those customers out may be difficult if not impossible. At the moment this preference point is an obstacle at a practical level, at least, to any sums being paid out on the footing of a rectified deed of trust.

One striking aspect of this line of cases is that there are many instances where the company is advised on how to safeguard the interests of the customers, but does not act fully in accordance with that advice. This is often why the courts have great difficulty in ascertaining that there is a trust in existence – the company is often not clear itself as to what its intentions are.

There may also be a concern that a trust set up in these circumstances may be viewed as a sham in that it is a means of avoiding repaying a debt to certain creditors. However, the courts are unlikely to view such arrangements as a sham – unlike the situation in *Midland Bank v Wyatt* [1997] 1 BCLC 242, there is no intimation that the 'true' beneficiary is the company itself. However, there may at some level be some concern that one category of creditors – i.e. the customers – are being treated preferentially over others. Therefore, unless it is clear that the money is given for a specific purpose,[1] and no other, it seems unlikely that a trust will be identified.[2]

Ring-fencing company assets

It may be advantageous for a company to be able to ring-fence assets so that they cannot be accessed by creditors in the event of a company going into administration. By putting assets in the hands of trustees, they are beyond the reach of creditors. Although the creation of a trust with the deliberate motive of avoiding creditors is likely to be at worst fraudulent, and at best liable to be undone by a court who views the arrangement as a sham trust, it may nevertheless be possible for commercial property to be owned beneficially, thus ensuring that the trust does not become indebted. This is an extension of the historical concept of the use whereby property was put in the hands of a group of trustees with the result that if one trustee died, a child never became the outright owner of the land, thus ensuring that the various obligations that would arise in that situation never became due. In the modern commercial context, a similar approach is adopted. The property of a business or a company is owned under a number of trusts, with the consequence that if the company becomes insolvent, all its assets will not be swallowed up by the repayment of the debt. In essence, this operates on the same principle as the safeguarding of customers' assets. However, instead of safeguarding the customers' assets, it may be an effective way of separating the assets used by a company, with the result that, rather than being the outright owner of specific assets, the company is merely a beneficiary under a trust, with the result that if the company goes into liquidation, assets belonging to the trustees of the holding company are not affected. There may nevertheless be a danger that the trust is perceived as a sham, but if trusts of this nature are established from the inception of the company, the law may view such an arrangement as being acceptable.

The fiduciary duty of company directors

The concept of a fiduciary duty is, as has been shown in Chapter 11, notoriously difficult to pin down. There are some situations, most notably in the context of the trust, where the existence of a fiduciary obligation is an established matter.[3] Therefore, in a trust relationship, there can be no question of the trustee being able to make a personal gain from the trust relationship,[4] and no question of the trustee being able to use information

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[1] *Twinsectra v Yardley* [2002] 2 AC 164, *Global Marine Drillships Ltd v Landmark Solicitors LLP* [2011] EWHC 2685 (Ch), *Templeton Insurance Ltd v Penningtons Solicitors LLP* [2006] EWHC 685 (Ch).
[2] *Abou-Rahmah and Others v Abacha and Others* [2005] EWHC 2662.
[3] *Clarke v Smith* [1940] 1 KB 126.
[4] *Boardman v Phipps* [1967] 2 AC 46.

he or she has obtained in his or her capacity as a trustee in order to obtain a benefit for him- or herself.[5]

Yet, there are many other instances where a fiduciary duty is found to exist, usually as a precursor to implying a trust. In commercial contexts therefore, a person such as a company director may find that fiduciary duties are imposed in order to enable the court to impose an equitable remedy.[6] Clearly, in the context of the company, a director will expect to gain from the relationship, in that he or she will expect to receive remuneration. However, there may nevertheless be an expectation of loyalty and good faith owed by a company's director to the company.

The concept of a fiduciary duty was explained by Lord Herschell in the case of *Bray v Ford* [1896] AC 44, where he explains:

> a person in a fiduciary position, such as the respondent's, is not, unless otherwise expressly provided, entitled to make a profit; he is not allowed to put himself in a position where his interest and duty conflict . . . human nature being what it is, there is danger, in such circumstances, of the person holding a fiduciary position being swayed by interest rather than by duty, and thus prejudicing those whom he was bound to protect. It has, therefore, been deemed expedient to lay down this positive rule.

Nevertheless, the concept of a fiduciary relationship is often nebulous, with the result that there have been different approaches to determining when a person will owe a fiduciary relationship. One approach is to consider whether the individual has undertaken to act for the benefit of another. In *White v Jones* [1995] 2 WLR 187 therefore, the solicitor had, by accepting the deceased testator's instructions regarding the writing of a new will, assumed a fiduciary responsibility to the intended beneficiaries to ensure that he did not act negligently in the execution of his client's instructions. Another approach has been to consider whether the power conferred upon the individual means that he or she is able to affect the interests of another, who therefore relies on that individual's integrity. However, interpreting this principle too broadly would result, as in the case of negligent misstatement in tort, in a risk that any number of people may be regarded as owing a fiduciary duty.

Accordingly, in the context of commercial enterprises, a company director may be the subject of a fiduciary relationship in terms of ensuring that there is no conflict between his or her interests as a buyer and the company's interests as a seller. In this type of situation, a duty is imposed and the company director will be liable if that duty is breached.

On the other hand, there are other cases where a fiduciary duty is not ordinarily expected to owe a duty, but the particular circumstances of the situation means that he or she is imbued with a fiduciary responsibility, and the court may then find that there is a constructive trust, or alternatively trace an asset into whatever it has been exchanged for or mixed with. This means that even though the claimant is unable to recover that which rightfully belongs to him or her, the claimant is nevertheless able to claim assets currently in the defendant's possession that represent the asset, of which the claimant has been unlawfully deprived. Accordingly, in *Aluminium Industrie Vaassen BV v Romalpa Aluminium Ltd* [1976] 1 WLR 676, Romalpa was regarded as owing AIV a fiduciary duty, even though a bailee is not ordinarily regarded as a fiduciary.

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[5] *Keech v Sandford* (1726) Sel Cas Ch 61.

[6] *Charles Terence Estates Ltd v Cornwall Council* [2012] EWCA Civ 1439.

Loans

The case of *Barclays Bank Ltd v Quistclose Investments Ltd* [1970] AC 567 indicates the scope of the trust as a means of enabling a loan to be issued in a way that circumvents the need for registration. In *Barclays Bank v Quistclose*, a loan was issued for the specific purpose of ensuring that a company was able to pay a dividend to its shareholder. This was held to be a form of trust whereby the money was given on trust until either the dividend was paid, or it became apparent that the dividend would not have to be paid because the company had gone into administration. However, because this is in principle an unsecured loan, although some measure of security is offered by the fact that the trust will result back to the settlor if the purpose is not fulfilled, there is no need for the loan to be registered. This may be very important for a business or a company, as consumer and lender confidence may be undermined if its indebtedness is known, leading to a loss of custom, a reluctance to trade and a reluctance to lend – all of which factors will worsen the company's situation. Accordingly, a trust may be a means of bolstering consumer confidence in the business, leading to increased custom, and therefore financial success.

Romalpa (retention of title) clauses

The *Romalpa* clause is another example of the trust concept being bolted onto the contractual relationship. It is therefore an example of equity and the common law melding together – a common law relationship is overlaid with an equitable construction of how the relationship should function. A *Romalpa* clause, more properly called a 'retention of title clause' or alternatively a 'reservation of title clause', is a clause that allows the seller to retain the title to goods until the buyer has paid for them. Ordinarily, title to goods is transferred when the buyer takes possession of them. However, if the buyer becomes insolvent, the seller will rank among the other unsecured creditors until the debt is repaid. Therefore, in order to protect him- or herself from this risk, the seller will include a retention of title clause in the contract, permitting him or her to retain title to the goods until payment is made, or alternatively, if payment is not made, for the goods to be held on a resulting trust for the seller.

A *Romalpa* clause, derived from the case where it was first successfully employed, *Aluminium Industrie Vaassen BV v Romalpa Aluminium Ltd* [1976] 1 WLR 676, however takes the reservation of title principle further. In this case, the claimants, AIV, had sold aluminium to the defendant, who had then sold most of the supply to third parties. The contract between AIV and Romalpa contained a reservation of title clause. Romalpa went into administration owing AIV £122,000. AIV therefore claimed for the return of the aluminium that Romalpa had not sold, and also for the money that buyers had paid Romalpa for the aluminium it had sold on. Returning the unsold aluminium was not problematic – the retention of title clause meant that this already belonged to AIV. However, it was more difficult to ascertain that AIV could claim the money paid by Romalpa's customers. Nevertheless, this is what the Court of Appeal concluded, on the basis that it found Romalpa to be a bailee of AIV's goods. Accordingly, Romalpa could be regarded as being liable for the loss of those goods, which was essentially the effect of Romalpa having sold the aluminium belonging to AIV to third parties. It was, thereafter 'lost' to AIV, as AIV was unable to claim it back from those customers.

Since *Aluminium Industrie Vaassen BV v Romalpa Aluminium Ltd* was decided however, the courts have been reluctant to apply the *Romalpa* principle to similar fact cases such as *Re Andrabell Ltd* [1984] 3 All ER 407, and have either declined to find that the

defendant owed the claimant a fiduciary duty or have declined to find that the money was kept sufficiently separate so as to be identifiable as being for the benefit of someone other than the defendants themselves. The use of Romalpa clauses has not therefore been as extensive as was initially anticipated.

EXTRACT

Aluminium Industrie Vaassen BV v Romalpa Aluminium Ltd [1976] 1 WLR 676

Case facts

AIV had sold aluminium to the defendant, who had then sold most of the supply to third parties. The contract between AIV and Romalpa contained a reservation of title clause. Romalpa went into administration owing AIV £122,000. AIV therefore claimed for the return of the aluminium that Romalpa had not sold, and also for the money that buyers had paid Romalpa for the aluminium it had sold on. Returning the unsold aluminium was not problematic – the retention of title clause meant that this already belonged to AIV. However, it was more difficult to ascertain that AIV could claim the money paid by Romalpa's customers.

Roskill LJ

It is obvious that the defendants' directors, the two ex-partners, knew precisely what the terms of business had been before the defendants came on the scene as a contracting party with the plaintiffs, and what those terms were going to be thereafter – that is to say after the defendants had so come on the scene – and in fact were at all material times; and their knowledge was manifestly the knowledge of the defendants. Whilst it is true that there are, as counsel for the defendants rightly said, many cases in the books in which the knowledge of a director of company A, acquired in that capacity, has been held not to be the knowledge of company B, of which that person is also a director, that principle to my mind has no application whatever here. The defendants took over the antecedent business of the partnership. If ever there were a case in which the past knowledge of the partners became the present knowledge of the defendants, whose two main directors were those two former partners, to my mind it is the present. With all respect to the argument of counsel for the defendants, the contrary seems to me to be almost unarguable.

Accordingly, it seems to me clear that the foil physically held by the receiver is the plaintiffs' foil, to which they are now entitled, and the appeal against that part of Mocatta J's judgment must in my view clearly fail.

I turn to the second part, which counsel for the defendants argued first. Are the plaintiffs entitled to the proceeds of sales to sub-purchasers now held by the receiver? We were told both by counsel for the defendants and by counsel for the plaintiffs that the receiver received these moneys after he had entered into his receivership from sales made by the defendants to sub-purchasers before that date. The receiver, properly if I may say so, kept those moneys separate; and we were told that there is no complication arising of those moneys having become mixed with other moneys, because they were always kept separate. There was no suggestion that the sub-sales in question were other than authorised by the plaintiffs or that the sub-purchasers concerned did not acquire a valid title to the several quantities of foil which each of them bought. The sole question is whether, on the facts and on the true construction of the bargain, including the general conditions, between the plaintiffs and the defendants, the plaintiffs are entitled to trace and recover those proceeds of the sub-sales, on the well-known principles laid down in the judgment of Jessel MR in *Re Hallett's Estate*. Those principles are so

well known that it is not necessary to quote Jessel MR's famous judgment or from the various restatements of principle in the several textbooks to which counsel for the defendants has referred. The most relevant passages from that judgment will be found in Mocatta J's judgment (Pages 555–557, ante)

The critical question is whether there was a fiduciary relationship between the plaintiffs and the defendants which entitles the plaintiffs successfully to claim these moneys in the way and on the footing which I have just described. Counsel for the defendants strenuously argued that the bargain between the parties was a perfectly ordinary bargain, creating the ordinary contractual relationship of seller and buyer, with the consequence that if the buyers-that is to say the defendants-became insolvent before payment for the goods was made by them to the sellers-that is the plaintiffs-the sellers were left with their ordinary contractual or, as he put it, personal remedy as unsecured creditors of the buyers, and that there was no additional proprietary remedy (again to borrow his language) available to them justifying their seeking to trace and recover the proceeds of the sub-sales which had come from the sub-purchasers into the hands of the receiver.

It seems to me clear that, but for the provisions of cl 13 – which have to be read in conjunction with the other relevant clauses I have mentioned – this would be the position. The individual contracts were for delivery ex the plaintiffs' works in Holland, and, apart from special provisions, in English law at least – as already stated, there is no evidence of Dutch law and therefore we must apply English law to these contracts – both property and risk would have passed to the defendants on such delivery.

But cl 13 plainly provides otherwise. The plaintiffs as sellers were to retain the property in the goods until all – and I underline 'all' – that was owing to them had been paid. It is a curious fact that the first part of cl 13 is so short while the second part is so long and detailed. But, as counsel for the plaintiffs said, the problems with which the second part had to deal were infinitely more complex than those with which the first part had to deal. It is obvious, to my mind, that the business purpose of the whole of this clause, read in its context in these general conditions, was to secure the plaintiffs, so far as possible, against the risks of non-payment after they had parted with possession of the goods delivered, whether or not those goods retained their identity after delivery. I unhesitatingly accept that part of counsel for the plaintiffs' submission. In the case of unmanufactured goods this was to be achieved by the plaintiffs retaining the property until all payments due had been made, to which were added the special rights given by cl 25. In the case of mixed or manufactured goods, more elaborate provisions were made and indeed were obviously required if the avowed objects of cl 13 were to be achieved in the case of the latter class of goods. The plaintiffs were to be given the ownership of these mixed or manufactured goods as 'surety' for 'full payment'. 'Surety' I think in this context must mean, as counsel for the plaintiffs contended, 'security'. This is as between the defendants and the plaintiffs, and it is not necessary to consider how far those provisions would protect the plaintiffs against adverse claims, at any rate in this country, by third parties. Further, the clause later provides that until 'full payment' is made the defendants shall keep the mixed goods for the plaintiffs as 'fiduciary owners' – not perhaps the happiest of phrases but one which suggests, at least to an English lawyer, that in relation to mixed or manufactured goods there was produced what in English law would be called a fiduciary relationship in this respect. The clause goes on to give to the defendants an express power of sale of such goods, and the right to deliver them; and adds an obligation on the defendants, if required by the plaintiffs to do so, to assign (to use English legal language) to the plaintiffs the benefit of any claim against a sub-purchaser so long as the defendants have not fully discharged all their indebtedness to the plaintiffs.

For my part, I accept that this last-mentioned provision is not itself an equitable assignment in English law. But I think that counsel for the plaintiffs is right in his general approach to the

construction of the second part of cl 13. Like the first part, it contemplates the resale by the defendants of goods which at the time of such resale were to be the property of the plaintiffs and not of the defendants. The second part of cl 13 clearly contemplates the creation of a fiduciary relationship in relation to mixed goods; and the assignment provisions are, as I think, clearly designed to give the plaintiffs if they so require, an additional security to recover debts otherwise payable to the defendants but not paid to them by the sub-purchasers, if the defendants have failed to discharge all or any of their current indebtedness to the plaintiffs.

The burden of counsel for the plaintiffs' argument was, first that all goods dealt with in pursuance of cl 13 were, until all debts were discharged, the plaintiffs' goods which the defendants were authorised to sell on the plaintiffs' behalf and for the plaintiffs' account but only within the framework of cl 13. Since the goods were the plaintiffs', the defendants remained accountable to the plaintiffs for them or for their proceeds of sale, so long as any indebtedness whatever remained outstanding from the defendants to the plaintiffs. Hence the creation of the fiduciary relationship on which counsel for the plaintiffs sought to rely. The burden of counsel for the defendants' argument was, as already stated, that the clause created in the first part no more than the ordinary debtor/creditor, buyer/seller, relationship, and that nothing in the second part justified placing additional fiduciary obligations on the defendants in respect of unmanufactured goods, referred to in the first part of the clause.

It was common ground at the trial and during argument in this court that some implication had to be made into the first part of cl 13; since otherwise the defendants could not lawfully sell the unmanufactured goods in their possession, at least until they were paid for-for, as already pointed out, they were the plaintiffs' and not the defendants' goods. To hold otherwise, as I think both parties accepted, would be to stultify the whole business purpose of these transactions. What, if any, implication is to be made beyond that? The first part of cl 13 is silent not only as to the power of sale but as to the dealing with any proceeds of the goods lawfully so sold by the defendants. Is the admitted power of sale (if I may respectfully borrow Goff LJ's phrase during the argument) fettered or unfettered? If it is fettered, is the fetter that, so long as any indebtedness remained outstanding in any respect from the defendants to the plaintiffs, the defendants after a sub-sale remained accountable to the plaintiffs for all proceeds of sub-sales, not even, as counsel for the defendants pointed out in argument, being able to retain for themselves the profit on any such sales? . . .

What, then, is there here to relieve the defendants from their obligation to account to the plaintiffs for those goods of the plaintiffs which they lawfully sell to sub-purchasers? The fact that they so sold them as principals does not, as I think, affect their relationship with the plaintiffs; nor, as at present advised, do I think – contrary to argument of counsel for the defendants – that the sub-purchasers could on this analysis have sued the plaintiffs on the sub-contracts as undisclosed principals for, say, breach of warranty of quality.

It seems to me clear (and so far from helping counsel for the defendants I think the second part of cl 13, properly construed, helps counsel for the plaintiffs) that to give effect to what I regard as the obvious purpose of cl 13 one must imply into the first part of the clause not only the power to sell but also the obligation to account in accordance with the normal fiduciary relationship of principal and agent, bailor and bailee. Accordingly, like the learned judge, I find no difficulty in holding that the principles in *Re Hallett's Estate*, to which I have already referred, are of immediate application, and I think that the plaintiffs are entitled to trace these proceeds of sale and to recover them, as the learned judge has held by his judgment . . .

Goff LJ

There is in my view no doubt at all that, the partners having accepted and signed the translation of the general terms and conditions, the whole of those terms, including cl 13,

applied to the contracts made by them, and that is agreed. It is said, however, that the defendants are in a better position than the partners and are not bound by cl 13. I cannot accept that argument. True, the company was a different entity in law. True also, a company is not necessarily to have imputed to it the knowledge of its directors acquired in another capacity. But here those directors were the vendors of the very business in relation to which they not only acquired the knowledge but agreed the terms on which the business was to be conducted, and they continued to manage the company and told the plaintiffs that they were doing so. It would be a travesty if the defendants were not bound, and I do not see anything to force one to the conclusion that they were not. On the contrary, it seems to me that the facts lead irresistibly to the conclusion that they were. In any case, the forms, which the defendants continued to receive and accepted, expressly pointed out that the full terms were filed in every county court in Holland, and I do not see how they can possibly be heard to say that they had no notice of cl 13 and did not contract on the full filed terms, which they could have caused to be inspected, but had no need so to do, because the majority at least, if not the whole, of the board knew them and had accepted them.

I agree with Roskill LJ in saying that the reasoning of Mocatta J on this part of the case is quite unchallengeable.

In my judgment the second part of the case comes down to a short question of construction. It is common ground that a power of sale during the period that any money remains owing to the plaintiffs must be implied; but the question is on what terms . . .

In considering what should be implied in a contract, the court has to consider what is required to give it business efficacy; but I agree with Roskill LJ that there are here two distinct and opposing approaches to 'business efficacy'. The one, looking at the matter from the point of view of the defendants, suggests that an unqualified power is required, because they would need to use the money in carrying on their business, and indeed, so it is suggested, anything else would largely stultify the agreement that they should have 75 days' credit. The other is, from the standpoint of the plaintiffs, that the power should not be so wide as to frustrate the whole purpose of cl 13, which it is submitted, and in my judgment rightly submitted, discloses a manifest intention to preserve the vendors from being left in the position of unsecured creditors.

In the end, in my judgment, the question is which of these ought to prevail; and I have come to a clear conclusion that the plaintiffs' contention should be preferred . . .

Megaw LJ

We are now concerned with a commercial transaction, or series of transactions, between parties who must be deemed to see and take the trouble to read documents which have, or which they should reasonably expect to be intended by the other party to have, a contractual status. On each occasion when the defendant company entered into contracts with the plaintiffs, as it did on hundreds of occasions, there was brought to the notice of the responsible representatives of the defendant company, even if those representatives had not earlier had full knowledge of it, a clearly printed document – an acknowledgement of order – which on its face said 'Vide epitome of our General Selling Terms at the back'. The English translation, on the back of the document, of the so-called 'epitome' said that the epitome was an epitome of 'the General Selling Terms and Conditions . . . which general selling terms and conditions are filed at the Record Office of all County Courts in the Netherlands'. There is no dispute but that cl 13, though not included in the 'epitome', was included in the general selling terms and conditions thus filed. There could not sensibly on the facts of this case be any suggestion that the defendant company, through its representatives, was in any way misled by that non-inclusion. There is no doubt that the two directors of the defendant company, Mr Rodbard and

> Mr Malyon, in their previous capacity as partners in the firm which was thereafter taken over by the defendant company, had seen and considered all those terms, including cl 13. Yet it is, apparently, seriously suggested that cl 13 was not a term of the relevant contracts. I am unable to see why not . . .
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> I agree that the appeal should be dismissed.

Providing an intermediary in arm's-length transactions

The versatility of the trust means that it is useful in contractual transactions where the buyer and the seller have not traded with each other previously. In such cases there may be a reluctance to rely upon a party whose reliability is not known. A trustee may be used to facilitate the transaction by becoming the transferee of both the seller's goods and the buyer's money. If both parties' consideration is provided, then the trustee may transfer the goods to the buyer and the payment to the seller. However, if one of the parties does not fulfil their obligations, the trustee will then hold the other's consideration on a resulting trust. Therefore, if, for example, the buyer does not deliver the payment, the trustee will hold the goods on a resulting trust for the seller.

Solicitors' clients' accounts

The solicitor's client account is a form of trust, very similar to the *Quistclose* trust described above, even though a solicitor's clients may not be conscious of the fact that when they give money to a solicitor that is not intended to be by way of payment for services rendered, the relationship they are creating is that of a trust. Solicitors regularly have to deal with money that belongs to the firm and money that belongs to their clients. For example, where a client has paid a solicitor for services rendered, that money will belong to the firm of solicitors. However, solicitors will also handle money that belongs to their clients, such as, for example, money paid by homebuyers as a deposit on a house, or money held by solicitors as trustees of a will. As a matter of professional conduct, a solicitors' firm will therefore need to have at least two bank accounts. Therefore, if the firm goes into liquidation, the clients' money is held on a trust, thus ensuring that clients will have their money returned to them. A similar obligation is imposed on estate agents under s.13 Estate Agents Act 1979.[7]

Employee incentives

Large organisations will often offer certain incentives to their employees. One such incentive is a company pension scheme, which will be discussed further in Chapter 17. However, other incentives may include share entitlement or medical care. These will be administered under a trust, whereby the trustees act as trustees of a discretionary trust for the benefit of a company's employees. The advantages of such schemes for the company is that they enable it to raise capital by issuing shares, or to enable the founding shareholders to sell their shareholding without risking that the company will be bought by persons outside the company.

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[7] (1979 c.38).

We therefore see how, although the trust's initial significance was purely domestic, the trust is becoming increasingly relevant in commercial contexts as well. Its flexibility means that it can be adapted therefore to a new range of situations. In essence, if it is necessary for one person to own something for the benefit of another, then the law's method of achieving this is the trust.

Chapter summary

This chapter may be useful for assessments and assignments on:

- The significance of the trust
- Commercial trusts
- Equity's capacity to innovate.

Further reading

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17

Investments and pensions

Chapter outline

This chapter will cover:

- Different types of investment trust
- Pensions.

Introduction

Another modern significance of the trust may be seen in the context of investments and pensions. Although, as has been shown, the trust has always had the objective of maintaining and preserving wealth, there is also a recognition of its capacity as a means of generating wealth. Accordingly, this chapter will focus on the use of the trust as an investment mechanism and also on its role for the purposes of safeguarding pension funds.

Investment trusts

The expansion of trustees' powers of investment under s.3(1) Trustee Act 2000 has meant that there is now far greater scope for trusts to be used specifically for the purpose of investment. The previous law in the form of the Trustee Investments Act 1961[1] required trust investments to be divided between narrow-range and wide-range investments. This limited the scope of the trust to make significant gain and the emphasis was placed very much on the preservation of the trust fund rather than growth. Because a trustee may now make '*any kind of investment that he could make if he were absolutely entitled to the assets of the trust*' (Trustee Act 2000, s.3(1)), there are far more opportunities for trusts to be used as investment mechanisms.

One way in which the trust may be used for the purposes of investment is through the use of what is termed the investment trust. Essentially, an investment trust operates by pooling the money of a group of investors together. A fund manager will then invest this money. The advantage of the investment trust is that by allowing for collective investment, the fund manager is able to invest in a broader range of companies than the individual would be able to manage. The investment therefore takes advantage of the potential to invest on a larger scale, and to spread the risk of loss across different types of companies. An investment trust is essentially a trust in accordance with the broader meaning of the term trust. It should therefore be distinguished from the strict three-party trust relationship that has been discussed elsewhere in this book. The investment trust is essentially a company. However, the elements of money being put into an entity's hands in order to confer a benefit on the settlor are manifested in an investment trust in the same way as any other type of trust. Therefore, although the fund manager's duty to the investor is one of a fiduciary nature, there is considerable overlap with the trust concept.

Unit trusts

The unit trust is more closely akin to the traditional concept of the trust than the investment trust. Although, as with the investment trust, the unit trust is a form of collective investment, the fact that trustees oversee the investment means that the trust relationship is far more clearly identified than is the case with investment trusts. Sin[2] also explains that the unit trust is not only a means of investing money, but that it is also an asset that may be bought and sold, and that it is used as a means of trading. Sin explains that the unit trust combines both the contract and the trust:

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[1] (1961 c.62).

[2] Sin, K.F. (1997) *The Legal Nature of the Unit Trust.* Oxford: Clarendon Press p.2.

> In a unit trust, the trust is being used, contractually, as a holding device to achieve collective ownership of unitholders themselves, rather than as a means of disposition in favour of objects of the unitholders' benefaction. This basic position implies that rights and obligations of all these three parties may be derived from contract, trust or both. This contractual – and non-gift – character means that the unit trust should not be subject to rules relating to perpetuities or the rule in *Saunders v Vautier* [(1841) 41 ER 482], but may be subject to the doctrine of frustration. Its dual trust and contractual characters will give parties remedies both at law and in equity, depending on the nature of a particular dispute.[3]

Furthermore, Sin explains that the unit trust does not sit entirely comfortably with the settlor-trustee-beneficiary pattern we have hitherto encountered because a unit trust '*is constituted without the participation of a settlor. It represents the terms that have been agreed by the manager and the trustee for the provision of their respective services to the unitholders and for the issue of units.*'[4] In other words, the manager advertises the unit trust as being available, and an investor subscribes to it. In spite of this, the unit trust nevertheless retains many of the characteristics of a trust, such as the three certainties encountered in *Knight v Knight* (1840) 3 Beav 148, and, according to French J in the case of *Famel Pty Ltd v Burswood Management Ltd* (1989) 15 ACLR 572*,* the manager may be equated with the settlor, albeit a settlor who continues to play an active role in the operation of the unit trust – a similar concept perhaps to the person who declares him- or herself to be a trustee. The current author suggests that it is not the manager or the trustee who assumes the role of the settlor in a unit trust. Instead it is the investor, who transfers money to the trustee, to be managed by the fund manager, for the benefit of the original investor.

This was the approach taken in New Zealand in the cases of *Baldwin v CIR* [1965] NZLR 1 and *Tucker v CIR* [1965] NZLR 1027. Therefore although the trust is in one sense created when the manager devises it and advertises it as being available, in another sense, it is not created until an investor subscribes to it, in that until that point the trust lacks subject matter and beneficiaries. However, the High Court of Australia took a different view. In *Truesdale v FCT* (1969) 120 CLR 353, Menzies J explains:

> The words 'created a trust' in s.102 [Income Tax Assessment Act 1936 (Australia)] are not, I think, apt to describe the payment of money to a trustee to hold under a trust already constituted. There is an obvious difference between creating a trust in respect of property, on the one hand, and on the other, transferring property to a trustee to hold upon the terms of an established trust . . . such a reading would be tantamount to saying that the transfer to the trustee of property to be held as part of the assets of an already constituted trust would be to create a second trust, whereas, from the point of view of both the trustee and of the beneficiary, there would be but one trust and the property transferred would be nothing more than an addition to the property subject to the trust.

The difficulty, according to Menzies J, appears to be that because the unit trust is a form of collective investment, the investor is not creating the trust, because he or she does not dictate the terms. Nevertheless, the investor is transferring property to another for the benefit of him- or herself or for the benefit of another. Accordingly, the separated character of legal and equitable ownership is encountered.

An analogy might be charitable trusts, which will be discussed further in Chapter 19. There does not appear to be any difficulty with identifying a charitable trust as such, with

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[3] Ibid., pp.4–5.
[4] Ibid., p.47.

the result that when a person gives money to charity, he or she is giving money to another person to be held on trust for the benefit of the public at large. The trust may already exist when the settlor donates to it, but there is nevertheless the sense that when one adds to a charitable pot one is in effect saying that money (or land or chattels) that was once in the sole ownership of one person, is to be given to another person in such a way that legal and equitable ownership is divided, so that legal ownership is vested in one person for the benefit of another. The determining question appears to be whether there is any material difference between the settlor who states 'I create a trust of this fund, according to these terms, for this beneficiary' and the settlor who states 'I create a trust of this fund, agreeing to the terms specified by another person, for this beneficiary'. The current author suggests that this does not create any material difference in the nature of the relationship, and that therefore, it is acceptable to view the unit trust as a form of trust. Sin however, comes to the opposite conclusion on this point by stating:

> The irresistible conclusion is that an investor subscribing units does not have any intention to create a trust in favour of himself, but only an intention to add property to an existing trust and to acquire rights as a beneficiary in it in addition to other contractual rights provided by the unit trust scheme.[5]

The current author nevertheless concedes that the unit trust does differ from the ordinary trust in a number of significant ways. The domestic trust envisages a high degree of control by the settlor and the beneficiaries, in that the adult beneficiaries of a domestic trust may terminate the trust under the principle in the case of *Saunders v Vautier* (1841) 41 ER 482. However, because a unit trust is a collective investment, the ability of one person to control its operation is far more restricted. The difference is essentially the difference between a trust for an individual and a trust for the benefit of a group. Although a sole beneficiary may invoke the rule in *Saunders v Vautier*, even a trust where there are only two adult beneficiaries will not result in the *Saunders v Vautier* rule being used if one of the two beneficiaries does not consent to the termination of the trust. This situation is of course magnified where there are multiple beneficiaries. Accordingly, even though there are differences between unit trusts and domestic trusts, this does not preclude the unit trust from being a type of trust, even though it is a type of trust that originates in a contract between the investor, the manager and the trustee.

Occupational pension schemes

It is likely that, once one is in employment, one will consider investing in a pension scheme. Many employers, especially in the public sector, offer an occupational pension scheme, and indeed from October 2012, there is a duty imposed on larger employers to do so.[6] Broadly, these schemes operate as follows. Both the employer and the employees will invest in the scheme and the money generated by these investments will produce an income to the employees on retirement, based on their salary and the length of their service with the organisation or the company. In essence, this is a form of trust. The employer and the employees settle money into the trust for the benefit of the employees on retirement. So far this is entirely consistent with the concept of the trust hitherto discussed in this book. The settlor (the employer and employee) transfers money to the pension fund operator for the benefit of a beneficiary (the employee).

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[5] Ibid., pp.54–5.
[6] Pensions Act 2008 (2008 c.30).

Yet there are a number of crucial issues that mean that a pension trust does not accord entirely with the concept of a trust. Firstly, the structure and management of a pension fund is governed more extensively by statute, and there is an increasing recognition that the law of pensions and the law of trusts should be different in character. For example, a general principle of the trust is that once the trust has been created, the settlor, qua settlor, plays no further part in the trust relationship. However, in the context of pension schemes, there is a recognition that the settlor-employer wishes to maintain a significant degree of control over the trust fund and the way in which it is invested – and of course the way in which it is distributed.

Secondly, the employer's contribution to an occupational pension scheme is something that may be the subject of negotiation. The employer's contribution is seen as an employment benefit, and accordingly it may be expedient for the employer to reduce its contribution if the organisation's economic situation demands it. Clearly, such a change may be unpopular with employees who may feel aggrieved that their employer, in effect, wishes to amend the terms by which the employment relationship is governed.

The fact that the employer is able to amend the conditions of its obligations after the trust has been set up does not conform with the concept of the trust as it is usually understood because it means that the employer-settlor is able to reserve powers for him- or herself whereas, as has been shown, the fundamental idea of the trust is that the trustee becomes the legal owner of the trust property for the benefit of the beneficiary and the settlor plays no further part in the governance of the trust.

The other way in which occupational pension schemes differ from other types of trust is that the employee beneficiaries and the trades unions that represent them will often be concerned about the way in which the trust fund is invested. Accordingly, it is likely that the beneficiaries will be keen to ensure that the fund is invested in an ethically responsible way, and in particular, to ensure that it is invested in a way that benefits the UK economy, because, of course, that will benefit employees. In essence, the argument is that if the fund is invested in companies that have an UK based workforce, then the employment conditions of UK workers will be better with fewer people being made redundant.

Furthermore, employees may wish to ensure that the trust is not invested in a way that conflicts with the interests of the industry in which they are employed. In essence this was the issue that prompted the litigation in the case of *Cowan v Scargill* [1985] Ch 270. The investment plan of the National Coal Board's pension scheme permitted overseas investments as well as permitting investment in oil and gas – the growth of which would be likely to be to the detriment of the coal miners who would benefit from the pension fund. However, it was held that this was not the concern of the trustees, whose responsibility was to obtain the best return for the fund.

This case highlights one of the main problems of the trust model in the context of pension trusts because it demonstrates the scope that exists for the personal interests of the trustees to conflict with those of the beneficiaries. For example, if the scheme's trustees are part of the organisation's management, then their corporate interests are best served by minimising employer contributions. On the other hand, the interests of the trust are best served if employer contributions are maximised.

Differences are also encountered in relation to the rules governing pensions. Firstly, the size of a pension fund means that the trustees are more likely to be professional fund managers than laypersons.

Secondly, the rules regarding investments and delegation are contained in the Pensions Act 1995, s.34 and s.35, rather than in the Trustee Act 2000 – although the rules are broadly similar, and in this respect, the Pensions Act 1995[7] may be viewed as the model

[7] (1995 c.26).

for trustee investments and delegations that was then followed in relation to all types of trust when the Trustee Act 2000 was enacted.

Thirdly, s.34 Pensions Act 1995 provides that the trustees of a pension trust may act by majority rather than having to act unanimously.

The categorisation of pension funds as trusts is therefore not an entirely easy one. Yet, there are a number of advantages to this categorisation and, therefore, the law of trusts cannot be discarded entirely.

Firstly, the trust model means that the pension fund is kept separate from the employee's assets in the same way as a solicitor's client account will be safe from the organisation's creditors if the organisation becomes insolvent.

Secondly, the irrevocable character of a trust means that it cannot be used by a company as a tax avoidance mechanism. As has been demonstrated, once a trust has been created it cannot be revoked. In the context of occupational pension schemes this means that an employer cannot set up a scheme as a form of ring-fenced account as a means of avoiding tax and then dismantling it when it needs the assets.

The third advantage of the trust is its flexibility. A trust may be drafted according to the settlor's wishes and, accordingly, the settlor may retain close control over the investment of the fund by appointing the company's directors or members of the organisation's senior management team to be the trustees.

Hannah[8] (1986) also argues that the use of the term trust is a strategic tool. The term has connotations of reliability and integrity. Accordingly, its use in the employment relationship may be highly advantageous in terms of promoting positive industrial relations among the workforce and providing an incentive for employees to co-operate with the employer. Furthermore, when the employer needs to reduce its workforce, the option to offer early retirement may be attractive to employees who might otherwise have to be offered redundancy packages from the employer's own resources.

Chapter summary

This chapter may be useful for assessments and assignments on:

- The contemporary uses of the trust
- The historical development of the trust
- Commercial uses of the trust mechanism.

Further reading

Nicholls, D. (1995) 'Trustees and their broader community: where duty, morality and ethics converge' 9(3) *Trusts Law International* 71.

Thornton, R. (2008) 'Ethical Investments: A Case of Disjointed Thinking' 67(2) *Cambridge Law Journal* 396.

Watchman, P. (2005) 'Fiduciary Duties in the 21st Century: A UK Perspective: A Legal Framework for the Integration of Environmental, Social and Governance Issues into Institutional Investment' 19(3) *Trust Law International* 127.

[8] Hannah (1986) *Inventing Retirement: The Development of Occupational Pensions in Britain.* Cambridge University Press: Cambridge p.19.

18

Non-charitable purposes

Chapter outline

This chapter will cover:

- What is an unincorporated association?
- The significance of the trust for unincorporated associations
- Methods for construing the trust as a form of unincorporated association
- Other non-charitable purposes.

Introduction

Another aspect of the law of trusts is trusts for purposes. Generally, a trust must exist either for the benefit of individuals or a group of individuals, or for a charitable purpose. However, there are some forms of purpose trusts that are not charitable, but neither are they for the benefit of a specific group of individuals. These are known as non-charitable purpose trusts. These types of trusts do not fit neatly into the classification of 'domestic trusts' or 'commercial trusts'. Unincorporated associations are by definition not commercial ventures, and the other types of non-charitable purposes, such as the maintenance of a specific animal, have a distinctly domestic character. However, in many situations, the trust relationship has an element of arm's-length dealing, with the result that a non-charitable purpose trust does not fit comfortably as a domestic trust either. Nevertheless, non-charitable purposes make up an important area of trusts law, precisely because of this uneasy identity.

Unincorporated associations

For the undergraduate student, an unincorporated association is likely to be their first contact with the experience of being a trustee. A person who is on the committee of a club or a society will be a trustee, especially if they are mandated to receive money and to make payments on behalf of the club or a society. A sports club, a drama society or a film appreciation society, if they are not created as companies, will be unincorporated associations, and will be governed by the law of trusts. Nevertheless, as shall be demonstrated, the application of the law of trusts to their governance is at times problematic, and the courts have demonstrated considerable ingenuity in recognising an unincorporated association as a trust and administering it accordingly.

What is an unincorporated association?

The case of *Conservative and Unionist Central Office v Burrell (Inspector of Taxes)* [1980] 3 All ER 42 involved considering three discrete elements when defining an unincorporated association:

> The structure of the Conservative party organisation is described in the blue book in following terms:
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> '. . . basically, the structure is very simple and is made up of three elements: – (i) the Parliamentary Party which consists of those Members of both Houses who take the Conservative Whip. This is the oldest element and embodies the Party in Parliament; (ii) the membership represented by the National Union of which the constituency association is the basic unit; and (iii) the Party headquarters–the Central Office–which with its area offices operates the machinery of Party organisation throughout England and Wales, and the Conservative Research Department. These three elements are complementary. This pattern, parliamentary, National Union and agency, is repeated at three levels, constituency, area and national. At the head stands the Leader of the Party.'

Vinelott J explained the characteristics that would define an unincorporated association as being:

> Counsel for the Central Office had submitted that there are six characteristics which are either essential or normal characteristics of an unincorporated association. They are: (i) there must be members of the association; (ii) there must be a contract binding

> the members inter se; (iii) there will normally be some constitutional arrangement for meetings of members and for the appointment of committees and officers; (iv) a member will normally be free to join or leave the association at will; (v) the association will normally continue in existence independently of any change that may occur in the composition of the association; and (vi) there must as a matter of history have been a moment in time when a number of persons combined or banded together to form the association.
>
> Counsel for the Central Office made it clear in his argument in this appeal that (iii), (iv) and (v) were not put forward as essential characteristics of an unincorporated association. It is possible to imagine an unincorporated association which lacked at least one of these characteristics. For instance, a members' club might be so exclusive as to make no provision for the admission of new members and the original members might conceivably band themselves together in life membership. But the first two characteristics are put forward, I think rightly, as essential characteristics. Indeed, they seem to me no more than an analysis of the concept of an unincorporated association. The sixth characteristic is, I think, also a necessary characteristic of an unincorporated association. If an unincorporated association is a 'group of people defined and bound together by rules and called by a distinctive name' (see per Lord Buckmaster in *Re Macaulay's Estate, Macaulay v O'Donnell* [1943] Ch 435 at 428) there must have been a moment in time when the first members agreed expressly or impliedly to be bound by the rules. But in practice the task of answering the question whether a body with a distinctive name is an unincorporated association will rarely if ever be much assisted by asking when it came into existence.

However, the reader will appreciate that this incorporates a number of different forms of association. On the one hand, it could encompass a fairly disparate and fluctuating group of persons, who share certain interests or viewpoints. The members of this type of group are likely to pay an annual subscription with the expectation of obtaining certain benefits – perhaps in the form of some form of social benefit, or an entitlement to receive certain goods or services. An example would be a student society, whereby the members join the society in order to benefit from the social activities arranged by the society.

Other forms of association may be smaller and with a more static membership. For example, the gift in *Leahy v Attorney General of New South Wales* [1959] AC 457 was made to a religious order, whose activities were not regarded as charitable. The significance of considering the type of organisation at issue is important because, as shall be demonstrated later in this chapter, it will affect the way in which the trust for the benefit of the organisation is construed.

As has been shown earlier (in Chapter 8), a trust requires three certainties: intention, subject matter and objects. The initial difficulty with identifying unincorporated associations as trusts is the certainty of objects. Generally, a trust must be either for a charitable purpose (as will be discussed in Chapter 19) or for specific beneficiaries, and a trust for a non-charitable purpose will generally not be valid because, as Sir William Grant MR explained in *Morice v Bishop of Durham* [1803–13] All ER Rep 451, there is a need for someone to enforce the trust. Consider for example a typical student society. This type of society is not likely to be a business, and is therefore unable to own property in its own name (thus unincorporated – it has no legal personality). Yet it is not an individual that owns property on his or her own behalf. But it receives money from the members. The only way in which this money can therefore be owned is by the committee members mandated to act as operators of the bank account. Yet, they do not own this money for their own benefit and must therefore be trustees for the members. Who are the members? In a club or a society, this is likely to change from year to year, with the result that it becomes very difficult for the trustees to list all the beneficiaries of the trust, according

to the fixed list requirement of *IRC v Broadway Cottages* [1955] Ch 20. A further difficulty is that the subscriptions paid by the members during one year will be used to pay for events during the following year, with the result that the question of who exactly the beneficiaries are becomes very difficult. The problem is compounded when the association is wound up. To whom does the money now belong when its fund is likely to comprise of a mixture of current and former members' contributions?

In *Re Denley's Trust Deed* [1969] 1 Ch 373 this was circumvented by construing the gift as being a trust for the benefit of a group of persons, namely the employees of a company called H.H. Martyn & Co Ltd. The reason why this is required is because an unincorporated association has no legal personality, and cannot therefore hold property in its own name. It cannot therefore be the recipient of a gift or the beneficiary of a trust. However, as has been demonstrated, a group of persons could be the beneficiaries of a trust, and therefore provided that the trust may be construed in such a way as to confer a benefit on identifiable beneficiaries, it may subsist as a private trust for the benefit of persons. A comparison of the cases of *Leahy v Attorney General of New South Wales* [1959] AC 457 and *Re Denley's Trust Deed* [1969] 1 Ch 373 is instructive here because these cases demonstrate the different possible approaches to determining how the trust concept is used in relation to gifts made to unincorporated associations.

EXTRACT

Leahy v Attorney General of New South Wales [1959] AC 457

Case facts

A testator made a will for the purpose of building or altering, and then furnishing, a convent. Because the trust could not be viewed as wholly charitable, the court had to consider whether it was valid as a non-charitable purpose trust.

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The disposition made by clause 3 must now be considered. As has already been pointed out, it will in any case be saved by the section so far as Orders other than Contemplative Orders are concerned, but the trustees are anxious to preserve their right to select such Orders. They can only do so if the gift is what is called an absolute gift to the selected Order, an expression which may require examination.

Upon this question there has been a sharp division of opinion in the High Court. Williams and Webb JJ. agreed with Myers J. that the disposition by clause 3 was valid. They held that it provided for an immediate gift to the particular religious community selected by the trustees and that it was immaterial whether the Order was charitable or not because the gift was not a gift in perpetuity. 'It is given' they said (and these are the significant words) 'to the individuals comprising the community selected by the trustees at the date of the death of the testator. It is given to them for the benefit of the community.' Kitto J. reached the same conclusion. He thought that the selected Order would take the gift immediately and absolutely and could expend immediately the whole of what it received. 'There is,' he said, 'no attempt to create a perpetual endowment.' A different view was taken by the Chief Justice and McTiernan J. After an exhaustive examination of the problem and of the relevant authorities they concluded that the provision made by clause 3 was intended as a trust operating for the furtherance of the purpose of the Order as a body of religious women or, in the case of the Christian Brothers, as a teaching Order. 'The membership of any Order chosen,' they said, 'would be indeterminate and the trust was intended to apply to those who should become members at any time. There was no intention to restrain the operation of the trust to these presently members or to make

the alienation of the property a question for the Governing Body of the Order chosen or any section or part of that Order.' They therefore held that unless the trust could be supported as a charity it must fail.

The brief passages that have been cited from the judgments in the High Court sufficiently indicate the question that must be answered and the difficulty of solving it. It arises out of the artificial and anomalous conception of an unincorporated society which, though it is not a separate entity in law, is yet for many purposes regarded as a continuing entity and, however inaccurately, as something other than an aggregate of its members. In law a gift to such a society simpliciter (i.e., where, to use the words of Lord Parker in *Bowman v. Secular Society Ltd.* [[1917] AC 406], neither the circumstances of the gift nor the directions given nor the objects expressed impose on the donee the character of a trustee) is nothing else than a gift to its members at the date of the gift as joint tenants or tenants in common. It is for this reason that the prudent conveyancer provides that a receipt by the treasurer or other proper officer of the recipient society for a legacy to the society shall be a sufficient discharge to executors. If it were not so, the executors could only get a valid discharge by obtaining a receipt from every member. This must be qualified by saying that by their rules the members might have authorised one of themselves to receive a gift on behalf of them all.

It is in the light of this fundamental proposition that the statements, to which reference has been made, must be examined. What is meant when it is said that a gift is made to the individuals comprising the community and the words are added 'it is given to them for the benefit of the community'? If it is a gift to individuals, each of them is entitled to his distributive share (unless he has previously bound himself by the rules of the society that it shall be devoted to some other purpose). It is difficult to see what is added by the words 'for the benefit of the community.' If they are intended to import a trust, who are the beneficiaries? If the present members are the beneficiaries, the words add nothing and are meaningless. If some other persons or purposes are intended, the conclusion cannot be avoided that the gift is void. For it is uncertain, and beyond doubt tends to a perpetuity.

The question then appears to be whether, even if the gift to a selected Order of Nuns is prima facie a gift to the individual members of that Order, there are other considerations arising out of the terms of the will, or the nature of the society, its organisation and rules, or the subject-matter of the gift which should lead the court to conclude that, though prima facie the gift is an absolute one (absolute both in quality of estate and in freedom from restriction) to individual nuns, yet it is invalid because it is in the nature of an endowment and tends to a perpetuity or for any other reason. This raises a problem which is not easy to solve, as the divergent opinions in the High Court indicate.

The prima facie validity of such a gift (by which term their Lordships intend a bequest or demise) is a convenient starting point for the examination of the relevant law. For as Lord Tomlin (sitting at first instance in the Chancery Division) said in *In re Ogden* [[1933] Ch 678], a gift to a voluntary association of persons for the general purposes of the association is an absolute gift and prima facie a good gift. He was echoing the words of Lord Parker in *Bowman*'s case that a gift to an unincorporated association for the attainment of its purposes 'may . . . be upheld as an absolute gift to its members.' These words must receive careful consideration, for it is to be noted that it is because the gift can be upheld as a gift to the individual members that it is valid, even though it is given for the general purposes of the association. If the words 'for the general purposes of the association' were held to import a trust, the question would have to be asked, what is the trust and who are the beneficiaries? A gift can be made to persons (including a corporation) but it cannot be made to a purpose or to an object: so also, a trust may be created for the benefit of persons as *cestuis que* trust but not for a purpose or object unless the purpose or object be charitable. For a purpose or object cannot sue, but, if it be charitable, the Attorney-General can

sue to enforce it . . . It is therefore by disregarding the words 'for the general purposes of the association' (which are assumed not to be charitable purposes) and treating the gift as an absolute gift to individuals that it can be sustained. The same conclusion had been reached 50 years before in *Cocks v. Manners* [(1871) LR 12 Eq 574] where a bequest of a share of residue to the 'Dominican Convent at Carisbrooke (payable to the Superior for the time being)' was held a valid gift to the individual members of that society. In that case no difficulty was created by the addition of words which might suggest that the community as a whole, not its members individually, should be the beneficiary. So also with *In re Smith* [[1914] 1 Ch 937]. There the bequest was to 'the society or institution known as the Franciscan Friars of Clevedon County of Somerset' absolutely. Joyce J. had no difficulty in construing this as a gift individually to the small number of persons who had associated themselves together at Clevedon under monastic vows. Greater difficulty must be felt when the gift is in such terms that, though it is clearly not contemplated that the individual members shall divide it amongst themselves, yet it is prima facie a gift to the individuals and, there being nothing in the constitution of the society to prohibit it, they can dispose of it as they think fit. Of this type of case *In re Clarke* [[1901] 2 Ch 110] may be taken as an example. There the bequest was to the committee for the time being of the Corps of Commissionaires in London to aid in the purchase of their barracks or in any other way beneficial to the Corps. The judge (Byrne J.) was able to uphold this as a valid gift on the ground that all the members of the association could join together to dispose of the funds or the barracks. He assumed (however little the testator may have intended it) that the gift was to the individual members in the name of the society or of the committee of the society. This might be regarded as an extreme case had it not been followed by *In re Drummond* . . . Their Lordships must now turn to the recent case of *In re Macaulay's Estate* [[1943] Ch 436], which appears to be reported only in a footnote to *In re Price* [[1943] Ch 422]. There the gift was to the Folkestone Lodge of the Theosophical Society absolutely for the maintenance and improvement of the Theosophical Lodge at Folkestone. It was assumed that the donee, 'the Lodge,' was a body of persons. The decision of the House of Lords in July 1933, to which both Lord Buckmaster and Lord Tomlin were parties, was that the gift was invalid. A portion of Lord Buckmaster's speech may well be quoted . . . 'A group of people,' he said, 'defined and bound together by rules and called by a distinctive name can be the subject of gift as well as any individual or incorporated body. The real question is what is the actual purpose for which the gift is made. There is no perpetuity if the gift is for the individual members for their own benefit, but that, I think, is clearly not the meaning of this gift. Nor again is there a perpetuity if the society is at liberty in accordance with the terms of the gift to spend both capital and income as they think fit . . . If the gift is to be for the endowment of the society to be held as an endowment and the society is according to its form perpetual, the gift is bad: but, if the gift is an immediate beneficial legacy, it is good.' In the result he held the gift for the maintenance and improvement of the Theosophical Lodge at Folkestone to be invalid. Their Lordships respectfully doubt whether the passage in Lord Buckmaster's speech in which he suggests the alternative ground of validity: viz., that the society is at liberty in accordance with the terms of the gift to spend both capital and income as they think fit, presents a true alternative. It is only because the society, i.e., the individuals constituting it, are the beneficiaries, that they can dispose of the gift. Lord Tomlin came to the same conclusion. He found in the words of the will 'for the maintenance and improvement' a sufficient indication that it was the permanence of the Lodge at Folkestone that the testatrix was seeking to secure and this, he thought, necessarily involved endowment. Therefore a perpetuity was created. A passage from the judgment of Lord Hanworth M.R. (which has been obtained from the records) may usefully be cited. He said: 'The problem may be stated in this way. If the gift is in truth to the present members of the society described by their society name so that they have the beneficial use of the property and can, if they please, alienate and put the proceeds in their own pocket, then there is a present gift to individuals which is good: but if the gift is intended for the good not only of the present but of future

members so that the present members are in the position of trustees and have no right to appropriate the property or its proceeds for their personal benefit then the gift is invalid. It may be invalid by reason of there being a trust created, or it may be by reason of the terms that the period allowed by the rule against perpetuities would be exceeded.'

It is not very clear what is intended by the dichotomy suggested in the last sentence of the citation, but the penultimate sentence goes to the root of the matter. At the risk of repetition their Lordships would point out that, if a gift is made to individuals, whether under their own names or in the name of their society, and the conclusion is reached that they are not intended to take beneficially, then they take as trustees. If so, it must be ascertained who are the beneficiaries. If at the death of the testator the class of beneficiaries is fixed and ascertained or ascertainable within the limit of the rule against perpetuities, all is well. If it is not so fixed and not so ascertainable the trust must fail. Of such a trust no better example could be found than a gift to an Order for the benefit of a community of nuns, once it is established that the community is not confined to living and ascertained persons. A wider question is opened if it appears that the trust is not for persons but for a non-charitable purpose. As has been pointed out, no one can enforce such a trust. What follows? *Ex hypothesi* the trustees are not themselves the beneficiaries yet the trust fund is in their hands, and they may or may not think fit to carry out their testator's wishes. If so, it would seem that the testator has imperfectly exercised his testamentary power; he has delegated it, for the disposal of his property lies with them, not with him. Accordingly, the subject-matter of the gift will be undisposed of or fall into the residuary estate as the case may be. Their Lordships do not ignore that from this fundamental rule there has from time to time been a deviation: see, for example, *In re Dean, In re Thompson*: and that attempts have been made to explain or justify such cases . . . But the rule as stated in *Morice v. Bishop of Durham* [(1805) 32 ER 1009] (per Sir William Grant M.R.27 (per Lord Eldon L.C.28 continues to supply the guiding principle . . .

In the first place, it is not altogether irrelevant that the gift is in terms upon trust for a selected Order. It is true that this can in law be regarded as a trust in favour of each and every member of the Order. But at least the form of the gift is not to the members, and it may be questioned whether the testator understood the niceties of the law. In the second place, the members of the selected Order may be numerous, very numerous perhaps, and they may be spread over the world. If the gift is to the individuals it is to all the members who were living at the death of the testator, but only to them. It is not easy to believe that the testator intended an 'immediate beneficial legacy' (to use the words of Lord Buckmaster) to such a body of beneficiaries.

In the third place, the subject-matter of the gift cannot be ignored. It appears from the evidence filed in the suit that Elmslea is a grazing property of about 730 acres, with a furnished homestead containing 20 rooms and a number of outbuildings. With the greatest respect to those judges who have taken a different view, their Lordships do not find it possible to regard all the individual members of an Order as intended to become the beneficial owners of such a property. Little or no evidence has been given about the organisation and rules of the several Orders, but it is at least permissible to doubt whether it is a common feature of them, that all their members regard themselves or are to be regarded as having the capacity of (say) the Corps of Commissionaires (see *In re Clarke* [[1901] 2 Ch 110] to put an end to their association and distribute its assets. On the contrary, it seems reasonably clear that, however little the testator understood the effect in law of a gift to an unincorporated body of persons by their society name, his intention was to create a trust, not merely for the benefit of the existing members of the selected Order, but for its benefit as a continuing society and for the furtherance of its work . . . The dominant and sufficiently expressed intention of the testator is in their opinion (again in the words of Lord Buckmaster) that 'the gift is to be an endowment of the society to be held as an endowment,' and that 'as the society is according to its form perpetual' the gift must, if it is to a non-charitable body, fail.

Essentially, the question for Viscount Simonds is whether there is sufficient certainty of objects. If the purported trust is for an imprecise number of people, then it cannot be a valid trust. Equally, if there is no one to whom the trustees are able to transfer the trust property, then the purported trust cannot be valid. Also, if the nature of the purported trust is to create an ongoing obligation that never terminates, then it cannot be a valid trust because it is is contrary to the rule against perpetuities (Perpetuities and Accumulations Act 2009). Indirectly, the question of whether there is a valid trust also requires consideration of the settlor's intention as well. The wording of the trust must be considered carefully in order to evaluate whether the settlor intended to benefit the members in existence at the time the trust was created or whether the trust can only be viewed as being for a purpose, and there are no identifiable beneficiaries. If an indirect benefit to individuals may be discerned as the intention, then a trust may exist. However, if there was no intention to confer a benefit upon identifiable individuals, then benefiting individuals does not fulfil the settlor's intentions and the gift cannot be construed as a trust.

The further difficulty created by a trust to benefit all the members of a group is the difficulties that arise from dividing the trust property between all the members of a large group. This may be possible – although problematic in terms of administrative workability (per *R v District Auditor No 3 Audit District of West Yorkshire Metropolitan County Council, ex p West Yorkshire Metropolitan County Council* [1986] RVR 24) where the trust consists of money but may be extremely impractical where the trust property consists of land. It therefore becomes probable that, where the trust property comprises of something that cannot readily be divided between a large group of persons, the settlor did not intend to create a trust for the benefit of individuals.

In the case of *Re Denley's Trust Deed* [1969] 1 Ch 373, the trust was construed as being for the benefit of individuals, defined by their connection to the company, even though the trust had been worded as though it were a purpose trust. The trust was valid because there was an indirect benefit to specific people.

EXTRACT

Re Denley's Trust Deed [1969] 1 Ch 373

Case facts

The trustees were given a plot of land that was to be maintained as a sports ground, primarily for the benefit of a company's employees and such other persons as were permitted by the trustees. The issue for the court was therefore, if the trust was not charitable, whether it was valid as a private trust.

Goff J

In re Astor's Settlement Trusts [[1952] Ch 534] . . . a trust for a number of non-charitable purposes was not merely unenforceable but void on two grounds; first, that it was not a trust for the benefit of individuals, which I will refer to as 'the beneficiary principle,' and, secondly, for uncertainty.

Mr. Mills has argued that the trust in clause 2 (c) in the present case is either a trust for the benefit of individuals, in which case he argues that they are an unascertainable class and therefore the trust is void for uncertainty, or that it is a purpose trust, that is, a trust for providing recreation, which he submits is void on the beneficiary principle, or, alternatively, that it is something of a hybrid, having the vices of both kinds.

I think there may be a purpose or object trust, the carrying out of which would benefit an individual or individuals, where that benefit is so indirect or intangible or which is otherwise so

framed as not to give those persons any *locus standi* to apply to the court to enforce the trust, in which case the beneficiary principle would, as it seems to me, apply to invalidate the trust, quite apart from any question of uncertainty or perpetuity. Such cases can be considered if and when they arise. The present is not, in my judgment, of that character, and it will be seen that clause 2 (d) of the trust deed expressly states that, subject to any rules and regulations made by the trustees, the employees of the company shall be entitled to the use and enjoyment of the land. Apart from this possible exception, in my judgment the beneficiary principle of *In re Astor's Settlement Trusts*, which was approved in *In re Endacott, decd.* [[1960] Ch 232] – see particularly by Harman L.J. – is confined to purpose or object trusts which are abstract or impersonal. The objection is not that the trust is for a purpose or object per se, but that there is no beneficiary or *cestui que* trust. The rule is so expressed in *Lewin on Trusts*, 16th ed. (1964), p. 17, and, in my judgment, with the possible exception I have mentioned, rightly so. In *In re Wood, decd.* [[1949] 1 All ER 1100], Harman J. said:

> 'There has been an interesting argument on the question of perpetuity, but it seems to me, with all respect to that argument, that there is an earlier obstacle which is fatal to the validity of this bequest, namely, that a gift on trust must have a *cestui que* trust, and there being here no *cestui que* trust the gift must fail.'

Again, in *Leahy v. Attorney-General for New South Wales* Viscount Simonds, delivering the judgment of the Privy Council, said:

> 'A gift can be made to persons (including a corporation) but it cannot be made to a purpose or to an object: so also,' – and these are the important words – 'a trust may be created for the benefit of persons as cestuis que trust but not for a purpose or object unless the purpose or object be charitable. For a purpose or object cannot sue, but, if it be charitable, the Attorney-General can sue to enforce it.'

Where, then, the trust, though expressed as a purpose, is directly or indirectly for the benefit of an individual or individuals, it seems to me that it is in general outside the mischief of the beneficiary principle. I am fortified in this conclusion by the dicta of Lord Evershed M.R. and Harman L.J. in *In re Harpur's Will Trusts* [[1962] Ch 78]. It is fair to say that there are two matters which, in my view, weaken those passages; first, of course, that *In re Astor's Settlement Trusts* and *In re Endacott, decd.* were not cited, and, secondly, so far as the Master of the Rolls is concerned, that he prefaced his remarks by saying that the argument had satisfied him, and if one refers to the argument one sees that the examples given were all powers, not trusts . . . In my judgment, therefore, these dicta, and especially that of Harman L.J., clearly show that in their view there are purpose or object trusts which escape the operation of that principle.

Some further support for my conclusion is, I think, to be found in *In re Aberconway's Settlement Trusts* [[1962] Ch 78], where it was assumed that a trust for the upkeep and development of certain gardens which were part of a settled estate was valid . . . it is, I think, not without significance that in the very next year after *In re Astor's Settlement Trusts* was decided, Lord Evershed M.R. appears to have had no doubt in his mind that a provision which he described as 'a trust for a very special and particular object, not, as I assume, a charitable object, but a public object of somewhat similar character,' that is to say, clearly a purpose trust, and which earlier on the same page he had said might no doubt be regarded as being indirectly for the benefit of the tenant for life, was a valid trust. Moreover, in the court below Danckwerts J., who thought the gift over was invalidated, did unquestionably assume the validity of the trust, and so did Denning L.J. in his dissenting judgment, where he said:

> 'It seems to me on that evidence that the trusts which were originally intended by the garden settlement can be carried out now in the retained part. The only modification necessary in the trusts is to make them apply to the retained part instead of to the whole gardens. That is, I think, quite permissible.'

I also derive assistance from what was said by North J. in *In re Bowes* [[1895 B 5880]]. That was a bequest of a sum of money upon trust to expend the same in planting trees for shelter on certain settled estates. It happened that there was a father and a son of full age, tenant for life in possession and tenant in tail in remainder respectively; so that, subject to the son disentailing, they were together absolutely entitled, and the actual decision was that they could claim the money, but North J. said:

> 'If it were necessary to uphold it, the trees can be planted upon the whole of it until the fund is exhausted. Therefore there is nothing illegal in the gift itself' – and later – 'I think there clearly is a valid trust to lay out money for the benefit of the persons entitled to the estate.'

The trust in the present case is limited in point of time so as to avoid any infringement of the rule against perpetuities and, for the reasons I have given, it does not offend against the beneficiary principle; and unless, therefore, it be void for uncertainty, it is a valid trust.

As it is a private trust and not a charitable one, it is clear that, however it be regarded, the individuals for whose benefit it is designed must be ascertained or capable of ascertainment at any given time: see *Inland Revenue Commissioners v. Broadway Cottages Trust* [[1955] Ch 20].

It is conceded that 'the employees of the company' in clause 2 (c), which must mean for the time being, are so ascertained or ascertainable, but Mr. Mills submits that the inclusion in the class of 'such other person or persons (if any) as the trustees may allow' is fatal, and that the qualification 'secondarily' in relation to such persons does not help. In my judgment, however, this is not so. I accept Mr. Parker's submission that the provision as to 'other persons' is not a trust but a power operating in partial defeasance of the trust in favour of the employees which it does not therefore make uncertain. Moreover, as it is a power, it is not necessary that the trustees should know all possible objects in whose favour it is exercisable: see *In re Gulbenkian's Settlements* [[1968] Ch 126]. Therefore, in my judgment, it is a valid power. If this were a will, a question might arise whether this provision might be open to attack as a delegation of the testamentary power. I do not say that would be so, but in any case it cannot be said of a settlement *inter vivos*.

Another question, perhaps of difficulty, might arise, if the trustees purported to admit not to a given individual or individuals but a class which they failed to specify with certainty, whether in such a case this would import uncertainty into and invalidate the whole trust or would be merely an invalid exercise of the power; but, as that has not in fact occurred, I need not consider it.

There is, however, one other aspect of uncertainty which has caused me some concern; that is, whether this is in its nature a trust which the court can control, for, as Lord Eldon L.C. said in *Morice v. Bishop of Durham*:

> 'As it is a maxim, that the execution of a trust shall be under the control of the court, it must be of such a nature, that it can be under that control; so that the administration of it can be reviewed by the court; or, if the trustee dies, the court itself can execute the trust: a trust therefore, which, in case of mal-administration could be reformed; and a due administration directed; and then, unless the subject and the objects can be ascertained, upon principles, familiar in other cases, it must be decided, that the court can neither reform maladministration, nor direct a due administration.'

The difficulty I have felt is that there may well be times when some of the employees wish to use the sports club for one purpose while others desire to use it at the same time for some other purpose of such natures that the two cannot be carried on together. The trustees could, of course, control this by making rules and regulations under clause 2 (d) of the trust deed, but they might not. In any case, the employees would probably agree amongst themselves, but I cannot assume that they would. If there were an impasse, the court could not resolve it, because it clearly could not either exercise the trustees' power to make rules or settle a scheme, this being a non-charitable trust: see *In re Astor's Settlement Trusts*.

> In my judgment, however, it would not be right to hold the trust void on this ground. The court can, as it seems to me, execute the trust both negatively by restraining any improper disposition or use of the land, and positively by ordering the trustees to allow the employees and such other persons (if any) as they may admit to use the land for the purpose of a recreation or sports ground. Any difficulty there might be in practice in the beneficial enjoyment of the land by those entitled to use it is, I think, really beside the point. The same kind of problem is equally capable of arising in the case of a trust to permit a number of persons – for example, all the unmarried children of a testator or settlor – to use or occupy a house or to have the use of certain chattels; nor can I assume that in such cases agreement between the parties concerned would be more likely, even if that be a sufficient distinction, yet no one would suggest, I fancy, that such a trust would be void.
>
> In my judgment, therefore, the provisions of clause 2 (c) are valid . . .

Therefore, in order for a donation to an unincorporated association to give rise to a valid trust, it is necessary that its purpose be for identifiable beneficiaries who may enforce the trust. The requirements are therefore as follows:

- The trust must be for a particular association, rather than for a more general purpose: therefore a trust for the benefit of a specific group 'the University of Stratford-Upon-Avon line dancing society' for example, rather than the furtherance of line dancing more generally.
- The purpose of the trust must be neither too abstract nor too impersonal. Accordingly, a trust for furthering a particular social or political objective is likely to be too impersonal – the trust makes no reference to possible beneficiaries. Nevertheless, a trust for such purposes may exist provided that there are identifiable beneficiaries. Therefore a trust for a specific political party may be valid, as there will be members who may benefit. However, a trust, for example, to advance the cause of socialism does not have clear individual beneficiaries. On the other hand, a purpose such as a sports ground for employees or to arrange social events for members displays a clear link between the purpose and those who will benefit from that purpose.
- The beneficiaries must have sufficient standing to be able to enforce the trust.

Identifying the beneficiaries

A particular problem with using the law of trusts in the context of unincorporated associations is that it may be unclear who the beneficiaries are. For example, membership of a student society will change from year to year. When money is given to the society, the question then arises whether the money is given for the benefit of the beneficiaries who existed when the association was set up, or whether it is for the benefit of those who are members of the society when the money is given, or whether future members of the association might be classed as possible beneficiaries of the trust.

If the trust is for the benefit of those who were members when the association was established, then the question to be considered is whether they have effectively resigned from their entitlement to the benefit of the trust by either formally resigning from the association or by not renewing their subscriptions. With a long-established association with many members, there may also be concerns about the workability of the trust in administrative terms. Other associations, although their membership may be large, may not have a membership list that fluctuates that frequently. For example, with a student society for example, the membership will be for a full academic year, and even if members

withdraw from the university or die, they will not be regarded as having resigned their membership, and therefore, for that period, the membership remains fairly constant. Furthermore, the vast majority of the members are likely to join at the beginning of the academic year rather than at any other time of year, with the result that thereafter although the membership may be large, it is unlikely to fluctuate significantly. Accordingly, an unincorporated association will exist as a valid trust if a group of individuals may be identified as members.

On the other hand, if the trust is for the benefit of the current members, then there may be difficulties with ownership of any surplus funds when the current membership period ends. If one considers a typical student society then, the difficulty becomes clear. A student law society has a £10 annual membership fee. During the first week of term, 100 students join the society. A trust therefore exists of the £1000 for the benefit of the society's current members. The law society committee arranges a Christmas party and spends £950, leaving £50 left over, which does not get spent. If the trust is solely for the benefit of the current members, this would mean that at the end of the academic year, the society would have to be disbanded, and a new law society created for the following academic year. In reality, this does not occur, and what is most likely is that the money that remains will be used during the following academic year.

However, if the trust also confers a benefit upon future members, then a further difficulty arises, namely that the trust may fail if it subsists beyond the perpetuity period operating when the trust was established.[1]

In order to resolve this problem, the courts have developed three principal approaches to the administration of unincorporated associations, outlined by Cross J in *Neville Estates v Madden* [1962] Ch 832.

The first of these is to regard any donation of money as being by way of a gift to the members of the association at the time the gift was made. This may be possible in some cases, where the group is a small circle whose membership does not fluctuate. The second approach is to treat the gift as an endowment to the association (i.e. a trust), and the third approach is to treat any donation as a gift to the members, subject to their rights and liabilities in contract.

Some of these approaches are more appropriate than others for different types of associations, and for ensuring the validity of different types of donation. The first approach avoids the difficulties of a trust, but it is not suited to an association whose members vary. The second approach risks offending against the rules against perpetuities, but has the advantage of allowing the donor to specify the purpose for which the fund is given. The third approach is perhaps better suited to societies and associations where members pay their subscriptions with the expectation of obtaining a service (such as attending a social event). On the other hand, donations that arise by way of a gift or a legacy in a will may be more appropriately dealt with by one of the other two approaches. What follows therefore is an explanation of how each approach has worked and the advantages and disadvantages of each method.

Gift to members at the time of the gift

One approach to construing a donation to an unincorporated association as being a form of trust is to construe it as a form of gift to the members of the association at the time the gift was made. In the case of a gift given in a will, this is a plausible construction for unincorporated associations that take the form of a small and relatively stable group –

[1] For trusts created after April 6 2010, when s.5 Perpetuities and Accumulations Act 2009 came into force, the relevant period is 125 years.

the gift to the members approach might be justified for example to an association such as a secluded religious community or an organisation made up of a circle of lifelong friends. In essence, the trust is construed as a gift to a class of persons in exactly the same way as in the case of *IRC v Broadway Cottages* [1954] 3 All ER 120. It is however more difficult to justify in the case of a national association where there is no intention to benefit the members individually, but rather to further the political cause of the organisation, or for the purposes of arranging social events. With the exception of associations that are in effect a very precise class of individuals therefore, the assertion that the settlor's true intention was a gift to the members cannot easily be sustained.

Endowment to the association

The second method is to construe the gift as an endowment to the association. Essentially, the argument here is that the gift is a gift to the trustees on the condition that the fund is used to further the objectives of the organisation. There may be scope to consider this as a form of conditional gift to the trustees. However, if it is regarded as a gift to the association, it will fail if the association is not charitable. Furthermore, it will fail if the trust continues beyond the perpetuity period, although this is perhaps more problematic with older trusts that use the common law perpetuity period – it is more likely that a trust will be completed before the end of one of the statutory perpetuity periods.

In both of these situations, if the club or the association creases to exist, the money will go *bona vacantia* to the Crown in the case of a gift, or, if a valid trust can be identified, the fund will revert back to the settlor.

Gift to members subject to their contractual entitlements and obligations

Although the previous constructions may assist in terms of ensuring that a gift in a will is valid, it does not assist with explaining how an individual may give a donation to the club or society in other ways. For example, it is difficult to construe that the payment of subscription fees and payments for goods and services may be construed as a gift to the members of the association at the time the gift was made, especially if the association is large, or is likely to comprise of a fluctuating body of members. In this situation, the gift is treated as a gift to the members that are in existence once the donor's contractual expectations have been fulfilled. This is explained by Brightman J in the case of *Re Recher's Will Trusts* [1972] Ch 526:

> A trust for non-charitable purposes, as distinct from a trust for individuals, is clearly void because there is no beneficiary. It does not, however, follow that persons cannot band themselves together as an association or society, pay subscriptions and validly devote their funds in pursuit of some lawful non-charitable purpose. An obvious example is a members' social club. But it is not essential that the members should only intend to secure direct personal advantages to themselves. The association may be one in which personal advantages to the members are combined with the pursuit of some outside purpose. Or the association may be one which offers no personal benefit at all to the members, the funds of the association being applied exclusively to the pursuit of some outside purpose. Such an association of persons is bound, I would think, to have some sort of constitution; that is to say, the rights and liabilities of the members of the association will inevitably depend on some form of contract inter se, usually evidenced by a set of rules. In the present case it appears to me clear that the life members, the ordinary members and the associate members of the London & Provincial society were

bound together by a contract inter se. Any such member was entitled to the rights and subject to the liabilities defined by the rules. If the committee acted contrary to the rules, an individual member would be entitled to take proceedings in the courts to compel observance of the rules or to recover damages for any loss he had suffered as a result of the breach of contract. As and when a member paid his subscription to the association, he would be subjecting his money to the disposition and expenditure thereof laid down by the rules. That is to say, the member would be bound to permit, and entitled to require, the honorary trustees and other members of the society to deal with that subscription in accordance with the lawful directions of the committee. Those directions would include the expenditure of that subscription, as part of the general funds of the association, in furthering the objects of the association. The resultant situation, on analysis, is that the London & Provincial society represented an organisation of individuals bound together by a contract under which their subscriptions became, as it were, mandated towards a certain type of expenditure as adumbrated in rule 1. Just as the two parties to a bi-partite bargain can vary or terminate their contract by mutual assent, so it must follow that the life members, ordinary members and associate members of the London & Provincial society could, at any moment of time, by unanimous agreement (or by majority vote, if the rules so prescribe), vary or terminate their multi-partite contract. There would be no limit to the type of variation or termination to which all might agree. There is no private trust or trust for charitable purposes or other trust to hinder the process. It follows that if all members agreed, they could decide to wind up the London & Provincial society and divide the net assets among themselves beneficially. No one would have any locus standi to stop them so doing. The contract is the same as any other contract and concerns only those who are parties to it, that is to say, the members of the society. The funds of such an association may, of course, be derived not only from the subscriptions of the contracting parties but also from donations from non-contracting parties and legacies from persons who have died. In the case of a donation which is not accompanied by any words which purport to impose a trust, it seems to me that the gift takes effect in favour of the existing members of the association as an accretion to the funds which are the subject-matter of the contract which such members have made inter se, and falls to be dealt with in precisely the same way as the funds which the members themselves have subscribed. So, in the case of a legacy. In the absence of words which purport to impose a trust, the legacy is a gift to the members beneficially, not as joint tenants or as tenants in common so as to entitle each member to an immediate distributive share, but as an accretion to the funds which are the subject-matter of the contract which the members have made inter se.

In my judgment the legacy in the present case to the London & Provincial society ought to be construed as a legacy of that type, that is to say, a legacy to the members beneficially as an accretion to the funds subject to the contract which they had made inter se. Of course, the testatrix did not intend the members of the society to divide her bounty between themselves, and doubtless she was ignorant of that remote but theoretical possibility. Her knowledge or absence of knowledge of the true legal analysis of the gift is irrelevant. The legacy is accordingly in my view valid, subject only to the effect of the events of January 1, 1957.

In essence, what the law considers is whether the donor of the gift has received that which he or she anticipated when he or she entered into a contract with the association. Therefore the payment of a membership fee will entitle the donor to a period of membership of the association (one month, three months, a year etc.), and once that has elapsed, the donor will have received that which he or she expected, and the money will be regarded as an accretion to the club's funds.

Similarly, if the association offers particular products or services as part of its activity, then the donor will have received his or her contractual expectation once he or she has received those goods or services. An association might for example create a series of books or pamphlets which the members may choose to buy, or perhaps it may arrange social events, which the members may wish to attend. Once the member has bought his or her copy of the book, or has attended the social event, he or she has obtained what was anticipated under the contract,[2] and the money is therefore regarded as a gift to the association, which will be distributed to the members in accordance with the association's rules in the event of the association being wound up.

Equal distribution is presumed (the maxim of equality is equity) but the association's rules may provide for an alternative means of distribution, especially if there are different classes of members, such as for example junior or associate members having a reduced share of the fund, proportionate to their reduced membership fee, and any premium members having a larger share if their membership fee has been higher. Therefore, if the ABC Building Block Appreciation Society has an annual membership fee of £10 for adults, £5 for children, and £20 for gold membership, then the gold members will receive a share of the distributed funds that is twice as large as that of the ordinary members, who will acquire a share of the funds that is twice as large as the child members. If the rules make no reference as to how the money should be distributed then the court will distribute the fund according to what is fairest under the circumstances. In for example *Re GKN Bolts and Nuts Ltd etc Works Sports and Social Club* [1982] 1 WLR 774, only members entitled to vote were entitled to a share of the fund when the club was wound up, while in *Re Horley Town FC* [2006] EWHC 2386 (Ch), only full members were entitled to a share of the proceeds.

The leading case on this issue is the case of *Re Bucks Constabulary Widows' and Orphans' Fund Friendly Society; Thompson v Holdsworth and others (No 2)* [1979] 1 All ER 623, although as shall be demonstrated, there are other grounds upon which it has not been followed.

EXTRACT

Re Bucks Constabulary Widows' and Orphans' Fund Friendly Society; Thompson v Holdsworth and others (No 2) [1979] 1 All ER 623

Case facts

The Bucks Constabulary Widows' and Orphans' Fund Friendly Society was established to provide for the widows and orphans of members of the Bucks Constabulary who had died. When the Buckinghamshire Constabulary was amalgamated with other police forces, the members of the widows and orphans fund decided that the fund should be wound up and its assets transferred to the benevolent fund of the Thames Valley Constabulary, with the remainder being given to the current members of the fund. However, the trustee did not have the authority to transfer assets to the Thames Valley benevolent fund, and therefore the issue for the court was whether the assets could be distributed between the members of the widows and orphans fund.

[2] *Re Bucks Constabulary Fund Friendly Society (No 2)* [1979] 1 WLR 936.

Walton J

Before I turn to a consideration of the authorities, it is I think pertinent to observe that all unincorporated societies rest in contract to this extent, that there is an implied contract between all of the members inter se governed by the rules of the society. In default of any rule to the contrary, and it will seldom if ever be that there is such a rule, when a member ceases to be a member of the association he ipso facto ceases to have any interest in its funds . . . I think that there is no doubt that, as a result of modern cases springing basically from the decision of O'Connor MR in *Tierney v Tough* [[1914] 1 IR 142], judicial opinion has been hardening and is now firmly set along the lines that the interests and rights of persons who are members of any type of unincorporated association are governed exclusively by contract, that is to say the rights between themselves and their rights to any surplus assets. I say that to make it perfectly clear that I have not overlooked the fact that the assets of the society are usually vested in trustees on trust for the members. But that is quite a separate and distinct trust bearing no relation to the claims of the members inter se on the surplus funds so held on trust for their benefit.

That being the case, prima facie there can be no doubt at all but that the distribution is on the basis of equality, because, as between a number of people contractually interested in a fund, there is no other method of distribution if no other method is provided by the terms of the contract, and it is not for one moment suggested here that there is any other method of distribution provided by the contract.

Although *Re Bucks Constabulary Widows' and Orphans' Fund Friendly Society; Thompson v Holdsworth and others (No 2)* remains good law on the issue of what happens to a donor's gift once their contractual expectations have been fulfilled, in *Hanchett Stamford v HM Attorney General* [2008] EWHC 330 (Ch), Lewison J disagreed with the judgment of Walton J in relation to what happens when membership of the association dwindles to a situation where there are only two surviving members. Walton J considered that on the death of one of those members, the fund should go *bona vacantia* to the Crown. On the other hand, Lewison J argued that this conflicted with the principle of a joint tenancy, and argued that where there was only one surviving member, the fund would belong to him or her.

The advantage of using the contractual approach to determining ownership of the funds of an unincorporated association is that it is possible to construe the contract as precluding the members from withdrawing their share of the association's funds, as Lewison J explains:

> 'The thread that runs through all these cases is that the property of an unincorporated association is the property of its members, but that they are contractually precluded from severing their share except in accordance with the rules of the association; and that, on its dissolution, those who are members at the time are entitled to the assets free from any such contractual restrictions. It is true that this is not a joint tenancy according to the classical model; but since any collective ownership of property must be a species of joint tenancy or tenancy in common this kind of collective ownership must, in my judgment, be a sub-species of joint tenancy, albeit taking effect subject to any contractual restrictions applicable as between members. In some cases (such as *Cunnack v Edwards* [[1896] 2 Ch 679] those contractual restrictions may be such as to exclude any possibility of a future claim. In others they may not. The cases are united in saying that on a dissolution the members of a dissolved association have a beneficial interest in its assets, and Lord Denning goes as far as to say that it is a 'beneficial equitable joint tenancy'. I cannot see why the legal principle should be any different if the reason for the dissolution is the permanent cessation of the association's activities or the fall in its membership to below two.'

Accordingly, even where membership has dwindled to one, the association's funds are not without an owner. However, if the association has not been wound up at the death of the last owner, then the fund will go *bona vacantia* to the Crown.

The unincorporated association represents a shifting notion of the concept of the trust. A trust for a charitable association fits fairly comfortably into the concept of the trust. However, construing the trust as a gift to the members is extremely problematic because it either requires the court to be extremely liberal in its construction of the gift as being a gift to the members rather than the association and its purposes, or, alternatively, it must incorporate elements of the law of contract into the relationship in order to preclude the members from acting as though they were beneficiaries under a trust and extracting their entitlement from the fund. Neither of these is entirely satisfactory. If the unincorporated association has no legal personality, then it cannot be a party to a contract. However, if the trust is for the benefit of a purpose, then necessarily it fails because there is no beneficiary. All that can be said therefore is that the unincorporated association is recognised as being a useful and valuable thing, but ideas regarding ownership of its assets are nebulous. It must therefore rely on the trust in order to enable its officers to own the property in a manner that is not for their personal benefit (as would a trustee) but must rely on the concept of the contract to allow the members to derive the benefit of the fund, but to preclude them from acting as though they were the owner of their share.

ACTIVITY

Think about an association that you are aware of, or that you are a member of.

1. Would anybody be able to take action if the association's treasurer kept the funds for him- or herself? If so who?
2. What is a beneficiary's entitlement under a trust? To what extent is this fulfilled by owning a share of an association's funds? What aspects of beneficial ownership are not manifested in the entitlement of an association member?
3. Does the trust plus contract relationship provide a satisfactory solution to the problem of unincorporated associations?
4. What scheme of property ownership would you consider would be more appropriate for the funds of an unincorporated association?

Other non-charitable purposes

A second, and potentially more anomalous, category of non-charitable purpose trusts also exists. Earlier, the court's emphasis on a need for the trust to have identifiable beneficiaries who could benefit from the trust was shown – in cases such as *Leahy v Attorney General of New South Wales* [1959] AC 457 and *Re Denley's Trust Deed* [1969] 1 Ch 373, the emphasis was placed very clearly on ensuring that behind the principal purpose, there was a defined group of beneficiaries who could benefit from the trust. It is anomalous therefore that the trusts described in the remainder of this chapter do not have clear human beneficiaries. These non-charitable purpose trusts include trusts for the maintenance of a particular animal, such as a domestic pet, or trusts to commemorate oneself

(or indeed someone else) in some way, such as by funding the establishment of some form of memorial, or by the saying of prayers in one's memory. Indeed, in many cases there is no one who will be able to enforce the trust if the trustee breaches his or her obligations. Therefore if one creates a trust for the maintenance of one's beloved pet, and after one's death, the trustee uses the money to buy him- or herself a car, the domestic animal is not able to enforce the trust. Perhaps more than any other form of trust therefore, these other non-charitable purposes rely solely on the integrity of the trustee in carrying out his or her promises in accordance with his or her word.

The courts' rationale for upholding these trusts has generally been to say that they are inoffensive, and that there is no reason to deny their existence. However, the current author wishes to suggest that further justifications may exist. Firstly, these trusts, by their very nature are unlikely to create a trust in perpetuity – the trust is likely to exist only for a short time and will not therefore result in property being tied up in trust on an indefinite basis (*Roche v M'Dermott* [1901] 1 IR 394). Secondly, these trusts are not likely to comprise of large amounts of money – even though it is possible in theory for a person to give the entirety of a very substantial estate to the maintenance of a pet or the erection of a memorial. Thirdly, many of these trusts are likely to be a corollary to charitable trusts. Accordingly, there may be a reluctance by the courts to see what is a minor and short-term non-charitable purpose from defeating a wider charitable objective.

Accordingly, the following types of trusts have been upheld as valid non-charitable purposes.

The erection and maintenance of memorials and tombs that are not in churches

The maintenance of a memorial or a tomb in a church is likely to be charitable as being for the advancement of religion. However, where a tomb or a monument is situated elsewhere, then it may not be charitable, unless it falls under one of the other heads of charity such as culture and heritage (which will be discussed further in Chapter 19). However, the case of *In Re Hooper* [1932] 1 Ch 38 confirms that a trust for the maintenance and erection of a tomb or memorial that is not charitable may nevertheless be a valid trust. However, the obligation subsists only for a specific period. In *In Re Hooper* it was stated as being 21 years from the date of the deceased's death, which would have been the perpetuity period under the common law. Such a requirement would be far more problematic however under the perpetuity period set out under s.5 of the Perpetuities and Accumulations Act 2009 of 125 years, and it will be interesting to see how courts deal with trusts for the erection and maintenance of tombs and memorials in the future.

The saying of masses

Linked to the possibility of establishing a trust for the erection and maintenance of tombs and memorials, a settlor may also establish a trust for the purpose of saying masses in memory of deceased persons. Again, there are many instances where these may be charitable, and therefore this residual category of trust exists for circumstances where the saying of mass would not be charitable, such as where no public benefit would derive from the activity.

The maintenance of a specific animal

In the case of *In Re Dean* (1889) 41 Ch D 552, the settlor created a trust for the maintenance of his dogs and his ponies.

EXTRACT

In Re Dean (1889) 41 Ch D 552

North J

The first question is as to the validity of the provision made by the testator in favour of his horses and dogs. It is said that it is not valid; because (for this is the principal ground upon which it is put) neither a horse nor a dog could enforce the trust; and there is no person who could enforce it. It is obviously not a charity, because it is intended for the benefit of the particular animals mentioned and not for the benefit of animals generally . . . But, in my opinion, as it is not a charity, there is nothing in the fact that the annuity arises out of land to prevent its being a good gift.

Then it is said, that there is no cestui que trust who can enforce the trust, and, that the Court will not recognise a trust unless it is capable of being enforced by someone. I do not assent to that view. There is not the least doubt that a man may if he pleases, give a legacy to trustees, upon trust to apply it in erecting a monument to himself, either in a church or in a churchyard, or even in unconsecrated ground, and I am not aware that such a trust is in any way invalid, although it is difficult to say who would be the *cestui que* trust of the monument. In the same way I know of nothing to prevent a gift of a sum of money to trustees, upon trust to apply it for the repair of such a monument. In my opinion such a trust would be good, although the testator must be careful to limit the time for which it is to last, because, as it is not a charitable trust, unless it is to come to an end within the limits fixed by the rule against perpetuities, it would be illegal. But a trust to lay out a certain sum in building a monument, and the gift of another sum in trust to apply the same to keeping that monument in repair, say, for ten years, is, in my opinion, a perfectly good trust, although I do not see who could ask the Court to enforce it. If persons beneficially interested in the estate could-do so, then the present Plaintiff can do so; but, if such persons could not enforce the trust, still it cannot be said that the trust must fail because there is no one who can actively enforce it.

Is there then anything illegal or obnoxious to the law in the nature of the provision, that is, in the fact that it is not for human beings, but for horses and dogs? It is clearly settled by authority that a charity may be established for the benefit of horses and dogs, and, therefore, the making of a provision for horses and dogs, which is not a charity, cannot of itself be obnoxious to the law, provided, of course, that it is not to last for too long a period . . .

Nevertheless, the courts are very keen to emphasise that these types of trust are anomalous – they do not fit the definition of a private trust or a charitable trust, and it appears from the cases that the courts would prefer that they were not upheld, but because there are precedents in existence where these trusts have been recognised, the courts cannot ignore them. Nevertheless, there are numerous instances of the courts making it abundantly clear that these anomalous trusts should not be extended further. In the case of *Re Endacott* [1960] Ch 232 for example, Harman LJ explains:

> I applaud the orthodox sentiments expressed by Roxburgh J in *Re Astor's Settlement Trusts* [[1952] Ch. 534], and I think, as I think he did, that though one knows that there have been decisions at times which are not satisfactorily classified, but are perhaps merely occasions when Homer had nodded, at any rate these cases stand by themselves and ought not to be increased in number, nor indeed followed, except where the one is exactly like another. Whether it would be better that some authority should

> now say that those cases were wrongly decided, this perhaps is not the moment to consider. At any rate, I cannot think that a case of [the present] kind, the case of providing outside a church an unspecified and unidentified memorial is the kind of instance which should be allowed to add to those troublesome, anomalous and aberrant cases.

In the same case, Lord Evershed MR explains:

> I now turn to Mr. Arnold's alternative argument based on the view that there is here a trust and a trust of a public character, but not a charitable trust. What he says is, that the trust is in line with the trusts which were rendered effective in those cases which I have called 'anomalous,' and many of which are referred to in Roxburgh J.'s decision, beginning with *Pettingall v. Pettingall* [(1842) 11 LJ Ch 176]. I include in that list cases such as the three to which we have had our attention particularly drawn today. The argument is that assuming the non-charitable but public nature of this trust, still it is of a character which the court can efficiently, and will, enforce. It must be said that these cases are of a somewhat anomalous kind. They are classified in the recent book written by Mr. J. H. C. Morris and Professor Barton Leach, *The Rule Against Perpetuities* (1956) (p. 298). 'We proceed,' say the authors, 'to examine these 'anomalous' exceptions. It will 'be found that they fall into the following groups: (1) trusts for the erection or maintenance of monuments or graves; (2) trusts for the saying of masses, in jurisdictions where such trusts are not regarded as charitable; (3) trusts for the maintenance of particular animals; (4) trusts for the benefit of unincorporated associations (though this group is more doubtful); (5) miscellaneous cases.' I am prepared to accept, for the purposes of the argument, that it does not matter that the trusts here are attached to residue and not to a legacy; that is to say, it does not matter that the persons who would come to the court and either complain if the trusts were not being carried out, or claim the money on the footing that they had not been carried out, are next-of-kin rather than residuary legatees. Still, in my judgment, the scope of these cases (and I can call them anomalous because they have been so called both in the book of Mr. Morris and Professor Barton Leach and in the course of the argument) ought not to be extended. So to do would be to validate almost limitless heads of non-charitable trusts, even though they were not (strictly speaking) public trusts, so long only as the question of perpetuities did not arise; and, in my judgment, that result would be out of harmony with the principles of our law. No principle perhaps has greater sanction or authority behind it than the general proposition that a trust by English law, not being a charitable trust, in order to be effective, must have ascertained or ascertainable beneficiaries. These cases constitute an exception to that general rule. The general rule, having such authority as that of Lord Eldon, Lord Parker and my predecessor, Lord Greene M.R., behind it, was most recently referred to in the Privy Council in *Leahy v. Attorney-General for New South Wales*. I add also that, in my judgment, the proposition stated in Mr. Morris and Professor Barton Leach's book (p. 308) that if these trusts should fail as trusts they may survive as powers, is not one which I think can be treated as accepted in English law.

The courts' approach to justifying these anomalous trusts also indicates a departure from their usual approach, namely that the law of trusts tends to focus on the obligation of the trustees, and the need for that obligation to be enforceable. The central tenet comes from the judgment of *Morice v Bishop of Durham* (1805) 32 ER 1009, with its emphasis on the fact that an obligation is imposed upon the trustee and he or she must carry out that obligation. His or her willingness to act is not an issue, except in the sense

that a person may decline to act as trustee if he or she does not wish to undertake the obligation. However, the approach adopted by the courts in relation to anomalous non-charitable purposes is to consider the trustee's willingness to act, and to accept that if the trustee is willing to act as the settlor directs, then the court has no power to stop him or her from doing so. However, this approach could justify many forms of behaviour that are currently either criminal or illegal. In the context of the law of trusts for example, it could justify the existence of many trusts that are currently void for uncertainty, such as trusts that are void for uncertainty of subject matter, or trusts that are dismissed by the courts on the grounds of being administratively unworkable.

Chapter summary

This chapter may be useful for assessments and assignments on:

- Unincorporated associations
- Types of trusts
- Private v public trusts
- The beneficiary principle
- The validity of trusts for purposes
- The certainty of objects.

Further reading

Baughen, S. (2010) 'Performing animals and the dissolution of unincorporated associations: the "contract-holding theory" vindicated' *Conveyancer and Property Lawyer* 216.

Evans, S. (2010) 'Only people and horses' 154(22) *Solicitors' Journal* 16.

Gunston, W. and Robertson, A. (2008) 'The purpose trust' 1(4) *Corporate Rescue and Insolvency* 125.

Niegel, J. (2012) 'Purposeful trusts and foundations' 18(6) *Trusts and Trustees* 451.

Pawlowski, M. and Summers, J. (2007) 'Private purpose trusts – a reform proposal' *Conveyancer and Property Lawyer* 440.

19

Introduction to charities

Chapter outline

This chapter will cover:

- Defining a charity
- Charitable purposes
- Public benefit.

Introduction

This chapter is concerned with the law relating to charities. A charity is a particularly salient example of the trust principle in operation because the charity exemplifies the separation of legal and beneficial ownership that is the defining characteristic of the trust. When one gives a donation to a charity, it is clear that one's intention is not to benefit the charity as an organisation, but instead to fund the work carried out by that charity, or the charity's purpose. A donation to Cancer Research UK for example is not made with an intention to confer a benefit upon Cancer Research UK, but rather with the intention that the donation will contribute towards research into finding cures for different form of cancer. The charity is therefore an important form of the trust concept. It is also subject to stringent regulation by the law. Firstly, the law regulates what forms of activity may be classed as charitable. It is an interesting topic about which much may be written. The discussion of charities will therefore cover three chapters. This chapter addresses what a charity is and how it is defined. The next chapter (Chapter 20) will consider how the law regulates the operation of charities, while the one following that (Chapter 21) explains how charities are enforced. The final section of this chapter will consider the benefits of charitable status.

What is a charity?

The recognition of what constitutes a charity is important for two reasons. Firstly, it is important that an organisation seeking to acquire charitable status manifests as its objectives a purpose or purposes that are deemed to be charitable. Secondly, where *inter vivos* or will trusts are created with the intention to benefit a particular cause, it is important to ascertain whether or not that purpose is charitable, as the trust will be void for uncertainty of objects if a charitable purpose is not established.

In order for a trust or an organisation to be recognised as being charitable therefore, it is necessary to demonstrate that it fulfils three requirements. Section 1(1) of the Charities Act 2011[1] defines the first two of these requirements, namely that the purposes are exclusively charitable and that the institution is regulated by the High Court.

EXTRACT

Charities Act 2011, s.1(1)

(1) For the purposes of the law of England and Wales, 'charity' means an institution which–

(a) is established for charitable purposes only, and

(b) falls to be subject to the control of the High Court in the exercise of its jurisdiction with respect to charities.

Exclusively charitable purpose

A charity must therefore have a charitable purpose, and its purposes must be exclusively charitable – in other words charitable status will not be conferred if the organisation's

[1] (2011 c.25).

purposes include activities that are not charitable. In order to be valid, the purpose or purposes of the charity must fit within one or more of the categories (or heads of charity) detailed in s.3(1) Charities Act 2011. If some of the charity's purposes are outside these categories, then the trust will not be charitable. An example of a situation where a trust was found not to be exclusively charitable may be seen in the case of *Re Gillingham Bus Disaster Fund.*[2] One of the issues arising from this case concerned whether a fund created in the aftermath of a road accident wherein a number of children were killed or injured and which was '*to be devoted, among other things, to defraying the funeral expenses, caring for the boys who may be disabled, and then to such worthy cause or causes in memory of the boys who lost their lives*' could be regarded as charitable. According to the judgment of Lord Evershed MR[3] 'worthy causes' could conceivably include charitable purposes. However non-charitable causes could also be regarded as worthy. The trust therefore failed because of the uncertainty regarding the intentions of the trust, and because its purposes could not be regarded as being exclusively charitable.

It is possible for an organisation to manifest itself as a number of different entities, with one section being exclusively charitable, while other sections engage in activities that would not fulfil the objectives of a charity. An example may be seen in relation to Amnesty International UK which has some purposes that are charitable (such as raising awareness of maternal health issues in developing countries), but also engages in some activities that are not charitable (campaigning). The organisation is separated into sections therefore – Amnesty International UK Section and Amnesty International UK Section Charitable Trust. Through the charitable trust, Amnesty International UK is therefore able to take advantage of the benefits of charitable status discussed in this chapter by being a charity for the promotion of human rights. However, its political activities and campaign work, which would not be regarded as charitable for the reasons discussed later in this chapter, may continue under the auspices of the non-charitable section. The extract below provides the objects clause of both the charitable trust and the non-charitable company.

EXTRACT

Memorandum and Articles of Association of the Amnesty International (UK Section) Charitable Trust

Objects

3.1 To promote human rights (as set out in the Universal Declaration of Human Rights ('UDHR') and subsequent United Nations conventions and declarations and in regional codes of human rights which incorporate the rights contained in the UDHR and those subsequent conventions and declarations) throughout the world by all or any of the following means:-

(a) monitoring abuses of human rights;

(b) obtaining redress for the victims of human rights abuse;

(c) relieving need among the victims of human rights abuse;

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[2] *In Re Gillingham Bus Disaster Fund, Bowman and Others v Official Solicitor and Others* [1959] Ch 62.
[3] At p.71.

(d) research into human rights issues;
(e) educating the public about human rights;
(f) providing technical advice to government and others on human rights matters;
(g) contributing to the sound administration of human rights law;
(h) commenting on proposed human rights legislation;
(i) raising awareness of human rights issues;
(j) promoting public support for human rights;
(k) promoting respect for human rights among individuals and corporations;
(l) international advocacy of human rights; and
(m) eliminating infringements of human rights.

Powers

3. to further its objects the Company may:

3.1 engage in political activities provided that the Trustees are satisfied that the proposed activities will further the purposes of the Company to an extent justified by the resources committed and the activities are not the dominant means by which the Company carries out its objects;

3.2 provide and assist in the provision of money, materials or other help;

3.3 organise and assist in the provision of conferences, courses of instruction, exhibitions, lectures and other educational activities;

3.4 publish books, pamphlets, reports, leaflets, journals, films, tapes and instructional matter on any media;

3.5 promote, encourage, carry out or commission research, surveys, studies or other work, making the useful results available;

3.6 provide or procure the provision of counselling and guidance;

3.7 alone or with other organisations seek to influence public opinion and make representations to and seek to influence governmental and other bodies and institutions regarding the development and implementation of appropriate policies provided that all such activities shall be conducted on the basis of well-founded, reasoned argument and shall in all other respects be confined to those which an English charity may properly undertake;

3.8 acquire any real or personal property and any rights or privileges and construct and maintains, alter and equip any buildings;

3.9 subject to any consent required by law dispose of or deal with all or any of its property with or without payment and subject to such conditions as the Trustees think fit;

3.10 subject to any consent required by law borrow or raise and secure the payment of money;

3.11 invest the Company's money not immediately required for its objects in or upon any investments, securities, or property;

3.12 delegate the management of investments to a financial expert provided that:

(a) the financial expert is:

(b) an individual who is an authorised person within the meaning of the Financial Services and Markets Act 2000; or

(c) a company or firm of repute which is an authorised or exempt person within the meaning of that Act except persons exempt solely by virtue of Article 44 and/or Article 45 of the Financial Services and Markets Act 2000 (Exemption) Order 2001.

3.12.2 the investment policy is set down in writing for the financial expert by the Trustees;

3.12.3 every transaction is reported promptly to the Trustees;

3.12.4 the performance of the investments is reviewed regularly by the Trustees;

3.12.5 the Trustees are entitled to cancel the delegation arrangement at any time;

3.12.6 the investment policy and the delegation arrangements are reviewed at least once a year;

3.12.7 all payments due to the financial expert are on a scale or at a level which is agreed in advance and are notified promptly to the Trustees on receipt;

3.12.8 the financial expert may not do anything outside the powers of the Trustees;

3.13 arrange for investments or other property of the Company to be held in the name of a nominee (being a corporate body registered or having an established place of business in England and Wales) under the control of the Trustees or a financial expert acting under their instructions and to pay any reasonable fee required;

3.14 lend money and give credit to, take security for such loans or credit and guarantee or give security for the performance of contracts by any person or company;

3.15 open and operate bank accounts and other facilities for banking and draw, accept, endorse, issue or execute promissory notes, bills of exchange, cheques and other instruments;

3.16 subject to clause 4.16 raise funds by way of subscription, donation or otherwise;

3.17 trade in the course of carrying out the objects of the Company and carry on any other trade which is not expected to give rise to taxable profits;

3.18 incorporate subsidiary companies to carry on any trade;

3.19 subject to clause 5 engage and pay employees and professional or other advisers and make reasonable provision for the payment of pensions and other retirement benefits to or on behalf of employees and their spouses and dependants;

3.20 establish and support or aid in the establishment and support of any other charitable organisations and subscribe, lend or guarantee money or property for charitable purposes;

3.21 undertake and execute charitable trusts;

3.22 amalgamate or co-operate with any Company having charitable objects wholly or in part similar to those of the Company;

3.23 acquire or undertake all or any of the property, liabilities and engagements of charities with which the Company may co-operate or federate;

3.24 pay out of the funds of the Company the costs of forming and registering the Company;

3.25 provide indemnity insurance to cover the liability of the directors which by virtue of any rule of law would otherwise attach to them in respect of any negligence, default, breach of trust or breach of duty of which they may be guilty in relation to the company: Provided that any such insurance shall not extend to any claim arising from any act or omission which the directors knew to be a breach of trust or breach of duty or which was committed by the directors in reckless disregard to whether it was a breach of trust or breach of duty or not provided also that any such insurance shall not extend to the costs of any unsuccessful defence to a criminal prosecution brought against the directors in their capacity as directors of the company;

3.26 do all such other lawful things as shall further the Company's objects.

Source: https://www.amnesty.org.uk/sites/default/files/trust_constitution_7.pdf. Site accessed 13 January 2013.

EXTRACT

Memorandum and Articles of Association of Amnesty International UK Section

Powers

4. To further its objects the Company may

4.1 provide and assist in the provision of money, materials or other help;

4.2 organise and assist in the provision of conferences, courses of instruction, exhibitions, lectures and other educational activities;

4.3 publish books, pamphlets, reports, leaflets, journals, films, tapes and instructional matter on any media;

4.4 promote, encourage, carry out or commission research, surveys, studies or other work, making the useful results available;

4.5 provide or procure the provision of counselling and guidance;

4.6 alone or with other organizations seek to influence public opinion and make representations to and seek to influence governmental and other bodies and institutions regarding the development and implementation of appropriate policies;

4.7 acquire any real or personal property and any rights or privileges and construct and maintain alter and equip any buildings;

4.8 deal with all or any of its property with or without payment and subject to such conditions as the Directors think fit;

4.9 borrow or raise and secure the payment of money;

4.10 invest the Company's money not immediately required for its objects in or upon any investments, securities or property;

4.11 delegate the management or investments to a financial expert provided that:

4.11.1 the financial expert is:

(a) an individual who is an authorised person within the meaning of the Financial Services and Markets Act 2000; or

(b) a company or firm of repute which is an authorised or exempt person within the meaning of that Act except persons exempt solely by virtue of Article 44 and/or Article 45 of the Financial Services and Markets Act 2000 (Exemption) Order 2001.

4.11.2 the investment policy is set down in writing for the financial expert by the Directors;

4.11.3 every transaction is reported promptly to the Directors;

4.11.4 the performance of the investments is reviewed regularly by the Directors;

4.11.5 the Directors are entitled to cancel the delegation arrangement at any time;

4.11.6 the investment policy and the delegation arrangements are reviewed at least once a year;

4.11.7 all payments due to the financial expert are on a scale or at a level which is agreed in advance and are notified promptly to the Directors on receipt;

4.11.8 the financial expert may not do anything outside the powers of the Directors;

4.12 arrange for investments or other property of the Company to be held in the name of a nominee (being a corporate body registered or having an established place of business

in England and Wales) under the control of the Directors or a financial expert acting under their instructions and to pay any reasonable fee required;

4.13 lend money and give credit to, take security for such loans or credit and guarantee or give security for the performance of contracts by any person or company;

4.14 open and operate bank accounts and other facilities for banking and draw, accept, endorse, issue or execute promissory notes, bills of exchange, cheques and other instruments;

4.15 raise funds by way of subscription, donation or otherwise;

4.16 trade in the course of carrying out the objects of the Company and carry on any other trade;

4.17 incorporate subsidiary companies to carry on any trade;

4.18 subject to clause 5 engage and pay employees and professional or other advisers and make reasonable provision for the payment of pensions and other retirement benefits to or on behalf of employees and their spouses and dependants;

4.19 establish and support or aid in the establishment and support of any other organizations and subscribe, lend or guarantee money or property;

4.20 amalgamate or co-operate with any organisation having objects wholly or in part similar to those of the Company;

4.21 acquire or undertake all or any of the property, liabilities and engagements of organisations with which the Company may co-operate or federate;

4.22 provide indemnity insurance to cover the liability of the Directors which by virtue of any rule of law would otherwise attach to them in respect of any negligence, default, breach or trust or breach of duty of which they may be guilty in relation to the Company: Provided that any such insurance shall not extend to any claim arising from any act or omission which the Directors knew to be a breach of trust or breach of duty or which was committed by the Directors in reckless disregard to whether it was a breach of trust or breach of duty or not provided also that any such insurance shall not extend to the costs of any unsuccessful defence to a criminal prosecution brought against the Directors in their capacity as Directors of the Company; and

4.23 do all such other lawful things as shall further the Company's objects.

Source: https://www.amnesty.org.uk/sites/default/files/trust_constitution_7.pdf. Site accessed 13 January 2013.

Subject to the control of the High Court

The second requirement, detailed in s.1(1)(b) Charities Act 2011 is that the organisation must be subject to the control of the High Court. This is an issue that will be discussed in Chapter 20 as it has greater bearing on the regulation of charities rather than how they are defined.

Public benefit

The third requirement is contained in s.2(1)(b) Charities Act 2011 which requires a charity to confer a public benefit. Unless these three aspects can be proved, an organisation will not be charitable, and a gift or a legacy purporting to be for a purpose rather than a person will also not be charitable. From the perspective of the person giving legal advice therefore, it is necessary to address each of these issues in turn. As with other areas of law, there has been considerable scope within the law of charities for arguing whether or not a particular activity is consistent with one of the recognised heads of charity, and

whether or not a sufficient public benefit is manifested. Accordingly, the decision regarding whether or not a trust will be charitable will ultimately rest on the extent to which the lawyer convinces the court that the instant case should be compared to or distinguished from earlier authorities. It is not possible in this chapter to give a definitive indication of what is charitable and what is not – instead, the aim is to provide an indication of the courts' approaches to determining whether or not a specific activity is a charitable purpose and whether or not a public benefit is manifested. The law student must therefore consider how those guiding principles would – or would not – apply to a given situation.

IS THE TRUST CHARITABLE?

Do its objectives fulfil one of the charitable purposes of the Charities Act 2011, s.2(2)?
Is it subject to the control of the High Court?
Is there a public benefit?

Establishing a charitable purpose

This section will consider in greater detail what purposes may be regarded as charitable, and the types of activities that will fulfil those purposes. The Charities Act 2011, s.3(1) lists the purposes that may be charitable, and in order to be charitable, the organisation must demonstrate that it fulfils one of these purposes. The case law on charities may provide illustrations of the types of activities that have been accepted as charitable purposes in the past. As will be seen, the types of activities that have been accepted as charitable are not exhaustive, and there is considerable scope for differing viewpoints within the cases as regards whether or not a particular activity is charitable. Nevertheless, the precedents may provide the reader with a useful starting point for formulating an argument as to why an activity ought – or ought not – to be charitable.

EXTRACT

Charities Act 2011, s.3(1)

3 Meaning of 'charitable purpose'

(1) A purpose falls within this subsection if it falls within any of the following descriptions of purposes-

(a) the prevention or relief of poverty;

(b) the advancement of education;

(c) the advancement of religion;

(d) the advancement of health or the saving of lives;

(e) the advancement of citizenship or community development;

(f) the advancement of the arts, culture, heritage or science;

(g) the advancement of amateur sport;

(h) the advancement of human rights, conflict resolution or reconciliation or the promotion of religious or racial harmony or equality and diversity;

(i) the advancement of environmental protection or improvement;

(j) the relief of those in need by reason of youth, age, ill-health, disability, financial hardship or other disadvantage;

(k) the advancement of animal welfare;

(l) the promotion of the efficiency of the armed forces of the Crown, or of the efficiency of the police, fire and rescue services or ambulance services;

(m) any other purposes within subsection (4).

Accordingly, in order to prove that a trust is charitable, the first aspect that needs to be satisfied is that the purposes of the trust fall within one or more of these headings. The range of purposes that may be charitable within the section is extremely broad, and it is entirely possible that a number of existing charities may fulfil more than one of the charitable purposes listed. It is entirely possible, for example, that a charity that advances education under s.3(1)(b) may also advance the arts, culture, heritage or science under s.3(1)(f) as is the case with the example given below of Skylight Circus Arts, a charity whose objectives relate to the educative role of the performing arts.

EXTRACT

Objectives of Skylight Circus Arts

Skylight Circus Arts aims to empower individuals and communities through the learning, practise and discipline of physical circus skills.

We create healthy bodies through improving coordination, fitness, strength, flexibility and stamina and healthy minds through improving concentration, teamwork, communication, setting and achieving targets, self-image and self-esteem, the joy of achieving skills and the freedom to play.

Circus Skills can be taught or explored as a one-off experience, a short course, or on a regular basis in the context of life-long learning for hobby or career. Once they have been mastered, circus skills can become Circus Arts.

Circus Arts can be performed on the street, on stage, at parties, on cruise ships, at huge festivals or in your living room.

We believe that Circus

- has no limits, anything is possible, imagination rules
- is not bound by convention, anything can happen and often it does
- can be magical, fun, beautiful, serious, sad, dangerous, funny, animated, dramatic and daring
- can tell stories or it can be pure art
- can raise serious issues, tackle them and find the humour in them, helping us to laugh at ourselves
- does not exclude, anyone is welcome and everyone is included
- is colourful and exciting, but never boring

- is not constrained by language, it speaks of human endeavor, the will to thrive, to succeed, to improve, to excel, to overcome obstacles, to work together and to laugh through tears
- is not just for children, it plays to the child in all of us

Source: http://www.skylightcircusarts.com/?About_Skylight:Aims_and_Beliefs. Site accessed 13 January 2013.

Despite the breadth of the purposes that may be charitable under s.3(1), defining precisely what activities will fulfil the charitable purposes of the Charities Act 2011 is left to the courts. Accordingly, the cases that defined charitable purposes prior to the Charities Act 2006 (the provisions of which were consolidated in the 2011 Act) continue to be used in order to explain what sorts of activities would be classed as charitable purposes. Prior to the Charities Act 2006, the range of charitable purposes was much narrower, and were classified under four broad headings identified by Lord Macnaghten in the case of *Income Tax Special Purposes Commissioners v Pemsel*,[4] namely the relief of poverty, the advancement of education, the advancement of religion and trusts for other purposes beneficial to the community.[5] Therefore, although the purpose continues to be charitable, it may be more appropriately classified under one of the newer charitable purposes of s.3(1) rather than being justified on the basis of one of Lord Macnaghten's classifications. Alternatively of course, it may be possible for a charity to be defined as having one of the newer charitable purposes detailed in s.3(1), in addition to one of the older purposes that appear both in the Charities Act 2011 and in Lord Macnaghten's classifications in *Pemsel*.

Public benefit

The second requirement of a valid charity is that it must provide a benefit to the public. It is necessary at this juncture to explain the interaction of the legislation and the case law. Much of the case law pre-dates the legislation. However the case law remains good law for the most part, except that the Charities Act 2006 introduced for the first time the requirement that public benefit must be demonstrated in relation to all types of trust (s.3(2)). This requirement is re-enacted in s.4 of the Charities Act 2011. This raises two key considerations, namely:

- Does the activity actually provide a benefit? and
- Is the benefit conferred upon a sufficiently large section of the public?

Does the trust confer a public benefit?

Firstly it must be decided whether the trust actually provides something that the public may benefit from. This means that there must be some social value to the proposed activity, with the result that in the context of education for example, the activity must actually improve education as opposed to increasing knowledge.[6] However, the dividing line between what is educational and what merely increases knowledge is a difficult one to draw, and much will therefore depend on the court's opinion of the social utility of the proposed activity.

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[4] *Income Tax Special Purposes Commissioners v Pemsel* [1891] AC 531.
[5] *Income Tax Special Purposes Commissioners v Pemsel* [1891] AC 531 per Lord Macnaghten at p583.
[6] *Re Shaw, Public Trustee v Day* [1957] 1 All ER 745.

Furthermore, the activity must involve some degree of engagement with the public, with the result that research must be disseminated,[7] recreational charities must allow for wide community participation and the advancement of religion cannot occur where the trust's beneficiaries are a closed order.[8]

EXTRACT

Re Pinion Decd, Westminster Bank Ltd v Pinion and Another [1965] Ch 85

Case facts

The testator in this case made a will directing that his artist's studio was to be turned into a museum that displayed various artworks, as well as items of furniture, china, glassware etc. Some of the atrociously bad pictures had been painted by the testator himself (mainly of his grandparents and other people with whom the testator had a connection), while others were the works of other painters. Other objects included trophies that the testator's father had won, his grandmother's coffee jug, two commodes and various items of (mainly damaged) china. The studio was shabby and unremarkable, and its contents were described as being a haphazard collection of poor-quality items, that did not belong to any specific period or style and had very little value. The court was called upon to decide whether the trust was charitable. Wilberforce J considered that once a trust was regarded as educational, it was not for the court to prefer one form of education over another. Accordingly it became necessary in his view to consider whether the trust was educational at all.

Wilberforce J (at p.96)

In my judgment, therefore, the court can, and indeed must, in this case receive evidence to support or negative the existence in this gift of educational value or public benefit. No doubt it must be cautious in the receipt of such evidence: as Lord Simonds put it 'the court will not be astute . . . to defeat on doubtful evidence the avowed benevolent intention of a donor': *National Anti-Vivisection Society v. Inland Revenue Commissioners*. Particularly where it is dealing with a subject matter in the sphere of art or aesthetics it must allow for the difficulty there is in making any secure objective judgment, for changes in fashion and in taste. It should recognise that the formation of an educated taste is a complex process, differing greatly as between individuals. It must allow for the differences – very great differences – of education and taste to be found among the members of the public who are likely to see the bequest. Nevertheless, making all these necessary allowances, there must come a point when the court, on the evidence, is impelled to say that no sufficient element of benefit to the public is shown to justify the maintenance in perpetuity of the subject matter given. A strong and a clear case has to be made before such a conclusion can be reached: Is this case sufficiently strong and clear? I now proceed to consider the evidence . . .

Outcome

Wilberforce J concluded that a small benefit could be provided to the public from the bequest, even if its only effect was to encourage the public to seek out work of a better quality. The Court of Appeal accepted Wilberforce J's reasoning, but not his conclusions. Harman LJ explains.

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[7] This was one of the stipulations in the case of *Re Besterman's Will Trusts* (21 January 1980, Unreported) per Slade J, and repeated by him in *McGovern v A-G* [1982] Ch 321 at 352–353.

[8] *Gilmour v Coats* [1949] AC 426.

Harman LJ (p.107)

The judge with great hesitation concluded that there was that scintilla of merit which was sufficient to save the rest. I find myself on the other side of the line. I can conceive of no useful object to be served in foisting upon the public this mass of junk. It has neither public utility nor educative value. I would hold that the testator's project ought not to be carried into effect and that his next-of-kin is entitled to the residue of his estate.

Davies LJ (p.108)

Wilberforce J. found himself just able to decide that the exhibition of the dozen or two dozen third-rate chairs together with a few of the other articles might have some educational value; and so he upheld the gift. But, as my Lord has pointed out, the testator's declared intention was that the whole collection should remain intact save for 'any goods and chattels not of an antique nature.' And if this were done, it is obvious that the chairs, such as they are, would be smothered by the intolerable deal of rubbish.

I, therefore, agree that the gift is bad.

Russell LJ

The mere fact that a person makes a gift of chattels to form a public museum cannot establish that its formation will have a tendency to advance education in aesthetic appreciation or in anything else. Inquiry must first be made, what are the chattels? Five hundred balls of string could not have that tendency. Nor is the inquiry ended on finding that the chattels are household furniture, carpets, light fittings, paintings, china and so forth: otherwise the contents of any dwelling-house in the land, if displayed to the public, could be said to have a tendency to advance education in aesthetic appreciation – which would, I think, be absurd. Some further judicial inquiry is needed directed to the quality of those chattels. The judge cannot conduct that inquiry on his own, unless the matter be so obvious as to call for no hesitation. He may be lacking in aesthetic appreciation. He is, I consider, entitled to the assistance of people expert in such matters, and to arrive at a conclusion based on such assistance. If the conclusion so based is that the quality of the articles is such that their exhibition to the public cannot be reasonably supposed to have the tendency mentioned, there is no charitable gift.

Outcome

Accordingly, the Court of Appeal decided unanimously that the appeal ought to be allowed, and that therefore the trust should not be charitable, as there was no educational benefit to be derived from it.

Although a benefit to the public must be demonstrated, it is not necessary to show that the approach taken by the purported charity is the most effective means of benefiting the public, merely that *some* benefit to the public ensues, as Vaisey J explains in the case of *In Re Shaw's Will Trusts*.[9] Correcting vulgarities of speech and defects of manners may not be the only method of giving individuals the opportunity to succeed in society, and indeed some may argue that the perception of vulgarities of speech and defects of manners represents a very specific view of appropriate behaviour. Nevertheless, the purpose of the trust in *In Re Shaw's Will Trusts* was for the advancement of education, and therefore the purposes of the trust could legitimately be regarded as being for the public benefit, irrespective of whether one agrees with the appropriateness of methods of education being proposed.

[9] [1952] Ch 163.

EXTRACT

In Re Shaw's Will Trusts, National Provincial Bank Ltd. v National City Bank Ltd. and Others [1952] Ch 163

Case facts

The case was concerned with a trust which aimed to make the fine arts accessible to the people of Ireland and also to provide training to correct 'vulgarities of speech and other defects' of manners that would prevent otherwise capable individuals from succeeding in society.

Vaisey J

The court ought not to weigh the respective merits of particular educational methods; it will suffice if the purposes are genuinely educational in their aim and scope.

Outcome

Accordingly, the trust was recognised as being charitable.

Benefit must be conferred upon a sufficient section of the public

Secondly, if the trust does confer a benefit to the public in terms of social value or utility, the benefit must be conferred upon a sufficient section of the public – a trust will not be charitable if the benefit it purports to confer is limited to a narrow group of people. The reasoning is simple – a trust cannot benefit the public if the beneficiaries consist of only a small number of individuals. It is not necessary however that the trust benefits everyone in society, merely that the group of beneficiaries is large enough to class as 'the public'. The courts will therefore have regard to the size of the proposed group, and also the question of whether the group of beneficiaries is defined by its personal connection to an individual or an organisation. The question of whether the trust benefits a sufficient section of the public raises a number of considerations, discussed in greater detail in the following sections, namely whether the size of the group is sufficiently large to constitute the public, whether the group is defined by a personal nexus, whether it is permissible to confer a benefit on a section of a larger community, and the extent to which the trust may legitimately exclude specific groups of people.

Beneficiaries must not be numerically negligible

In order for the trust to be for the benefit of the public, the beneficiaries must not be too small in number. It seems that the distinction drawn by the court is whether the beneficiaries are a community or whether they are a group of private individuals, as Lord Wrenbury explains in the case of *Verge v Somerville*.[10] Therefore the residents of a village or town may be regarded as a section of the public, as may people of a particular profession, but a very small group of individuals will not be regarded as being sufficiently numerous to constitute the public.

[10] [1924] AC 496.

EXTRACT

Verge v Somerville [1924] AC 496

Case facts

This case concerned a trust for the benefit of returned soldiers in New South Wales.

Lord Wrenbury

To ascertain whether a gift constitutes a valid charitable trust so as to escape being void on the ground of perpetuity, a first inquiry must be whether it is public – whether it is for the benefit of the community or of an appreciably important class of the community. The inhabitants of a parish or town, or any particular class of such inhabitants, may, for instance, be the objects of such a gift, but private individuals, or a fluctuating body of private individuals, cannot.

Outcome

Returned soldiers could be regarded as a community and the trust was therefore found to be charitable.

Beneficiaries must not be defined by a personal nexus

It is also necessary to show that a benefit is conferred upon a group of beneficiaries that is not defined by some personal connection or nexus to the settlor – a trust for the benefit of one's family members for example will not be charitable. Accordingly, even a very large group of private individuals will not be classed as the public for the purposes of the law relating to charities and so will not be charitable if they are selected on the basis of their connection to a particular individual, organisation or society. However, persons within a particular geographical location or persons in a particular field of work (e.g. teachers or railway employees) will be regarded as a sufficient section of the public in that they constitute a community of which many different people can be a member. On the other hand, those identified by their connection to a particular entity are not a community, in that their membership is determined either by their connection to a particular individual or on the basis of their having been selected in some way.

This may seem like a reasonably straightforward distinction, but it is not without its problems. Consider the following paradox. In the days before rail privatisation there was one rail company – the nationalised British Rail – for whom all railway employees would have worked. We have seen above that railway workers could be regarded as a community for the purpose of setting up a charitable trust for their benefit. However, employees of British Rail would have been regarded as a group of private individuals owing to their connection to the organisation, British Rail. As such, they would not constitute 'the public' and so a charitable trust for their benefit would not be permitted. However, in this instance both groups would have been composed of exactly the same people. How can this be reconciled?

EXTRACT

Oppenheim v Tobacco Securities [1951] AC 297

Case facts

The trust in this case was an educational trust for the benefit of the children of current and former employees of a large company. Accordingly, the potential beneficiaries of the trust numbered in excess of 110,000.

Lord Simonds

If I may begin at the bottom of the scale, a trust established by a father for the education of his son is not a charity. The public element, as I will call it, is not supplied by the fact that from that son's education all may benefit. At the other end of the scale the establishment of a college or university is beyond doubt a charity. 'Schools of learning and free schools and scholars of universities' are the very words of the preamble to the Statute of Elizabeth. So also the endowment of a college, university or school by the creation of scholarships or bursaries is a charity and none the less because competition may be limited to a particular class of persons. It is upon this ground, as Lord Greene, M.R., pointed out in *In re Compton* [[1946] 1 All ER 117], that the so-called Founder's Kin cases can be rested. The difficulty arises where the trust is not for the benefit of any institution either then existing or by the terms of the trust to be brought into existence, but for the benefit of a class of persons at large. Then the question is whether that class of persons can be regarded as such a 'section of the community' as to satisfy the test of public benefit. These words 'section of the community' have no special sanctity, but they conveniently indicate first, that the possible (I emphasize the word 'possible') beneficiaries must not be numerically negligible, and secondly, that the quality which distinguishes them from other members of the community, so that they form by themselves a section of it, must be a quality which does not depend on their relationship to a particular individual. It is for this reason that a trust for the education of members of a family or, as in *In re Compton*, of a number of families cannot be regarded as charitable. A group of persons may be numerous but, if the nexus between them is their personal relationship to a single propositus or to several propositi, they are neither the community nor a section of the community for charitable purposes.

Outcome

The trust was therefore held not to be charitable.

At the two extremes of the spectrum, Lord Simonds' categorisation seems to be very simple – trusts for one's family members are not charitable, while trusts for the benefit of the public are charitable. However, in practice, the distinction is often far more difficult to draw. Accodingly, a trust for children at a particular school may be charitable, as Lord Simonds explains in *Oppenheim v Tobacco Securities* (above) even though they are defined by their connection to a particular organisation, namely the school at which they are enrolled, and even though admission to the school has been as a result of specific selection criteria (such as examination performance, faith or the ability to pay the fees). In practice therefore, it can be difficult to ascertain whether a group of people is a section of the community or whether it is a fluctuating group of individuals, with the result that in *Williams' Trustees v Inland Revenue Commissioners*[11] Welsh people living in London were not regarded as a section of the community.[12]

[11] [1947] AC 447.

[12] However, the lack of a clear charitable purpose, and the connection to the London Welsh Association, was also significant in this instance.

Therefore distinction appears to be based on whether there is a relationship of dependence between the beneficiaries and the individual or organisation. Accordingly, a family connection or a connection to a particular company will suggest a relationship of dependence (either familial or contractual) and accordingly, a trust that would benefit such a group would not be regarded as charitable. On the other hand, pupils at a particular school are more easily categorised as being defined as a section of the community (children or adolescents) within a geographical location, and therefore charitable status is more readily recognised. As with many other issues of law therefore, the question of whether a purported charitable purpose benefits the public or a section of the public, or whether it merely benefits an individual, will be a matter for the lawyers to argue and for the courts to construe.

Beneficiaries may be a section of the public

It is permissible for a valid charitable gift to benefit a section of the public, as opposed to the public at large. Trusts for particular sections of the public who have specific needs, such as women, children, people from a common profession, the elderly, people of a particular nationality or people suffering from disabilities may be charitable. Equally trusts for people living in a particular geographical location may have charitable status, provided that the geographical location is not too narrow. A charitable trust may exist for the inhabitants of a village or town, but a trust is unlikely to be accepted as being charitable if the beneficiaries are the residents of a particular street or a very small area. Accordingly, a trust that benefits a section of the public may be charitable, provided that that section of the public is not defined with reference to an individual or individuals or an organisation. The following examples are examples of charitable purposes that benefit particular sectors of the public, in that the benefit is primarily conferred on people who are defined by certain characteristics (age, sex etc.) or geographical location.

EXTRACTS

Purposes of Save The Children Fund

To relieve the distress and to promote the welfare of children in any country or countries, without differentiation on the ground of race, colour, nationality, creed or sex to educate the public concerning the nature, causes and effects of distress, and want of welfare as aforesaid, and to conduct and procure research concerning the same and to make available the useful results thereof.

Source: http://apps.charitycommission.gov.uk/Showcharity/RegisterOfCharities/PrintReport.aspx?RegisteredCharityNumber=213890&ReportType=BW. Site accessed 21 January 2014.

Purposes of The Disabled People's Electronic Village Hall

The disabled people's electronic village hall exists to provide top quality training in computer use and related careers for disabled and disadvantaged people in order to improve their lifestyles, education and employment prospects.

Source: http://apps.charitycommission.gov.uk/Showcharity/RegisterOfCharities/PrintReport.aspx?RegisteredCharityNumber=1048748&ReportType=BW. Site accessed 21 January 2014.

Purposes of The Aberystwyth Silver Band

The principal aim of the Aberystwyth Silver Band is to support local tourism, civic duty and charity fund-raising events through the media of music. It performs in association with local choral societies in particular to promote this aim.

Source: http://apps.charitycommission.gov.uk/Showcharity/RegisterOfCharities/PrintReport.aspx?RegisteredCharityNumber=1004037&ReportType=BW. Site accessed 21 January 2014.

ACTIVITY

Using the paper-based or electronic resources available in your law library, search for a case where the beneficiaries were defined as being a section of the public. Compare this case with the judgment in *Oppenheim v Tobacco Securities*. What characteristics do you consider to be significant when the courts determine whether a trust is for the benefit of a group of individuals or whether it is for the benefit of a section of the public?

Manifesting a preference for particular individuals or groups in a trust that otherwise confers a public benefit

A further dimension to the question is added by the fact that a charitable purpose that confers a benefit on the public or a section of the public could possibly be valid even where a preference is expressed for conferring the benefit on a particular class of persons within that community. Such a trust was accepted as being charitable in the case of *Re Koettgen's Will Trusts*,[13] although it was significant in this case that the exercise of the preference in favour of the company employees and their families was not mandatory, and that the preference was not to be exercised in respect of the entirety of the trust fund. The Charity Commission's guidelines regarding the manifestation of such a preference also indicate that such an approach would no longer be acceptable.[14] Nevertheless, the decision in *Re Koettgen's Will Trusts* continues to be an authority in favour of the validity of purported charitable purposes where a preference is manifested in favour of a particular group, and therefore it remains to be seen how the courts will deal with trusts that manifest a preference in this way in the future. Given the Charity Commission's enhanced role in determining whether a trust is charitable however (discussed later in this chapter), it is anticipated that there will be a reluctance to accept as charitable those trusts where a preference is manifested in favour of benefiting a particular group, unless the offending clause can be severed from the wider objectives of the trust, or an appropriate cy-près scheme (discussed in greater detail later in this chapter) can be devised.

[13] [1954] Ch 252.

[14] Charity Commission (2008) *Analysis of the Law Underpinning Public Benefit and the Advancement of Education*. http://www.charity-commission.gov.uk/Library/guidance/pblawae.pdf March 2008. Site accessed 18 January 2011. Paragraphs 2.24–2.25.

EXTRACT

Re Koettgen's Will Trusts, Westminster Bank Ltd. v Family Welfare Association Trustees Ltd. and Others [1954] Ch 252

Case facts

This case concerned a trust for providing education for those who wished to pursue a commercial career, but who did not have the means to pay for the tuition. The testatrix however expressed that when allocating the trust fund, preference ought to be given to applicants who were the employees of a particular company or their families.

Upjohn J

The matter must be approached by asking the question: who are eligible under the will? They must be 'persons of either sex who are British born subjects and who are desirous of educating themselves or obtaining tuition for a higher commercial career but whose means are insufficient or will not allow of their obtaining such education or tuition at their own expense . . .' That is the primary class.

If the will concluded there, the trust would clearly be a valid charitable trust, having regard to the admission that a gift for commercial education is for the advancement of education.

The next task is to make a selection from that primary class of eligible persons. At that stage there is a positive direction to give a preference to the employees of John Batt & Co. and members of their families. In some years there might be sufficient members of such limited class to fill the 75 per cent. available for them, and in other years there might not be. The evidence, as I have said, is inconclusive on this point. The time may come when John Batt & Co. (London) Ld. ceases to carry on business, and in that event the income of the whole trust fund must be applied for the benefit of the primary class which fulfils qualifications contained in subclause (d).

It is only when one comes to make a selection from that primary class that the employees of John Batt & Co. and the members of their families come into consideration, and the question is, does that direction as to selection invalidate the primary trust? In my judgment it does not do so.

Outcome

Accordingly, the trust was found to be charitable.

Will there be a public benefit if the trust discriminates against particular groups?

The modern importance of the concepts of equality and non-discrimination means that although older trusts may have legitimately purported to confer a benefit only on a particular group,[15] the question of whether, and the extent to which, a purported charitable purpose may discriminate against particular groups must therefore be addressed. The law's approach has been to regard charities that only confer a benefit on persons of a

[15] In the case of *Re Gwyon* [1930] 1 Ch 255, for example, although the court took issue with the exclusion of children who were supported by a charitable institution, there was no objection to the fact that black children could not benefit.

particular colour as being for the benefit of persons generally.[16] Therefore a charitable trust for white people will be construed as conferring a benefit on all persons. However, charities may legitimately continue to limit the class of beneficiaries with reference to other indicators of race, such as national or ethnic origin or racial grouping.[17] Nevertheless, the Charity Commission's guidelines indicate that it will consider whether the discriminatory element is justified as a matter of ensuring that the trust benefits the public.[18] In some cases, an apparently discriminatory element may be justified – single-sex schools for example may be legitimate charitable purposes. Similarly, charities may legitimately confer a benefit only on persons of one sex (such as Women's Aid). The Charity Commission's approach therefore is to consider whether the discriminatory element is necessary. If it is not necessary, then the Charity Commission will advise the organisation to alter its objectives so that it does not operate in a discriminatory manner.

Indirect public benefit

The third issue to be considered is whether an indirect benefit to the public will be acceptable. If the benefit is only conferred upon a small section of the public (e.g. children), the trust may be charitable if there is an indirect benefit to the public more generally. For example, the primary beneficiary of a scholarship will be the recipient of the fund. However, the product of their scholastic or research endeavour offers a wider public benefit because it will be disseminated to the public and may change behaviour and practices in a positive way (such as where research into medicine is disseminated and leads to the adoption of more effective forms of treatment by medical practitioners).[19] Similarly, trusts for the welfare of animals provide a direct benefit to the animal itself, but the wider public benefit is manifested in the fact that kindness to animals is a means of checking the human tendency to cruelty and brutality.[20] This is illustrated by the case of *Incorporated Council of Law Reporting v Attorney General and Others*.[21]

EXTRACT

Incorporated Council of Law Reporting v Attorney General and Others [1972] Ch 73

Case facts

This case concerned an attempt by the Incorporated Council for Law Reporting to establish itself as a charity. The question for the Court of Appeal's consideration was whether materials that would primarily be used by the legal profession in order to earn their professional fees could be regarded as being charitable, and whether a sufficient public benefit could be derived from the dissemination of such materials.

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[16] Equalities Act 2010 s.193.
[17] Equalities Act 2010 s.193(1).
[18] Charity Commission (2011) Public Benefit: The Public Benefit Requirement https://www.charitycommission.gov.uk/media/535059/pb1_the_public_benefit_requirement.pdf. Site accessed 7 April 2014.
[19] *In Re Hopkins' Will Trust Naish and others v Francis Bacon Society Inc. and others* [1965] Ch 669 at p.680 per Wilberforce J.
[20] *In Re Wedgewood, Allen v Wedgewood* [1915] 1 Ch 113 at 117–118 per Lord Cozens-Hardy MR.
[21] [1972] Ch 73.

Russell LJ

It cannot be doubted that dissemination by publication of accurate copies of statutory enactments is beneficial to the community as a whole: and this is not the less so because at least in many instances the ordinary member of the public either does not attempt to, or cannot by study, arrive at a true conclusion of their import, or because the true understanding is largely limited to persons engaged professionally or as public servants in the field of any particular enactment, or otherwise interested in that field. The fact that to perhaps the majority of those who acquire and study a copy of (for example) a Finance Act it constitutes what might be described as a tool of their trades or professions or avocations in no way lessens the benefit to the community that results if accurate versions of that Finance Act are published and not kept like a cat in a bag to be let out haphazard. The same is to be said of the other source of our law, judicial decisions and the reasons therefor, especially in the light of our system of precedent. It is in my view just as beneficial to the community that reliable reports of judicial decisions of importance in the applicability of the law to varying but probably recurrent circumstances, or demonstrating development in the law, should be published; and all the more so if the publication be supervised by those who by training are best qualified to present the essence of a decision correctly and to distinguish the ephemeral from the significant. To state that the publication also supplied many professional men with the tools of their trade does not seem to me in any way to detract from the benefit that accrues to the community from the fact that the law does not remain locked in the bosom of the judiciary . . .

It was next contended for the Commissioners of Inland Revenue that a main purpose, even if not the only main purpose, of the association is to advance the interests of the legal profession by supplying it with the tools of its trade. . . . I am not persuaded of the validity of this contention. It seems to me that if the publication of reliable reports of decisions of the courts is for the benefit of the community and of general public utility in the charitable sense, it is an inevitable and indeed necessary step in the achievement of that benefit that the members of the legal profession are supplied with the tools of their trade. I do not see how the benefit to the public, assuming it to be a charitable object, could otherwise be achieved . . . Accordingly I reject the contention that the association is not established for purposes which are exclusively charitable in so far as that contention is based upon the submission that a main purpose or object is to supply members of the legal profession with tools of their trade.

I come now to the question whether, if the main purpose of the council is, as I think it is, to further the sound development and administration of the law in this country, and if, as I think it is, that is a purpose beneficial to the community or of general public utility, that purpose is charitable according to the law of England and Wales . . . In a case such as the present, in which in my view the object cannot be thought otherwise than beneficial to the community and of general public utility, I believe the proper question to ask is whether there are any grounds for holding it to be outside the equity of the Statute [of Charitable Uses 1601]: and I think the answer to that is here in the negative. I have already touched upon its essential importance to our rule of law . . . Accordingly the purpose for which the association is established is exclusively charitable in the sense of Lord Macnaghten's fourth category. I would not hold that the purpose is purely the advancement of education: but in determining that the purpose is within the equity of the Statute I by no means ignore the function of the purpose in furthering knowledge in legal science.

I would dismiss the appeal.

Sachs LJ (p92)

Against that background I turn to the question whether the council's purposes are educational. It would be odd indeed and contrary to the trend of judicial decisions if the institution and

maintenance of a library for the study of a learned subject or of something rightly called a science did not at least prima facie fall within the phrase 'advancement of education,' whatever be the age of those frequenting it. The same reasoning must apply to the provision of books forming the raw material for that study, whether they relate to chemical data or to case histories in hospitals: and I can find no good reason for excluding case law as developed in the courts. If that is the correct approach, then when the institution is one whose individual members make no financial gain from the provision of that material and is one which itself can make no use of its profits except to provide further and better material, why is the purpose not charitable?

On behalf of the Attorney-General the only point taken against this conclusion was that the citation of the reports in court cannot be educational – in part, at any rate, because of the theory that the judges are deemed to have complete knowledge of the law. For the Commissioners of Inland Revenue the main contention was that the use by the legal profession of the reports was in general (not merely when in court) a use the purpose of which was to earn professional remuneration – a use for personal profit: and that it followed that the purpose of the council was not charitable.

Taking the latter point first, it is, of course, the fact that one of the main, if not the main, uses to which law reports are put is by members of the legal profession who study their contents so as to advise clients and plead on their behalf. Those reports are as essential to them in their profession as the statutes: without them they would be ill equipped to earn professional fees. Does it follow, as submitted by Mr. Francis, that a main purpose of the reports is the advancement of professional interests and thus not charitable? The argument put thus is attractive, not least to those who, like myself, are anxious not to favour or to seem to favour their one-time profession. But the doctor must study medical research papers to enable him to treat his patients and earn his fees; and it would be difficult indeed to say that because doctors thus earn their emoluments the printing and sale of such papers by a non-profit making institution could not be held to be for the advancement of education in medicine.

Where the purpose of producing a book is to enable a specified subject, and a learned subject at that, to be studied, it is, in my judgment, published for the advancement of education, as this, of course, includes as regards the Statute of Elizabeth I the advancement of learning. That remains its purpose despite the fact that professional men – be they lawyers, doctors or chemists – use the knowledge acquired to earn their living. One must not confuse the results flowing from the achievement of a purpose with the purpose itself, any more than one should have regard to the motives of those who set that purpose in motion . . .

For these reasons I reject the contentions that the user of The Law Reports by the legal profession for earning fees of itself results in the purposes of the council not being charitable and thus return to the question whether they are charitable on the footing that their substantially exclusive purpose is to further the study of the law in the way already discussed. Such a purpose must be charitable unless the submission that the advancement of learning is not an advancement of education within the spirit and intendment of the preamble is upheld: but for the reasons already given that submission plainly fails. Accordingly, having regard to the fact that the members of the council cannot themselves gain from its activities, its purposes in my judgment fall within the second of Lord Macnaghten's divisions.

Despite the above conclusion, it seems desirable to consider as compactly as is practicable whether had the council's purpose not fallen within the second division it would none the less have come within the fourth as being beneficial to the community . . . the wider test – advancement of purposes beneficial to the community or objects of general public utility – has an admirable breadth and flexibility which enables it to be reasonably applied from generation to generation to meet changing circumstances . . .

The first question to be considered in relation to the wider test is whether the advancement of the administration of the law in its broad sense (which would include the elucidation, proper application and betterment of the law) is something beneficial to the community . . . Looking at the issue squarely and attempting to use the eyes of the generality of subjects of either Elizabeth I or Elizabeth II there is, however, manifestly only one answer – of course it is beneficial to the community . . .

Next comes the question whether the particular purpose of the council's activities sufficiently contribute to that advancement. Does it benefit a sufficiently wide section of the community? As satisfactory administration of the law in practice depends on there being a proper system of law reporting, it can well be said that the whole community benefits from the purposes of the council: but even if the benefits were confined to those who have to make judicial decisions and to the members of the legal profession advising clients and appearing for them in court, none the less a sufficiently large section of the community would derive the relevant benefits.

Adopting the test propounded by Russell L.J., I next turn to consider whether there is any reason for excluding these benefits from the range of those that are capable of being classified as charitable, and can find no such reason.

Finally as regards this head comes the question whether the contribution is made in a charitable manner. This point having been fully discussed in the judgments of my brethren to an effect with which I agree, it is not necessary to go over the ground again. The way in which the council operates qualifies it for inclusion amongst charities as defined by the Act of 1960 once it is shown that its purposes can properly be said to be charitable if operated in a charitable manner.

Accordingly if, contrary to my view, the purposes of the council do not fall within the second division, they are none the less charitable because they would then fall within the fourth.

Accordingly I would dismiss this appeal.

Buckley LJ

[I]f a body is established for a charitable purpose, it will be not the less a charity because the pursuit of that purpose will or may confer incidental benefits upon the members of a profession: see *Royal College of Surgeons of England* v. *National Provincial Bank Ltd.* [1952] A.C. 631 and *Royal College of Nursing* v. *St. Marylebone Borough Council* [1959] 1 W.L.R. 1077.

For the council it is argued that its objects are charitable upon the ground that they fall within the scope either of purposes for the advancement of education, using that term in a broad sense, or of the fourth head of Lord Macnaghten's celebrated enumeration of charitable purposes in *Pemsel's case* [1891] A.C. 531, 583 as being purposes beneficial to the community, which fall within the spirit and intendment of the Statute of Elizabeth I. It is emphasised that the members of the council, who are not more than 20 or so in number at any one time are precluded by the council's constitution from obtaining any profit or benefit as members from its activities. The council's publications can be bought by the general public and are, as the evidence shows, bought by a wide variety of users, including academic bodies, commercial and industrial bodies (including public utility undertakings), public authorities, government and public departments and offices, trade unions, and a wide variety of libraries, professional institutes and miscellaneous bodies, as well as a great many bodies and persons concerned with the administration and practice of the law, and all of these not merely in this country but also in many other countries within the Commonwealth and elsewhere. These circumstances, it is said, demonstrate that the council's publications constitute a general public purpose or, to use Sir Samuel Romilly's language in argument in *Morice v. Bishop of Durham* (1805) 10 Ves. 522, 531, an object of general public utility, and that this falls within the spirit of the

preamble . . . We were also referred to *Inland Revenue Commissioners v. City of Glasgow Police Athletic Association*: [1953] A.C. 380, where Lord Normand, at p. 391, Lord Morton of Henryton, at p. 400, and Lord Reid, at p. 402, all expressed the view that the promotion of the efficiency of the police would be a charitable purpose. By analogy it was contended that the advancement of the administration of justice is a charitable purpose and that the objects of the council are charitable on this ground. Alternatively the council has contended that its objects are educational in that they result in dissemination of information about the latest state of and development in the science of the law and so are educational in a broad sense . . .

I agree with Foster J. in thinking that, when counsel in court cites a case to a judge, counsel is not in any real sense 'educating' the judge, counsel performing the role of a teacher and the judge filling the role of a pupil; but I do not agree with him that the process should not be regarded as falling under the charitable head of 'the advancement of education.'

In a number of cases learned societies have been held to be charitable. Sometimes the case has been classified under Lord Macnaghten's fourth head, sometimes under the second. It does not really matter under which head such a case is placed, but for my own part I prefer to treat the present case as falling within the class of purposes for the advancement of education rather than within the final class of other purposes for the benefit of the community. For the present purpose the second head should be regarded as extending to the improvement of a useful branch of human knowledge and its public dissemination . . .

The council was established for the purpose of recording in a reliably accurate manner the development and application of judge-made law and of disseminating the knowledge of that law, its development and judicial application, in a way which is essential to the study of the law. The primary object of the council is, I think, confined to this purpose exclusively and is charitable. The subsidiary objects, such as printing and publishing statutes, the provision of a noting-up service and so forth, are ancillary to this primary object and do not detract from its exclusively charitable character. Indeed, the publication of the statutes of the realm is itself, I think, a charitable purpose for reasons analogous to those applicable to reporting judicial decisions.

The fact that the council's publications can be regarded as a necessary part of a practising lawyer's equipment does not prevent the council from being established exclusively for charitable purposes. The practising lawyer and the judge must both be lifelong students in that field of scholarship for the study of which The Law Reports provide essential material and a necessary service. The benefit which the council confers upon members of the legal profession in making accurate reports available is that it facilitates the study and ascertainment of the law. It also helps the lawyer to earn his livelihood, but that is incidental to or consequential on the primary scholastic function of advancing and disseminating knowledge of the law, and does not detract from the exclusively charitable character of the council's objects . . .

The service which publication of The Law Reports provides benefits not only those actively engaged in the practice and administration of the law, but also those whose business it is to study and teach law academically, and many others who need to study the law for the purposes of their trades, businesses, professions or affairs. In all these fields, however, the nature of the service is the same: it enables the reader to study, and by study to acquaint himself with and instruct himself in the law of this country. There is nothing here which negatives an exclusively charitable purpose.

Although the objects of the council are commercial in the sense that the council exists to publish and sell its publications, they are unselfregarding. The members are prohibited from deriving any profit from the council's activities, and the council itself, although not debarred from making a profit out of its business, can only apply any such profit in the further pursuit of

its objects. The council is consequently not prevented from being a charity by reason of any commercial element in its activities.

I therefore reach the conclusion that the council is a body established exclusively for charitable purposes and is entitled to be registered under the Act of 1960 . . .

Outcome

Accordingly, Sachs LJ and Buckley LJ classified the trust as being for the purposes of the advancement of education as well as for other purposes beneficial to the community. Russell LJ declined to accept that the trust advanced education, even though it advanced learning. He was satisfied that the trust was to the advantage of other purposes beneficial to the community. Accordingly, the Attorney General's appeal was dismissed, and the Incorporated Council of Law Reporting's status as a charity was upheld.

Thus, a trust may be charitable, even if the benefit to the public is indirect. Accordingly, when determining the question of whether the trust confers a benefit upon the public, regard must be had to the following considerations.

Is there a public benefit?

- Does the activity provide a benefit to the public?
  - What is the social value of the activity?
  - Is the activity political in character?
  - Is there an indirect public benefit?
- Does the activity provide a benefit to a sufficiently large section of the public?
  - Are the beneficiaries defined by a connection to an individual or an organisation?
  - Are the beneficiaries a section of the public?
  - Is a trust that expresses a preference for a particular group/individuals acceptable?
- Does the activity conform with the law as regards discrimination?
- Is there an indirect benefit to the public?

This chapter has sought to provide an outline of the main principles for determining what a charity is. In the next chapter, these principles will be considered more specifically, with reference to the different types of charitable purposes, and how public benefit may be demonstrated in each case.

Chapter summary

This chapter may be useful for assignments and assessments on:

- Charitable trusts
- Defining a charity
- Trusts for purposes.

Further reading

Bright, S. (1989) 'Charity and trusts for the public benefit – time for a re-think' *Conveyancer and Property Lawyer* 28.

Iwobi, A. (2009) 'Out with the old, in with the new: religion, charitable status and the Charities Act 2006' 29(4) *Legal Studies* 619.

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Specific charitable purposes

Chapter outline

This chapter will cover:

- The different types of charitable purposes listed in s.3(1) Charities Act 2011.

Introduction

The different types of charitable purposes, as listed in s.3(1) Charities Act 2011 are:

(a) the prevention or relief of poverty;
(b) the advancement of education;
(c) the advancement of religion;
(d) the advancement of health or the saving of lives;
(e) the advancement of citizenship or community development;
(f) the advancement of the arts, culture, heritage or science;
(g) the advancement of amateur sport;
(h) the advancement of human rights, conflict resolution or reconciliation or the promotion of religious or racial harmony or equality and diversity;
(i) the advancement of environmental protection or improvement;
(j) the relief of those in need because of youth, age, ill-health, disability, financial hardship or other disadvantage;
(k) the advancement of animal welfare;
(l) the promotion of the efficiency of the armed forces of the Crown or of the efficiency of the police, fire and rescue services or ambulance services;
(m) any other purposes –
    (i) that are not within paragraphs (a) to (l) but are recognised as charitable purposes by virtue of section 5 (recreational and similar trusts, etc) or under the old law,
    (ii) that may reasonably be regarded as analogous to, or within the spirit of, any purposes falling within any of paragraphs (a) to (l) or sub-paragraph (i), or
    (iii) that may reasonably be regarded as analogous to, or within the spirit of, any purposes which have been recognised, under the law relating to charities in England and Wales, as falling within sub-paragraph (ii) or this sub-paragraph.

This chapter considers these specific charitable purposes and will address how the charitable purpose and the public benefit are established in relation to each head of charity. It must be emphasised however that the cases merely provide illustrations of what type of activities will be regarded as charitable, and the extent to which a public benefit is demonstrated. It will be a matter for the lawyer (and accordingly also the law student) to establish that the activity is charitable and that a sufficient public benefit is shown, by drawing analogies or distinctions between these and other examples.

(a) The prevention or relief of poverty

Charitable purpose

Section 3(1)(a) of the Charities Act 2011 recognises the prevention or relief of poverty. Although interlinked, the prevention and the relief of poverty are two distinct issues. While the relief of poverty has long been recognised as being charitable – and may even be traced back to the medieval usage of the use as a means of providing for monks who, because of their vow of poverty were prevented from owning assets – the prevention of poverty, introduced for the first time in the Charities Act 2011, is a new development and, as will be explained, is potentially more controversial.

Relief of poverty

In order to be charitable, an organisation's purposes must be for the relief of poverty, rather than for the benefit of the poor – essentially the charitable purpose must be aimed at ensuring that those who are classed as poor will be assisted as a consequence of the charity's intervention. In the case of *Joseph Rowntree Memorial Trust Housing Association and Others v Attorney General*,[1] Peter Gibson J attempted to explain the distinction between 'the relief of poverty' and 'benefitting the poor':

> The word 'relief' implies that the persons in question have a need attributable to their condition as aged, impotent or poor persons which requires alleviating and which those persons could not alleviate, or would find difficulty in alleviating, themselves from their own resources. The word 'relief' is not synonymous with 'benefit'.

Nevertheless, he accepted that relief of poverty was not confined to the provision of financial assistance to the poor, and that the provision of other resources, such as accommodation or healthcare, could equally have the effect of relieving poverty if the recipients could not provide such resources for themselves. Peter Gibson J traces the authorities back, reiterating the views of Lord Wilberforce in 1969,[2] and Lord Herschell in 1891 that:

> I am unable to agree with the view that the sense in which 'charities' and 'charitable purpose' are popularly used is so restricted as this. I certainly cannot think that they are limited to the relief of wants occasioned by lack of pecuniary means. Many examples may, I think, be given of endowments for the relief of human necessities, which would be as generally termed charities as hospitals or almshouses, where, nevertheless, the necessities to be relieved do not result from poverty in its limited sense of the lack of money.[3]

This has been confirmed more recently by the Charity Commission's guidance, issued in 2008 and amended in 2011, where the Commission seeks to explain what relieving poverty entails:

EXTRACT

Charity Commission (2011) The Prevention or Relief of Poverty for Public Benefit, Section C1

C1. What does the prevention or relief of 'poverty' mean?

In the past, the courts have always defined 'poverty' by reference to financial hardship or lack of material things but, in current social and economic circumstances, poverty includes many disadvantages and difficulties arising from, or which cause, the lack of financial or material resources.

There can be no absolute definition of what 'poverty' might mean since the problems giving rise to poverty are multi-dimensional and cumulative. It can affect individuals and whole communities. It might be experienced on a long or short-term basis.

Poverty can both create, and be created by, adverse social conditions, such as poor health and nutrition, and low achievement in education and other areas of human development. Charities operating in this area often express concerns about the voicelessness, vulnerability, fear and

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[1] [1983] Ch 159.
[2] *In re Resch's Will Trusts* [1969] 1 AC 514 at p.542.
[3] *Inland Tax Special Purposes Commissioners v Pemsel* [1891] AC 531, 571.

powerlessness experienced by people in poverty and the fact that people in poverty can become excluded from the opportunities, goods and services necessary for them to live a decent life in modern society. Charities preventing or relieving poverty can, additionally, provide a very valuable platform for promoting and protecting the interests of people in poverty.

The meaning of 'poverty' has to be considered in the context of an organisation's aims, whom the aims are intended to benefit, and where the organisation carries out its aims.

For example, for a charity carrying out its aims in the poorest areas in developing countries, 'people in poverty' might typically mean people who lack even the most basic essentials to sustain life, such as adequate clean water, food and shelter.

For a charity carrying out its aims in England and Wales, 'people in poverty' might typically mean households living on less than 60% of median income who go short in some unacceptable way. This includes those people who, despite working, might still fall into this category and people may qualify for assistance from a poverty charity whether or not they are eligible for state benefits.

The prevention or relief of poverty is not just about giving financial assistance to people who lack money; poverty is a more complex issue that is dependent upon the social and economic circumstances in which it arises. We recognise that many charities that are concerned with preventing or relieving poverty will do so by addressing both the causes (prevention) and the consequences (relief) of poverty.

People in poverty: throughout this guidance we have used the term 'people in poverty' to describe 'the poor'. 'People in poverty' does not just include people who are destitute, but also those who cannot satisfy a basic need without assistance. The courts have avoided setting any absolute criteria to be met in order for poverty to be said to exist, although they have been prepared to state in specific cases whether or not a particular level of income or assets meant that a person was 'poor'. In essence, 'people in poverty' generally refers to people who lack something in the nature of a necessity, or quasi-necessity, which the majority of the population would regard as necessary for a modest, but adequate, standard of living.

Financial hardship: we recognise that poverty and financial hardship can be, but are not necessarily, the same. All people who are poor are in financial hardship and, in many cases, the term 'financial hardship' has been used interchangeably with the term 'poverty' as meaning the same thing. Where that is the case then this guidance also applies to charities concerned with the relief of those in need by reason of financial hardship.

Not everyone who is in financial hardship is necessarily poor, but it may still be charitable to relieve their financial hardship.

For example, an elderly person who owns their own house might be 'asset rich', but has insufficient income to meet the costs of a heating bill during the winter and so might experience temporary financial hardship.

Similarly, someone might suffer a temporary period of financial hardship due to a sudden change in circumstances (such as redundancy, illness, an accident, or a death in the family).

For example, a person might experience temporary financial hardship if they lose their job and are unable to provide adequately for themselves and their family from their own resources until they can find alternative employment. That condition might be temporary.

In most cases, we will treat the relief of poverty and the relief of financial hardship the same. Generally speaking, it is likely to be charitable to relieve either the poverty or the financial hardship of anyone who does not have the resources to provide themselves, either on a short or long-term basis, with the normal things of life which most people take for granted.

However, it would not be within a charity's prevention or relief of poverty aims to provide financial assistance to someone who is neither poor nor in financial hardship, nor at risk of either. It may be open to the charity to address other charitable needs of such people where that is within its aims and it is appropriate for it to do so.

Poverty charities addressing other needs: we recognise that there is often a significant degree of overlap between preventing or relieving poverty and advancing other charitable aims. Many charities concerned with the prevention or relief of poverty, or the relief of people in financial hardship, are also concerned with relieving other needs, such as needs associated with ethnicity, geography, gender, age, disability, educational and skills attainment.

For example, a charity may be specifically concerned with relieving poverty and other needs associated with old age, or ill health or disability.

This guidance is relevant to the prevention or relief of poverty aims of those charities.

Source: Available from http://www.charity-commission.gov.uk/Charity_requirements_guidance/Charity_essentials/Public_benefit/pbpoverty.aspx. Site accessed 16 January 2014.

What is seen in this guidance is that a broad range of activities may be regarded as being for the relief of poverty. Accordingly, in developing countries or countries affected by a significant natural disaster, the relief of poverty could include activities such as the provision of accommodation, food, clothing, medication and clean water. In England and Wales, the relief of poverty might include providing grants and financial assistance to those who find themselves facing financial hardship because of short-term problems such as redundancy, unemployment or illness. Providing advice and support to people in such circumstances may therefore be regarded as charitable, as would the provision of education and training opportunities that would enable people to escape from poverty. In the case of *In Re Roadley*[4] for example, a trust for patients at two specific hospitals was treated as being a charitable trust for the relief of poverty because the hospitals in question were hospitals whose purpose was to treat the poor. *In Re Lucas*,[5] and *In Re Wall,*[6] the trusts were concerned with payments being made periodically to people who were classed as poor, while *Trustees of the Mary Clark Home v Anderson*[7] concerned the provision of accommodation for ladies in reduced circumstances. A trust to enable educated women and girls to become self-supporting was considered to be an acceptable charitable activity in the case of *Re Central Employment Bureau for Women and Students' Careers Association Incorporated*[8] because it proposed to provide education for women and girls that would then enable them to earn an independent income, and because it also aimed to provide them with a loan that would allow them to establish a business or enterprise from which they could earn a living. The fact that the beneficiaries would not be able to become self-supporting without assistance from the fund meant that the trust could legitimately be regarded as being for the relief of poverty.

The indirect relief of poverty has also been regarded as being charitable. For example, providing allotments[9] may be charitable, as will the funding of institutions and resources

[4] *In Re Roadley. Iveson v Wakefield* [1930] 1 Ch 524.
[5] *In Re Lucas. Rhys v Attorney General* [1922] 2 Ch 52.
[6] *In Re Wall, Pomeroy v Willway* (1889) 42 Ch D 510.
[7] *Trustees of the Mary Clark Home v Anderson* [1904] 4 KB 645.
[8] *Re Central Employment Bureau for Women and Students' Careers Association Incorporated* [1942] 1 All ER 232.
[9] *Crafton v Frith* (1851) 4 De G & Sm 237.

that will in turn provide relief from poverty. In *Biscoe v Jackson*[10] for example, soup kitchens were regarded as a charitable purpose for the relief of poverty – the institution was not itself poor, but the work it did was for the relief of poverty. Similarly, in *Re Dean's Will Trust*,[11] a trust was established in order to provide accommodation for the relatives of people who are critically ill in hospital. The visitors themselves may not be poor, but providing a direct benefit to them conferred an indirect benefit on the hospital patients who would not otherwise have the support of their family. Harman J explains (at p.883):

> If and so far as that is a purpose of the hospital, then, in my judgment, there is no difficulty because the purposes of the hospital generally are admittedly charitable purposes. If one of the purposes was not a 'purpose' of the hospital properly so called, difficulty might arise, but I find no difficulty in saying that the provision of such accommodation may be a very important purpose of a hospital of this kind for the spiritual and psychological comfort of its patients, and, indeed, to aid their recovery. It may be absolutely necessary to house their relations near them when they are *in extremis*. It may make all the difference between life and death to a patient to know that his mother, his child, or his nearest relative, is at hand. Even though he or she may never see the relative in question, it may be vital to have that support.

Prevention of poverty

Under the Charities Act 2011, the prevention of poverty is also charitable. The courts have not yet been required to adjudicate on what is meant by the prevention of poverty and what may or may not be included. However, while the relief of poverty is aimed at alleviating the situation of those who are already poor, the prevention of poverty is potentially more controversial, in that charitable support may be provided for those who are wealthy, but who may become poor in the future. In its guidance for example, the Charity Commission specifically provides that:

> we recognise that the prevention of poverty includes preventing those who are poor from becoming poorer, and preventing people who are not poor from becoming poor . . .[12]

The potential controversies here are numerous. Firstly, it is possible that the probability of future poverty may be difficult to establish. Secondly, the section has the potential to confer a benefit on those who are not poor as well as those that are poor, thus representing a departure from the earlier law where a trust that purported to confer a benefit on the rich as well as the poor could not be regarded as charitable. A further concern arises from the fact that charities for the relief of poverty may confer a benefit on a limited class of persons who may be defined by a personal connection to the settlor. It is possible that s.3(1)(a) Charities Act 2011 may have the consequence of conferring a charitable benefit on wealthy persons who are connected to the settlor, thus defeating entirely the philanthropic purposes of charitable giving.

Poverty

Poverty may neither be prevented nor relieved unless it is clear what is meant by the term poverty. It is acknowledged however that is not desirable to define poverty according to

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[10] (1887) 35 Ch D 460.

[11] *Re Dean's Will Trusts, Cowan v Board of Governors of St Mary's Hospital Paddington and Others* [1950] 1 All ER 882.

[12] Charity Commission (2011) The Prevention or Relief of Poverty for the Public Benefit. Paragraph C1 https://www.charitycommission.gov.uk/detailed-guidance/charitable-purposes-and-public-benefit/charities-and-public-benefit/the-prevention-or-relief-of-poverty-for-the-public-benefit/. Site accessed 7 April 2014.

some precise mathematical formula. It is also acknowledged that the concept of poverty may have a different meaning and signification in different situations.

EXTRACT

In Re Coulthurst, Decd. Coutts & Co. v Coulthurst and Another [1951] Ch 661, 665–666 per Lord Evershed MR

Case facts

In this case, a trust was created for the benefit of the widows and orphaned children of bank officials, whose financial situation meant that providing them with support could be justified.

Lord Evershed

It is quite clearly established that poverty does not mean destitution; it is a word of wide and somewhat indefinite import; it may not unfairly be paraphrased for present purposes as meaning persons who have to 'go short' in the ordinary acceptation of that term, due regard being had to their status in life, and so forth.

[And (pp.667–668), referring to the judgment of Vaisey J in the court of first instance:]

Vaisey, J., considered separately the formulæ 'by reason of his, her or their financial circumstances' and 'most deserving of such assistance'. The whole sentence seems to me to mean, essentially, that the persons selected are persons whose financial circumstances are such that they are not only deserving of assistance, that is to say, wanting help, but, of all such, are those who most want it. I therefore think that this sentence, so far from reversing the tendency which I should have thought emerged from the earlier words, rather emphasized it. The point was made that the use of the phrase 'most deserving' had, in fact, the contrary result. If the persons to benefit were persons who, by reason of their financial circumstances, were deserving of assistance, then it might be said that the standard imposed was an objective one, namely, that they were persons whose financial circumstances left them in want. Can it be said that by using the superlative 'most' you must discard the objective standard and that those to benefit are the people whom the bank will regard as being (of the whole class) the most deserving, that is the least undeserving? For my part, I think that that view is too subtle an interpretation of these words, and I think, reading the clause as a whole, it would defeat the intention in the mind of the testator.

Outcome

Accordingly, the Court of Appeal affirmed the decision of the High Court, and the trust was accepted as charitable.

Therefore, poverty is defined not according to some universal objective standard, but as being relative to one's social situation. Although victims of famine or natural disasters may be regarded as people suffering from the most extreme forms of poverty, this does not preclude the fact that charities for the prevention and relief of poverty may be legitimately established or continued with the view to preventing and relieving poverty among students, low income families, or people who are temporarily unemployed. Even though loans or state-funded support may be provided, there is nevertheless an acknowledgement that these individuals may be poor in comparison with other sectors of society in England and Wales. This distinction is discussed fairly extensively by Romer J in the case of *In Re Clarke, Bracey v the Royal National Lifeboat Institution* [1923] 2 Ch 407.

EXTRACT

Re Clarke, Bracey v the Royal National Lifeboat Institution [1932] 2 Ch 407

Case facts

This case concerned a will which contained a number of clauses. One of the clauses purported to create a trust for persons of moderate means, and accordingly, one of the issues to be decided by the High Court was whether persons of moderate means could be regarded as being in poverty.

Romer J

It was contended on behalf of the next of kin that the objects designated under heading (a) are not charitable, because the persons to be benefited by the institution, society or nursing homes are not poor persons but persons of moderate means, and because such persons can only benefit on payment by themselves of some moderate contribution. But in *Trustees of the Mary Clark Home v. Anderson* [[1904] 2 KB 645], a home for ladies in reduced circumstances, of which the inmates were to be ladies of fifty years old or upwards possessed or in the actual enjoyment of a fixed yearly income of not less than 25l. and not more than 55l., was held to be exempt from landlord's property tax and inhabited house duty as being a 'house provided for the reception or relief of poor persons.' Channell J. in the course of his judgment, after referring to the case of *Attorney-General v. Wilkinson* [(1859) 29 LJ Ch 41], said: 'That seems to lead to the conclusion that the expression "poor person" in a trust for the benefit of poor persons does not mean the very poorest, the absolutely destitute; the word "poor" is more or less relative.' A little further on he added: 'I do not know any standard of poverty, nor how I can lay down any rule; the only thing to guide me is this: these ladies go to the institution for the sole reason that they are poor, and the institution is absolutely charitable.' In *In re Gardom* [[1914] 1 Ch 662] it was held that a gift for the maintenance of a temporary house of residence for ladies of limited means was a good charitable gift. Eve J. in giving judgment said: 'It is true that ladies of limited means are not destitute, and that the expression "limited means" may vary in its signification according to the standard by which the means are measured, but these arguments provoke the rejoinder that there are degrees of poverty less acute than abject poverty or destitution, but poverty nevertheless, and further that in this case the limitation of means contemplated is presumably a limitation such as will necessitate some contribution from the bounty of the testatrix before the recipient would be able to defray the expense of a temporary sojourn in the home. In other words the objects to be benefited by the bequest are ladies too poor to provide themselves with a temporary home without outside assistance. I think it is a good charitable trust and am fortified in this view by some observations of Channell J. in the case of *Trustees of the Mary Clark Home v. Anderson*' and then after citing the passage from the judgment of Channell J. to which I have just referred he added: 'I think those words apply exactly to the section of the public and to the institution which the testatrix here intended to benefit and to subsidize.'

In the present case I think that the words of Channell J. and the words of Eve J. which I have quoted apply exactly to the section of the public and to the institutions which the testator intended to benefit and to subsidize. The 'moderate means' to which he refers are presumably means so moderate as to necessitate some contribution from the bounty of the testator before the recipient would be able to procure the surgical operation or medical treatment of which the recipient might stand in need. In *In re Estlin* [(1903) 72 LJ Ch 687] it was moreover held by Kekewich J. that a bequest for the purpose of establishing a home of rest for lady teachers was none the less charitable because each lady was required to contribute 10s. a week for board and lodging. I therefore hold that the objects under heading (a) are charitable objects.

Valid charitable trusts have been recognised where there was an attempt to confer a benefit on those who may be regarded as being comparatively wealthy in comparison with the very poorest sections of society, but who are poor in comparison with their expectations and status in society. In the case of *Re Coulthurst* (discussed above) for example, the trust was created for the widows and orphaned children of deceased bank officials, and was held to be charitable, even though there may be widows and children who might be considerably poorer than those whose husband or father had been a bank official. Similarly in the case of *In Re Gardom*,[13] the trust was created for the benefit of 'ladies of limited means' while *Shaw v Mayor of Halifax*[14] concerned a trust for 'ladies by birth and education . . . who had become reduced in circumstances'. However, such persons may be regarded as poor compared with their peers, and may benefit from trusts for the prevention and relief of poverty. In *Shaw v Mayor of Halifax* for example, the trust conferred a benefit upon those whose financial situation was worse than it once was, and whose pecuniary needs rendered them as *'deserving a better or more comfortable position in life.'*[15] Such ladies may be wealthier, in objective terms, than many other sections of society, but their situation in life, as compared with expectations to which they had been accustomed, meant that they could legitimately be viewed as poor.

Accordingly, a charity that seeks to relieve hardship and difficulty caused by a lack of financial or material resources, either on a short-term (such as where a person is unemployed for a short term, or is unable to work for a short period of time because of injury or illness), or a long-term basis (such as where advice is provided to farmers in developing countries regarding more effective farming techniques) will be valid as a charity for the relief of poverty. In essence 'those who cannot satisfy a basic need without assistance'[16] will be regarded as deserving of relief from poverty, although social basic needs will vary across time and across social situations. Consequently, the types of activities that will be regarded as having the objective of relieving property are extremely wide ranging. The Charity Commission's guidelines list the types of activities that may be regarded as relieving poverty.

EXTRACT

Charity Commission (2011) The Prevention or Relief of Poverty for the Public Benefit, Annex A

Annex A: Examples of ways in which charities might prevent or relieve poverty

Examples of ways in which charities might prevent or relieve poverty include:

- providing debt or money management advice;
- awarding a 'fair trade mark' to products, the sale of which is intended to relieve the poverty of producers by ensuring they receive a fair price for their goods;

[13] *In Re Gardom, Le Page v Attorney General* [1914] 1 Ch 662. The decision in this case was reversed on other grounds on appeal, but the validity of a trust for ladies of limited means was not disputed.

[14] *Shaw and Others v Mayor of Halifax* [1915] 2 KB 170.

[15] *Shaw and Others v Mayor of Halifax* [1915] 2 KB 170 at p.179 per Buckley LJ.

[16] Charity Commission (2011) The Prevention or Relief of Poverty for the Public Benefit. http://www.charity-commission.gov.uk/Charity_requirements_guidance/Charity_essentials/Public_benefit/pbpoverty.aspx#annex. Site accessed 16 January 2014.

- advising such producers of the best ways in which to engage in the trading process;
- advising poor farmers in developing countries about more effective farming techniques;
- providing legal advice and/or support on land tenure and ownership issues to widows in countries where women's rights are restricted;
- working with women's groups who are concerned about a lack of equitable conditions for women workers;
- providing emergency aid in the wake of a natural disaster to people who are at imminent risk of becoming poor because of the loss of their home, possessions, crops or business;
- providing money management and debt counselling advice and training to someone at actual risk of being in poverty;
- establishing a micro-credit scheme or schemes (ie a scheme for making small loans to poor borrowers and providing other forms of assistance such as skills training) in an area of particular deprivation in a developing country;
- providing a grant to a local business so that they can give a job to an unemployed person (and so relieve their poverty);
- helping people gain access to safe water and sanitation and contributing to helping the world's poorest people gain access to these basic requirements;
- sending essential food supplies, cooking sets and bedding, to help people in a state of poverty as a result of an emergency;
- sending tools and materials to help people hit by an emergency situation build shelter for their families;
- donations to other charities accommodating those in need in the area of the charity, such as almshouses, homes or hostels for the old, infirm, or homeless; and
- the provision of basic supplies, such as children's clothes and shoes, books and other personal or educational supplies to help families, children and schools throughout the world that are unable to afford them.

Examples of ways in which charities might relieve poverty include:

Grants of money in the form of:

- weekly allowances for a limited period;
- payments to meet a particular need;
- one-off payments in a crisis or disaster;
- payment of travelling expenses for visiting people, for example in a hospital, convalescent home, children's home, prison or other similar place, particularly where more frequent visits are desirable than payments from public funds will allow;
- payments to meet expenses associated with visiting people (as mentioned above) for example, child-minding, accommodation, refreshments etc;
- payments to assist in meeting energy and water bills.

The provision of items (either outright or, if expensive but appropriate, on loan), such as:

- furniture, bedding, clothing, food, fuel, heating appliances;
- washing machines and fridges.

Payment for services, such as:

- essential house decorating;
- insulation and repairs;

- laundering;
- meals on wheels;
- outings and entertainment;
- child-minding;
- telephone line, rates and utilities.

The provision of facilities, such as:

- the supply of tools or books;
- payments of fees for instruction, examination, or other expenses connected with vocational training, language, literacy, numerical or technical skills;
- travelling expenses to help the recipients to earn their living; or
- equipment and funds for recreational pursuits or training intended to bring the quality of life of the beneficiaries to a reasonable standard.

Charities for the relief of financial hardship might give extra help to people in poverty who are also **sick, convalescent, infirm, or with disabilities**, whether physical or mental. This might include:

Grants of money in the form of:

- special payments to relieve sickness or infirmity;
- payment of travelling expenses on entering or leaving hospitals, convalescent homes, or similar institutions, or for out-patient consultations;
- payment towards the cost of adaptations to the homes of people with disabilities; or
- payment of telephone installation charges and rentals.

The provision of items, such as:

- food for special diets; or
- medical equipment, (such as wheelchairs) either outright or, if expensive but appropriate, on loan.

The provision of services, such as:

- exchange of library books;
- gardening;
- bathing, hair washing, shaving, foot care;
- help in the home;
- nursing aid, physiotherapy in the home;
- shopping;
- reading, sitting-in, audio tapes for the housebound; and
- travelling companions.

The provision of facilities, such as:

- arrangements for a period of rest or change of environment;
- treatment at convalescent homes or other institutions; or
- transport.

Other practical ways of assisting people in poverty

- a national helpline to direct people to the correct state benefit and to what benevolent funds might be available to them.

Making grants to other charities

As well as giving grants to individual people in poverty, or to organisations on behalf of those individual people, trustees can also make grants to other charities and organisations which offer help to people in poverty. In this case, however, trustees should take reasonable care to ensure that any donation will be passed on, in cash or kind, to persons who qualify as proper recipients of assistance from the donor charity.

On this basis, grants to almshouse charities, and other charities which cater exclusively for people in poverty, are permissible provided that the receiving charities operate in the same area of benefit as the donor charity.

Grants can be made by a charity for the relief of poverty to another charity even if that charity's aims and activities do not include the relief of poverty provided that the effect of the grant is to relieve poverty (the receiving charity would only be able to accept the grant if it also furthered its own aims).

Some local charities might cater only or mainly for people in poverty even though their aims might not be strictly confined to the relief of poverty.

For example, in a particularly deprived area most people attending a youth club or an old age pensioners' club might be in poverty, although membership of the club is not limited to people in poverty.

If trustees wish to give a general grant to another charity in such circumstances, they will need to find out whether, in practice, the charity's beneficiaries are people in poverty. If they are, then a grant might be permissible if its effect is likely to relieve poverty. Even if a few people who are not in poverty will also benefit, this will not prevent a grant if their benefit is merely incidental and unavoidable, and the bulk of the benefit is for people in poverty. Again, we suggest that trustees contact us for advice if they are in any doubt.

A grant could also be made to another charity having a variety of aims, one of which was for relief of poverty. In such a case, a grant could be made in support of that charity's work subject to the specific condition that it be used by that charity in relieving poverty.

Source: Available from http://www.charity-commission.gov.uk/Charity_requirements_guidance/Charity_essentials/Public_benefit/pbpoverty.aspx. Site accessed 16 December 2014.

What is seen here is that the relief of poverty is not limited to the provision of financial and material resources, but also includes the provision of advice and advocacy, education and training, and respite opportunities, such as entertainments and outings or childcare facilities.

Nevertheless, the provision of such services do not of themselves mean that a purpose is for the relief of poverty, and therefore the provision of such services to those who are not regarded as poor will not be treated as a charitable purpose. Accordingly, the courts must consider whether the wording of a charitable donation will mean that it is possible for those who are not poor to derive a benefit. An example may be seen in the case of *Re Gwyon* [1930] 1 Ch 255.

EXTRACT

Re Gwyon, Public Trustee v Attorney General [1930] 1 Ch 255

Case facts

In this case, the testator wished to set up a trust, the income from which would be used in order to provide that which was referred to as knickers (meaning short trousers) to boys in Farnham in Surrey.

Eve J

. . . although a gift to or for the poor other than those who were in receipt of parochial relief – that is, paupers – would be a good charitable gift, it does not follow that a gift to all and sundry in a particular locality and not expressed to be for the poor ought to be construed as evidencing an intention to relieve poverty merely because the testator is minded to exclude paupers. I think that according to the true construction of these testamentary documents the benevolence of the testator was intended for all eligible boys other than paupers, and I cannot spell out of them any indication which would justify the Foundation Trustees refusing an applicant otherwise eligible on the ground that his material circumstances were of too affluent a character. In these circumstances I cannot hold this trust to be within the description of a legal charitable trust.

Outcome

The trust failed in this case because the fact that wealthy boys as well as poor boys could benefit from the trust meant that the trust was not for the relief of poverty, even though Eve J acknowledged that it was probable the testator foresaw that the likely candidates would be from less affluent sections of society.

A similar conclusion may be seen from the judgment in the case of *Re Sanders* [1954] Ch 265.

EXTRACT

Re Sanders' Will Trusts, Public Trustee v McLaren [1954] Ch 265

Case facts

This case concerned a will whereby the testator left a portion of his estate in order to provide 'dwellings for the working classes and their families resident in the area of Pembroke Dock, Pembrokeshire, Wales, or within a radius of five miles therefrom (with preference to actual dockworkers and their families employed at the said docks)'.

Harman J

This gift was primarily upheld before me as being in effect a gift for the relief of poverty. Indeed, I do not think that it was suggested that there was any way in which the gift could be upheld unless there was to be found somewhere in it an indication sufficient to induce the court to find the clement of poverty in the recipients, who are described as 'the working classes and their families'; not widows nor orphans, nor dependants of persons of the working classes, but persons still working, preferably dockers working in the Pembroke Docks. It is difficult to see how poverty is to be attributed to them.

As long ago as the beginning of the present century Lord Wrenbury, sitting at first instance, in *In re Sutton* [[1901] 2 Ch 640], dealing with the well-known Sutton Charity, said at the end of his judgment: 'the Act of 1890' – that is the Working Classes Dwellings Act referred to by the testator in his codicil – 'is not an Act dealing with charitable matters, but is an Act providing for erecting dwellings for the working classes. Now, the poor need not necessarily be poor of the class known as the working class, and many of the working class, as we know, are not poor.' So that 50 years ago the law recognized that the working classes and the poor were not synonymous. Although a man might be a member of the working class and poor, the first does not at all connote the second.

It has been pointed out recently by Denning L.J., when sitting at first instance, in *H. E. Green & Sons v. Minister of Health (No. 2)* [[1948] 1 KB 34], that the expression 'working classes' is an anachronism and does not really mean anything in these days. 'Much has been said,' said the judge, 'in this case as to the meaning of "working classes." These words "working classes," have appeared in a number of Acts for the last hundred years. I have no doubt that in former times it had a meaning which was reasonably well understood. "Working classes" fifty years ago denoted a class which included men working in the fields or the factories, in the docks or the mines, on the railways or the roads, at a weekly wage. The wages of people of that class were lower than those of most of the other members of the community, and they were looked upon as a lower class. That has all now disappeared. The social revolution in the last fifty years has made the words "working classes" quite inappropriate today. There is no such separate class as the working classes. The bank clerk or the civil servant, the school teacher or the cashier, the tradesman or the clergyman, do not earn wages or salaries higher than the mechanic or the electrician, the fitter or the mineworker, the bricklayer or the dock labourer. Nor is there any social distinction between one or the other. No one of them is of a higher or a lower class. In my opinion the words 'working classes' used in the Acts are quite inappropriate to modern social conditions.' Then he went on to point out that they nevertheless appear in the Housing Act, 1936, but it is notable that that solecism, if such it was, was remedied by the Housing Act, 1949, which, by its first schedule, removes the words 'working classes,' whenever those words appear in the Act of 1936.

In *Belcher v. Reading Corporation* [[1950] Ch 380] the court again had to deal with this expression 'the working classes' in a case where certain inhabitants of council houses in Reading sued the Reading Corporation, which had put up the rents of their houses, putting forward various reasons why they should not have their rents raised. That contention was rejected by Romer J., who only in passing glanced at the judgment in *Green*'s case. He said this: 'As to this I may say that, in the light of modern conditions, I share the difficulty which Denning L.J. felt and expressed in *H. E. Green & Sons v. Minister of Health (No. 2)* with regard to who does, and who does not, belong to the working classes; the phrase has a far wider, and far less certain, signification than it used to possess, and it is to be observed that, possibly for this reason, it has now been jettisoned from section 85 by Sch. I to the Housing Act, 1949. In so far as the expression, the working class, is still capable of definition, there is no doubt but that it can properly and fairly be applied to the tenants of the privately owned houses in and near Reading of which particulars were given in evidence.'

The working class, if it means anything, may, I suppose, mean persons who occupy council houses; but there are many privately owned houses of that type or standard, and it may be that 'working class' means persons who would occupy such houses if they could get them. I cannot think that the qualification or description of a man as a man who would be anxious to get a council house, if he could, would connote that he was poor. It does not follow at all that poverty is any part of the qualification for getting a house of that type. I do not see that I can infer poverty from the words used.

I was referred by counsel on behalf of the Attorney-General to a number of cases in which, though the word 'poverty' was not used, the qualification of poverty was inferred from the

general context. Thus in the most recent case, In *re Coulthurst*, the Court of Appeal came to the conclusion that a gift for widows whose financial circumstances made them most deserving of assistance connoted that they were poor widows. Similarly, in *In re Dudgeon* [(1896) 74 LT 613] Stirling J. held that the fact that the amount there under discussion was 4s. 0d. a week could be taken to mean that it must be given to a person to whom 4s. 0d. a week would be worth having, and who, therefore, must be a poor person. The same argument was used in *In re Lucas*, which was decided by Russell J.

Finally, in the most recent case, *In re Glyn Will Trusts* [[1950] 2 All ER 1150], Danckwerts J. had to construe the words 'for . . . building free cottages for old women of the working classes of the age of 60 years or upwards.' There the expression 'working classes' again appears, and he construed it merely as meaning persons who had to work for their living, and he came to the conclusion that an old woman who had worked for he living and was over 60 was a person likely to be in straitened circumstances, and, therefore, poor. On that account he held the gift to be a good gift. He also made some observations about aged persons with which I am not concerned here, but the ratio decidendi was that out of old age and working class it might be inferred that poverty was a necessary qualification.

What is there here? Nothing of that kind. These are not old persons; they are not widows. They are merely men working in the docks and their families, and, therefore, I cannot infer any element of poverty here.

Outcome

Accordingly, the trust in this case failed on the basis that the working classes were not a section of the public confined to those who were poor.

As with *Re Gwyon*, the trust did not exclude those who were not poor in that, as Harman J explains (at p.270), 'Although a man might be a member of the working class and poor, the first does not at all connote the second.'

In other words, the term working class does not necessarily mean that a person is poor, and that the section of society that is in employment includes a whole gamut of persons who may be, but who are not necessarily poor. Later cases however have considered the type of relief being provided, as well as the wording of the trust, and the case of *Re Niyazi* [1978] 1 WLR 910 considered that the establishment of a working men's hostel could validly be regarded as a charitable purpose, not because working men cannot be wealthy, but because:

> The word 'hostel' has to my mind a strong flavour of a building which provides somewhat modest accommodation for those who have some temporary need for it and are willing to accept accommodation of that standard in order to meet the need. When 'hostel' is prefixed by the expression 'working men's', then the further restriction is introduced of the hostel being intended for those with a relatively low income who work for their living, especially as manual workers. The need, in other words, is to be the need of working men, and not of students or battered wives or anything else. Furthermore, the need will not be the need of the better paid working men who can afford something superior to mere hostel accommodation, but the need of the lower end of the financial scale of working men, who cannot compete for the better accommodation but have to content themselves with the economies and shortcomings of hostel life.[17]

[17] *Re Niyazi's Will Trusts* [1978] 3 All ER 785 at p.789 per Megarry VC.

What the law demonstrates is that although the beneficiaries under a trust for the relief of poverty do not need to be destitute, merely that they are comparatively poor, a trust for the relief of poverty will not be valid if the beneficiaries cannot be regarded as poor or if it is possible for poor people and rich people to benefit from it.

ACTIVITY

Do you consider that the following activities would be regarded as charitable:

- providing accommodation for former railway workers;
- providing hostels for undergraduate students;
- providing financial support for new parents in London?

If you were representing the organisation that is seeking to obtain charitable status as being for the relief of poverty, what arguments would you put forward in order to support your case?

Public benefit

In addition to the general public benefit criteria discussed earlier (see Chapter 19), the issue of public benefit in relation to trusts for the prevention or relief of poverty must have regard to two specific considerations. Firstly, there must be a demonstrable benefit to the public, and secondly, it is necessary to show that the benefit is conferred upon a sufficient section of the public. The relief of poverty will benefit the public because any number of people who are regarded as poor may benefit from it, provided that the definition of the group is sufficiently large as to constitute the public. In *Biscoe v Jackson*[18] for example, the poor of Shoreditch were a sufficiently large section of the public who could benefit from the trust.

In relation to the question of whether the benefit is conferred upon a sufficient section of the public, unlike other forms of charitable purpose, charities for the relief of poverty may exist where the beneficiaries are defined by a personal connection to the donor, and it would appear that this has not been abolished by the Charities Act 2011. A personal connection may be in the form of a donation to one's poor relations, or a donation to one's poor employees[19] or a donation to the fellow members of one's club. In the case of *Re Compton*,[20] Greene MR regarded these cases as being anomalous, but could not deny that they had been accepted as being valid for a long time. Accordingly, he alluded to the fact that even though the beneficiaries are defined by a personal connection to the testator, the trust may be beneficial to the public at large, possibly on the grounds that alleviating poverty, however small the group of people whose poverty is to be alleviated, is a benefit to society more generally on the grounds that it reduces inequality and the lack of opportunity that arises from poverty.

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[18] *Biscoe v Jackson* (1887) 35 Ch D 460.
[19] *Dingle v Turner* [1972] AC 601.
[20] *In Re Compton, Powell v Compton and Others* [1945] Ch 123.

EXTRACT

Re Compton, Powell v Compton & Others [1945] 1 Ch 123

Case facts

The case concerned a trust to provide scholarships for the children of three relatives of the deceased testatrix.

Lord Greene MR

I must now turn to the 'poor relations' cases on the analogy of which Cohen J. felt himself constrained, against his own view, to decide against the next of kin. The authorities relied on by the respondent are as follows. In *Isaac v. De Friez* [(1754) 2 Amb 595] the gifts were (1.) a gift of two annuities to the poorest relations of the testator and of his wife; (2.) a gift of income to one poor relation of the testator 'for a portion in the way of marriage and putting him or her out in the world,' and (3.) a similar gift of income to one poor relation of his wife. These gifts were upheld as good charitable gifts, but no reasons for the decision appear in the report. This case was followed in *Attorney-General v. Price* [(1810) 17 Ves 571], where the gift was in favour of the testator's poor kinsmen and kinswomen and their offspring and issue which shall dwell in the county of Brecon.' Sir William Grant M.R., followed *Isaac v. De Friez* saying: 'This seems to be just as much in the nature of a charitable bequest as that. It is to have perpetual continuance, in favour of a particular description of poor; and is not like an immediate bequest of a sum to be distributed among poor relations.' In an earlier case *White v. White* [(1802) 7 Ves 423], Sir William Grant had supported as charitable a gift by a testatrix for the purpose of putting out 'our poor relations' as apprentices. By a codicil this gift was confined to two families. Sir William Grant appears to have thought that the case was similar to an earlier case of his own where 'a great number of Jews were the objects'; such a gift would no doubt be regarded to-day as satisfying the well-established rule that a good charitable gift must be for the benefit of the public or a section of the public, a test which Sir William Grant does not appear to have taken into consideration in *White v. White* or in *Attorney-General v. Price*. *Bernal v. Bernal* [(1838) 3 Myl & Cr 559], was a case in which the only matter decided arose on the construction of a will providing for poor relations who were in fact (as the will was construed) the male descendants of certain named relatives of the testator. It appears from the petition that the gift was established as a charity under a decree of December 9, 1728. What the reasons were for the decision in that behalf does not appear, and when the question of construction was raised in 1838 before Lord Cottenham L.C., there was no issue as to the charitable nature of the bequest. In *Browne v. Whalley* [[1866] W N 686], where the gift was for the relations of the testator 'who might happen to be in want or fall to decay,' the charity had similarly been established by a decree of the year 1763. In *Gillam v. Taylor* [(1870) L R 16 Eq 581], the gift was in favour of such of the lineal descendants of the testator's maternal uncle as they might severally need. This was held to be a good charitable gift on the authority of *Isaac v. De Friez* and *Attorney-General v. Price*. In *Attorney-General v. Duke of Northumberland* [(1877) 7 Ch D 745], the will, as construed by Sir George Jessel M.R., was in favour of poor persons generally with a preference for poor persons who were kindred of the testator, and in that respect the case was similar to the 'founder's kin' cases. But Sir George Jessel in his judgment referred to *Isaac v. De Friez* and *Attorney-General v. Price* and did not cast doubt on the correctness of those decisions. From this review of the authorities it will be seen that they are really all derived from *Isaac v. De Friez* and *Attorney-General v. Price*. We are invited to overrule them. I agree that they are far from satisfactory, and the original decisions were given at a time when the public character of a charitable gift had not been as clearly laid down as it has been in more modern authorities. If the question of the validity of gifts of this character had come up for the first time in modern days I think that it would very likely have been

decided differently on the ground that their purpose was a private family purpose, lacking the necessary public character, but it is in my view quite impossible for this court to overrule these cases. Many trusts of this description have been carried on for generations on the faith that they were charitable, and many testators have no doubt been guided by these decisions. The cases must at this date be regarded as good law, although they are, perhaps, anomalous.

In these circumstances the question arises whether we ought to extend the analogy of these decisions, so as to cover a trust of the kind now in controversy. Taking the view which I have already expressed, I do not think that we are bound, or ought, to do so. There may perhaps be some special quality in gifts for the relief of poverty which places them in a class by themselves. It may, for instance, be that the relief of poverty is to be regarded as in itself so beneficial to the community that the fact that the gift is confined to a specified family can be disregarded: whereas in the case of an educational trust, where there is no poverty qualification, the funds may at any time be applied for the purpose of educating a member of the family for whose education ample means are already available, thus providing a purely personal benefit and one freed, incidentally, from the burden of income tax. Failing such a ground of distinction, I can only regard the 'poor relations' cases as anomalous, and I prefer to let them remain as such rather than to extend the anomaly to a different class of case. I would allow the appeal.

Outcome

The trust itself failed, but Lord Greene's obiter comments regarding poverty trusts explain the justification for allowing poverty charities to confer a benefit upon poor relations, even though the court declined to extend this to trusts for the advancement of education.

In this extract from Rahmatian's article, an explanation is given as to the extent to which the anomaly identified by Lord Greene MR in *Re Compton* continues to be valid since the enactment of the Charities Act 2006 and remains good law since the Charities Act 2011 became law.

EXTRACT

Rahmatian, A. (2009) 'The continued relevance of the "poor relations" and the "poor employees" cases under the Charities Act 2006' 73(1) *Conveyancer and Property Lawyer* 17–19

The presumed position of the 'poor relations' and 'poor employees' cases under the new law

The abolition of the public benefit presumption for all categories of charitable purposes in the Charities Act 2006 puts all charitable purposes on the same footing. That is claimed by the Explanatory Notes, but if that were indeed the case, then the 'poor relations' and 'poor employees' cases could hardly survive in their present form. There are, however, indications that these cases have survived, so that the envisaged complete levelling of the public benefit requirement for all charitable purposes has in fact not occurred.

It appears that the abolition of the public benefit presumption does not seem to have an effect on the 'poor relations' and 'poor employees' cases because these cases were effectively not regarded as being subjected to the standard rule of public benefit requirement in the first place. The courts did not state that so pointedly, but in fact their interpretation of these cases as anomalies or exceptions leads to that result. The dividing line between a charitable trust for the

relief of poverty and a private trust has been, as was stated in Scarisbrick [[1951] Ch 622], whether the trust is for 'poor relations' with a primary intent to relieve poverty (charitable trust), or whether it is for a particular type of poor relations (private trust). A separate public benefit test does not come into play, hence the abolition of the public benefit presumption does not make any difference. Furthermore, the courts generally expressed an uneasiness in relation to these exceptional cases, but emphasised that these cases have a long tradition which numerous settlors/testators and trusts rely on, and it would therefore be inappropriate to overrule them. This argument is still important under the Charities Act 2006, particularly, because the Act had the opportunity to repeal these exceptions, but did not do so. This would have been an example of a remedial intervention by the legislator to correct the common law that has not provided for a 'mischief and defect' (reflecting the rationale of the classical 'mischief rule' in statutory interpretation). Such a correcting intervention was, for instance, the express abolition of the rule in Bain in the Law of Property (Miscellaneous Provisions Act) 1989. But the Charities Act 2006 and the Explanatory Notes are silent on the 'poor relations' and 'poor employees' cases. The Act generally did not intend to change the criteria of charitable status, and this also suggests that the 'poor relations' and 'poor employees' exceptions are still valid.

This is also the view of the Charity Commission. In accordance with s.4 of the Charities Act 2006, the Charity Commission issued guidance in pursuance of its public benefit objective. It published a legal analysis of the law on public benefit, which complements its general guidance on public benefit. In its legal analysis, the Charity Commission discusses the public benefit requirement on the understanding that Dingle [[1972] AC 601] and Scarisbrick ('the principal authority establishing that charities for the relief of poverty, are excepted from the general principle that there must not be a personal family connection or tie') remain good law. In its general guidance, the Charity Commission states that:

> '"[P]oor relations" trusts (that are concerned with the relief of poverty of people with a particular family connection) and employee benevolent funds (that are concerned with the relief of poverty of people who are connected by a common employer) can be charitable.'

Thus the situation of the 'poor relations' and 'poor employees' cases appears to be the same under the Charities Act 2006, as it was under the old law.

(b) The advancement of education

Charitable purpose

The advancement of education is a purpose that is regarded as charitable, and historically, the courts have taken a very broad approach to what may legitimately be regarded as having an educational purpose. In the case of *Royal Choral Society v IRC*[21] for example Lord Greene MR explains that to view education as only being synonymous with teaching is too narrow. Providing that the objectives of the education being provided is not political in character, or affiliated to a particular political party therefore, the courts have accepted a broad range of subjects and activities as being educational. The provision of education in the form of teaching – either by an individual or by the establishment – and maintenance of an educational institution such as a school or a university,[22] will be

[21] *The Royal Choral Society v Commissioners of Inland Revenue* [1943] 2 All ER 101.
[22] *R v Income Tax Special Comrs, ex p University College of North Wales* (1909) 78 LJKB 576, CA.

charitable.[23] Research will also be educational,[24] providing that it fulfils the requirement of providing a public benefit, discussed below, with the result that there is a need to demonstrate that the research fulfils some useful purpose rather than merely adding to the store of knowledge.[25] The provision of scholarships and prizes will also be regarded as educational.[26] Activities linked to education may also be regarded as charitable, for example sport within education[27] has been regarded as an educational purpose, as have trusts to provide annual outings for children,[28] or trusts for the establishment of a students' union.[29] Museums,[30] art galleries, theatre companies and other cultural centres may also have an educational purpose, as will projects aimed at providing educational opportunities within particular communities. Education may be advanced without there being any connection to any specific educational establishment or formalised teaching. In the case of *Royal Choral Society v IRC*[31] for example, a valid charitable trust was created for the advancement of choral singing in London, while *In Re Koeppler's Will Trust*[32] was concerned with a trust whose purpose was to organise conferences. Accordingly, any activity that may be construed as advancing education will fulfil this charitable purpose, and it will be a matter for the organisation claiming charitable status to convince the Charity Commission or the court that the proposed activity offers some educational benefit.

EXTRACT

The Royal Choral Society v Commissioners of Inland Revenue [1943] 2 All ER 101 at pp.104–105

Case facts

The Royal Choral Society was formed in order to advance choral singing in London. The case was concerned with whether this could be a charitable purpose for the advancement of education.

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[23] *Royal College of Surgeons of England v National Provincial Bank and Others* [1952] AC 631.

[24] *Re Hopkins Will Trusts, Naish and Another v the Francis Bacon Society Inc and Others* [1965] Ch 669. Here the trust was concerned with funding research into establishing whether plays attributed to William Shakespeare had in fact been written by Francis Bacon. The trust succeeded on the basis that the research and its dissemination were for the advancement of education.

[25] *Re Shaw (deceased) Public Trustee v Day and Others* [1957] 1 All ER 745.

[26] *In re Mariette, Mariette v Governing Body of Aldernham School* [1915] 2 Ch 284 where a trust to provide an annual prize to be awarded to school pupils for their performance in athletic sports was held to be charitable.

[27] *IRC v McMullen* [1981] AC 1.

[28] *Re Ward's Estate, Ward v Ward* (1937) 81 Sol Jo 397.

[29] *London Hospital Medical College v IRC* [1976] 2 All ER 113.

[30] In the case of *Re British School of Egyptian Archaeology; Murray and Others v Public Trustee and Others* [1954] 1 All ER 887, for example the trust's purpose was to conduct archaeological digs in Egypt, and to present the findings to appropriate museums. The trust was held to be charitable. The fact that materials presented to museums confers a public benefit indicates the acceptability of museums having an educational purpose. Similarly, *The Royal Choral Society v Commissioners of Inland Revenue* [1942] 2 All ER 610, Macnaghten J refers to an example of *Allsop Gell v Carver* (1884) 1 TLR 4, where an art gallery and a museum were accepted as having charitable status. Modern examples of museums that have charitable status include local museums, such as Ashby-de-la-Zouch Museum and the Brighstone Village Museum Trust, as well as larger museums such as the National Museum of Wales and the London Transport Museum.

[31] *The Royal Choral Society v Commissioners of Inland Revenue* [1943] 2 All ER 101.

[32] *In Re Koeppler's Will Trust, Re Barclays Bank Trust Company v Slack* [1986] Ch 423.

Lord Greene MR

Dealing with the educational aspect from the point of view of the public who hear music, the Solicitor-General argued that nothing could be educational which did not involve teaching-as I understood him, teaching in the sense of a master teaching a class. He said that in the domain of art the only thing that could be educational in a charitable sense would be the education of the executants: the teaching of the painter, the training of the musician, and so forth. I protest against that narrow conception of education when one is dealing with aesthetic education. Very few people can become executants, or at any rate executants who can give pleasure either to themselves or to others; but a very large number of people can become instructed listeners with a trained and cultivated taste. In my opinion, a body of persons established for the purpose of raising the artistic taste of the country and established by an appropriate document which confines them to that purpose, is established for educational purposes, because the education of artistic taste is one of the most important things in the development of a civilised human being.

In the case of artistic taste, one of the best ways of training it is by presenting works of high class and gradually training people to like them in preference to works of an inferior class. The people who undergo this process go no doubt with the idea of being amused or entertained; but it is not the state of mind of the people who go to the performance which matters for the present purposes, it is the purpose of the people who provide it which is important. If the people who are providing the performance are really genuinely confining their objects to the promotion of aesthetic education by presenting works of a particular kind, or up to a particular standard, it seems to me that that is just as much education (and, in fact, having regard to the subject-matter the best available method of education) as lecturing or teaching in a class, or anything of that kind. The Solicitor-General referred to a number of cases in which he said it was established that education in the charitable context is limited to teaching in that narrow sense. In my opinion, those cases do not establish any such proposition. I should be very sorry to think that they did. The matters that were being dealt with in those cases have nothing to do with aesthetic education or the cultivation and improvement of public taste in music or the other arts. I cannot help thinking that the Board of Education, which has taken the Council for the Encouragement of Music and the Arts under its wing, would be very surprised to learn that that enterprise, in which public funds are now being used, was not an educative one.

However, when one analyses this particular case, the fact that the performances are given to the public is not of such great importance, because the circumstance that the choir is being trained, that the training and practice of the choir is one of the principal objects, and in fact may be the primary object, of this society leads to the result that the public performance, as Du Parcq LJ pointed out, really may be regarded as something which is a consequential and necessary part of the training; because you cannot train people satisfactorily if they do nothing but rehearse-they must perform. So far as the performance to the public is to be regarded as an object in itself, it seems to me that the performance of this type of work by a trained choir is designed to raise the standard of musical taste, and to give to the public an opportunity of hearing, becoming familiar with, and appreciating a particular type of music which comprises some of the very finest musical works that have ever been written. So far as the performers are concerned, they are not members of the society; they are not paid for their services; but what they are getting is a very high level of musical education in connection with this particular type of music.

Outcome

The trust was found to be charitable.

ACTIVITY

What arguments would you propose in order to argue that the following activities are educational:

- a school of acrobatics;
- an organisation that conducts research for the purposes of finding ways of living happily;
- an organisation that distributes novels to students of sciences and humanities?

Public benefit

A number of specific issues must be considered in the context of educational trusts, in addition to the requirements discussed earlier (in Chapter 19). Firstly, it must be ascertained that the education being provided offers a benefit to the public. Accordingly, in order for educational purposes to have a public benefit it must be shown for example that the research relates to some useful topic,[33] and must do more than merely add to the body of existing knowledge.[34] There is an expectation that the research for example will be disseminated, rather than merely undertaken.[35]

Furthermore, the work to be carried out must actually educate the public. In the cases where an educational purpose has been identified, activities such as developing artistic or literary tastes,[36] correcting vulgarities of speech[37] or promoting loyalty and good discipline[38] have been regarded as being charitable, while translating a play into a 40-letter alphabet,[39] or preserving a collection of poor-quality paintings and broken crockery[40] were activities that were not so regarded.

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[33] *Society of Immigrant and Visible Minority Women v Minister of National Revenue* (1999) 169 DLR (4th) 34, Can SC.

[34] In the case of *Re Hopkins' Will Trust, Naish and Another v Francis Bacon Society and Others* [1965] Ch 669, Wilberforce J explains (at p.680) that in order to be charitable, research must be shown to be 'either be of educational value to the researcher or must be so directed as to lead to something which will pass into the store of educational material, or so as to improve the sum of communicable knowledge in an area which education may cover – education in this last context extending to the formation of literary taste and appreciation (compare *Royal Choral Society v Inland Revenue Commissioners*), Whether or not the test is wider than this, it is, as I have stated it, amply wide enough to include the purposes of the gift in this case.'

[35] This was one of the stipulations in the case of *Re Besterman's Will Trusts* (21 January 1980, Unreported) per Slade J, and repeated by him in *McGovern v A-G* [1982] Ch 321 at 352–353.

[36] *Royal Choral Society v IRC* [1943] 2 All ER 101.

[37] *Re Shaw's Will Trusts, National Provincial Bank Ltd v National City Bank Ltd* [1952] Ch 163, [1952] 1 All ER 49.

[38] *Re Webber, Barclays Bank Ltd v Webber* [1954] 3 All ER 712.

[39] *Re Shaw, Public Trustee v Day* [1957] 1 All ER 745.

[40] *Re Pinion, Westminster Bank v Pinion and Another* [1964] 1 All ER 890.

EXTRACT

In Re Shaw, Public Trustee v Day [1957] 1 All ER 745 at pp.754–756

Case facts

The playwright George Bernard Shaw left a legacy in his will which provided money for the purposes of undertaking research in order to discover whether implementing a 40-letter alphabet Shaw had devised would save time compared to using the standard 26 letter alphabet, and also in order to translate Shaw's play *Androcles and the Lion* into this alphabet.

Harman J

It is hard to ascertain what are the limits of purposes held to be beneficial to the community 'in a way which the law regards as charitable'. Lord Simonds in the case last cited grapples with this difficulty, and is fair to admit that it is very difficult to reconcile all the cases. His Lordship opines (ibid, at p 520) that 'Each case must be judged on its own facts and the dividing line is not easily drawn . . . 'It seems to me, however, that in the present case I am stopped on the threshold by the word 'beneficial'. Who is to say whether this project is beneficial? That, on the face of it, is a most controversial question, and I do not think that the fact that the testator and a number of other people are of opinion that the step would be a benefit proves the case, for undoubtedly there are a great many more people, at present at any rate, who think the exact contrary. That is why the testator directs the steps which he recommends to be taken. They are intended to overcome the opposition and sloth of the great majority who prefer to stick to what they know and to use that to which they are accustomed. I do not see how mere advertisement and propaganda can be postulated as being beneficial. Mr Isaac Pitman is the author of a singularly able piece of pleading on the subject in his affidavit, but, even if I were persuaded of the merits of the scheme, I cannot think that my opinion on that subject is relevant or can be the deciding factor.

I feel unable to pronounce that the research to be done is a task of general utility. In order to be persuaded of that, I should have to hold it to be generally accepted that benefit would be conferred on the public by the end proposed. That, however, is the very conviction which the propaganda based on the research is designed to instil. The testator is convinced, and sets out to convince the world, but the fact that he considers the proposed reform to be beneficial does not make it so any more than the fact that he describes the trust as charitable constrains the court to hold that it is.

A case on a parallel subject, spelling reform, came before Rowlatt J on an income tax point. That is Trustees of the *Sir G B Hunter (1922) 'C' Trust v Inland Revenue Comrs* ((1929), 14 Tax Cas 427). The headnote reads:

> 'The appellants claimed that the income of a trust of which they were trustees was exempt from income tax under s. 37(1)(b), Income Tax Act, 1918, on the ground that the trust was established for charitable purposes only, and that the trust income was applied to such purposes only. The trust deed provided that the net income and, after a period of years, the capital, of the trust should be paid or applied to the benefit of the Simplified Spelling Society or in certain circumstances, as to which the trustees had wide discretionary powers, to the benefit of or to promote the formation of any other society or association having similar objects. The objects of the society were to recommend and to further the general use of simpler spellings of English words than those now in use. It engaged in propaganda to influence public opinion in favour of its objects and to gain for them the approval of education authorities. The appellants claimed that the purposes for which the society was established were charitable either as being educational or as being beneficial to the community. Held, that the trust was not established for charitable purposes.'

In the Case Stated (ibid, at p 430) I find that it was contended for the society that its proposal had two practical advantages:

> '(i) By the adoption of the system, spelling would be more quickly learned by a child, and the time so saved could be utilised in training the child's mind in other directions. The system would thus benefit education indirectly. (ii) The system was of general advantage, because by making the sound of words correspond with their written representation, it would lead to better speech, and by facilitating the learning of English by non-English speaking people, whether British subjects or foreigners, would help the adoption of English as an instrument of international communication.'

The society contended:

> '(1) That the society was established for educational purposes only: (2) That alternatively the society was established for purposes beneficial to the community only . . .'

The Crown claimed:

> '(1) That the trust was not established for educational purposes only or for purposes beneficial to the community but for the advancement of an idea or theory . . .'

With that view the Special Commissioners agreed, and there was an appeal which came before Rowlatt J who said (ibid, at p 432):

> 'I think that the commissioners were clearly right here. It must be distinctly understood that what the court has to decide in cases of this kind is not whether it appears that the society is pursuing a beneficial object or not, in the opinion of the court; I think that the court has nothing to do with that at all. But what the court has to decide is whether the object of the society is one that is charitable within the meaning of the rule governing courts of equity and the Income Tax Acts. The objects of this society or any other society which would benefit under this trust is simply to make spelling more simple. Everyone would agree up to a point that it is probably advantageous. Probably as you go on you will get differences of opinion; but, right or wrong, the question is whether that is a charitable object. You have people trying to promote the simplification of spelling, or the simplification of grammar, or the uniformity of pronouncing, or the simplification of dress, or the simplification or reform of any of the conveniences of life. But in my judgment they are nowhere near either of the express categories mentioned by Lord MacNaghten [[1891] AC 531] in the well-known judgment, *Income Tax Special Purposes Comrs. v. Pemsel*, or within the classes of cases which come within the general classes in the Act. I think that this case is hardly arguable.'

Such words of such a judge must have great weight with me.

It seems to me that the objects of the alphabet trusts are analogous to trusts for political purposes, which advocate a change in the law. Such objects have never been considered charitable. In his celebrated speech in *Bowman v Secular Society Ltd* ([1917] AC 406) Lord Parker of Waddington said (ibid, at p 442):

> 'Now if your Lordships will refer for a moment to the society's memorandum of association you will find that none of its objects, except, possibly, the first, are charitable. The abolition of religious tests, the disestablishment of the Church, the secularisation of education, the alteration of the law touching religion or marriage, or the observation of the Sabbath, are purely political objects. Equity has always refused to recognise such objects as charitable. It is true that a gift to an association formed for their attainment may, if the association be unincorporated, be upheld as an absolute gift to its members, or, if the association be incorporated, as an absolute gift to the corporate body; but a trust for the attainment of political objects has always been held invalid, not because it is illegal, for everyone is at liberty to advocate or promote by any lawful means a change in the law, but because

the court has no means of judging whether a proposed change in the law will or will not be for the public benefit, and therefore cannot say that a gift to secure the change is a charitable gift.'

I, therefore, do not reach the further inquiry whether the benefit is one within the spirit or intendment (as it is called) of the Statute of Elizabeth (43 Eliz c 4), but, if I had to decide that point, I should hold that it was not.

Outcome

The trust was not regarded as being charitable.

Political objectives and education

As was outlined above however, educational charities that have a political objective will not confer a public benefit, as may be demonstrated from the case of *Southwood v Attorney General*.[41]

EXTRACT

Southwood v Attorney General [2000] All ER (D) 886 para 29–31

Case facts

Two university lecturers had attempted to establish a charity, the purpose of which was to undertake a project on demilitarisation.

Chadwick LJ

The point, as it seems to me, is this. There is no objection – on public benefit grounds – to an educational programme which begins from the premise that peace is generally preferable to war. For my part, I would find it difficult to believe that any court would refuse to accept, as a general proposition, that it promotes public benefit for the public to be educated to an acceptance of that premise. That does not lead to the conclusion that the promotion of pacifism is necessarily charitable. The premise that peace is generally preferable to war is not to be equated with the premise that peace at any price is always preferable to any war. The latter plainly is controversial. But that is not this case. I would have no difficulty in accepting the proposition that it promotes public benefit for the public to be educated in the differing means of securing a state of peace and avoiding a state of war. The difficulty comes at the next stage. There are differing views as to how best to secure peace and avoid war. To give two obvious examples: on the one hand it can be contended that war is best avoided by 'bargaining through strength'; on the other hand it can be argued, with equal passion, that peace is best secured by disarmament – if necessary, by unilateral disarmament. The court is in no position to determine that promotion of the one view rather than the other is for the public benefit. Not only does the court have no material on which to make that choice; to attempt to do so would be to usurp the role of government. So the court cannot recognise as charitable a trust to educate the public to an acceptance that peace is best secured by 'demilitarisation' in the sense in which that concept is used in the Prodem background paper and briefing documents. Nor, conversely, could the court recognise as charitable a trust to educate the public to an acceptance that war is best avoided by collective security through the membership of a military alliance – say, NATO.

[41] [2000] All ER (D) 886.

- making available (whether on the internet or otherwise) teaching materials used in the school;
- making available to students of local state schools other facilities such as playing fields, sports halls, swimming pools or sports grounds;
- making those last facilities available to the community as a whole;

were regarded as fulfilling a charitable purpose. However, the court went on to explain that merely making facilities available to the community would not suffice to render a fee-paying school charitable:

> It is obvious, we think, that a school could not assert that it was established for charitable purposes only by reference to the possibility that it might make provision of the sort described in paragraph f. We do not consider that it would even be a factor which could be taken into account, since it does not go to whether education is being provided for the public benefit; it only shows that the ancillary activity may promote the provision of education. We consider that that was the case even before the 2006 Act. But even if there is a doubt about that, the position after the Act, is tolerably clear. Section 1 requires the charity to be established for charitable purposes only. It is therefore necessary to identify each purpose which is said to be charitable. A purpose is a charitable purpose only if it fulfils the public benefit test. The public benefit test is concerned with whether the relevant purpose (education in the context of the present proceedings) is a charitable purpose, a question which is not affected by the ways in which that purpose might be promoted in contrast with being implemented. It all comes back to the proposition which we consider to be correct, namely, that ancillary activities of this sort are not part of the purpose to which they are ancillary.

Yet, this was qualified by explaining that most fee-paying schools will have charitable status:

> But the schools with which we are concerned are in a very different position. Those schools cannot as easily admit one person as another. Who a school is able to admit depends on the financial state of the school, the size of its endowment and the way in which those running the school choose to prioritise expenditure (e.g. on providing scholarships or keeping class sizes down by employing more staff) and the facilities which it provides. It is necessary for all of the schools to charge fees. They do not, it seems to us, choose the majority of their students because of a preference for students who have as a characteristic an ability to pay fees; they do so because they cannot afford not to choose such students. And, of course, the charging of fees does not, as we have seen, *per se* preclude charitable status.
>
> These practical constraints on free selection mean that the position of schools is very different from the position of the association in *Educational Grants Association Ltd*. Indeed, the class of those able to pay fees is different in nature from the type of private class considered in *Oppenheim* [[1951] AC 297] and *Educational Grants Association Ltd*. There is no nexus at all; there is simply a shared characteristic which necessarily excludes the poor. Thus those cases do not really lend any support to the argument set out in paragraph 208 which we are now addressing. The reasoning of the House of Lords in *Oppenheim* and of the Court of Appeal in *Educational Grants Association Ltd* [[1967] Ch 993] does not take us to the conclusion at paragraph c. of the argument.

The court concluded by stating that the Charity Commission's guidelines were not an accurate representation of the law. At the time of writing, the Charity Commission has yet to rewrite these guidelines. However, it is obvious that there must be a clear and more

Conclusion

The reason why Dr Southwood's contentions failed below – and the reason why, to my mind, they must fail in this Court – is not because he starts from an irenical perspective that peace is preferable to war. It is because it is clear from the background paper prepared in October 1992, and from the briefing papers to which I have referred, that Prodem's object is not to educate the public in the differing means of securing a state of peace and avoiding a state of war. Prodem's object is to educate the public to an acceptance that peace is best secured by 'demilitarisation'. I have no reason to doubt Dr Southwood's sincerity when he protests to the contrary; but the evidence is firmly against him. It is because the court cannot determine whether or not it promotes the public benefit for the public to be educated to an acceptance that peace is best secured by 'demilitarisation' that Prodem's object cannot be recognised as charitable.

For that reason I would dismiss this appeal.

Outcome

The trust was not charitable on the basis that the research was political in character.

Fee-paying schools

A controversial area in the law of charities is the question of whether fee-paying schools should have charitable status, and when the Charities Act 2011 was being enacted, this question garnered a great deal of media attention. The fact that the Charities Act 2011 removes the presumption of public benefit in relation to educational charities means that educational establishments must demonstrate that they provide a benefit to the public. However, where access is restricted to those who are able to pay the fees, it is argued that no benefit is conferred on the public at large. The legislature has however been reluctant to withdraw the charitable status of fee-paying schools, and the current guidance indicates that fee-paying schools should endeavour to ensure that an inability to pay fees should not be a barrier to access. Accordingly, there is greater pressure on fee-paying schools to demonstrate that they provide a public benefit, by, for example, making their sports facilities available to a wider sector of the public, and offering scholarships and bursaries to those who cannot afford the fees.

At the time of writing, the law relating to fee-paying schools is complicated by the judgment in *The Independent Schools Council v The Charity Commission* [2011] All ER (D) 198. Here, the court concluded that 'the hypothetical school addressed in Question A2 of the Reference (ie where the sole object of the school is the advancement of the education of children whose families can afford to pay fees representing the cost of the provision of their education) does not have purposes which provide that element of public benefit necessary to qualify as a charity.' The reason for this is that there can be no public benefit if the organisation excludes the poor. Yet, it qualified this statement by explaining that schools within this category were not likely to exist in practice. Where the school does educate those who are poor therefore, such as by the provision of grants and bursaries, then it could be charitable.

The second question to consider is whether the school is established for purposes that are purely charitable. Accordingly, activities such as

- provision of scholarships and bursaries;
- arrangements under which students from local state schools can attend classes in subjects not otherwise readily available to them;
- sharing of teachers or teaching facilities with local state schools;

than tokenistic benefit to the public from fee-paying schools, and that there must be a benefit to a wider section of the community than merely those who are able to afford the fees. The extract that follows considers the impact of the Charities Act 2006 on independent schools. However, the issues raised remain applicable post the 2011 Act.

EXTRACT

Lawson, D. (2009) 'The Charities Act 2006 and Independent Schools' *Education Law Journal* 10

The Charities Act 2006 removes the presumption that there is a public benefit flowing from any apparently charitable activity. This has been widely interpreted in the context of the charitable status of independent schools. It is seen by some as an indirect attempt to undermine independent schools while avoiding the controversy and human rights cases that would follow from any direct attempt at abolition or restriction. Against this background, the aim of this article is to explore: (1) the basic concepts of charitable status; (2) the history of fee-paying schools and their exemption from tax; (3) early steps towards applying the Charities Act 2006 (the 2006 Act).

Both in terms of number and scale, educational charities are a significant part of the sector. Over one-third of charities have objects which refer to education (68,000 out of 190,000 registered charities). Over 90% of the income for the charitable sector goes to under 10% of charities and 60% of charities have an income under £10,000. There are over 2,000 schools with charitable status. All of these will have incomes far in excess of £10,000. Schools in England and Wales are a significant part of charitable activity.

Lord Macnaghten's speech in *Pemsel* is taken as the modern legal definition of charitable purposes. Four categories of charitable purpose are given: the relief of poverty, the advancement of education, the advancement of religion and other purposes beneficial to the community. His Lordship went on to make it express that at least some charitable purposes could benefit the rich:

> 'The trusts last referred to are not the less charitable in the eye of the law, because incidentally they benefit the rich as well as the poor, as indeed, every charity that deserves the name must do either directly or indirectly.'

There are also several concepts tied up in the idea of 'public benefit'. One is that the activity should be beneficial rather than harmful. The second meaning of public benefit is that the benefit is for the public or a significant section of it and not some private group. A rebuttable presumption developed that education satisfies the second of these tests, it being self-evident that it satisfied the first.

The 2006 Act has two key provisions on public benefit. First, a purpose can only be a charitable purpose if it is for the public benefit as well as being for a charitable aim (for example the advancement of education). Secondly, the 2006 Act removes any presumption that a purpose is for the public benefit.

It is a vital starting point that education is not seen by the courts as inevitably and of itself for the public benefit in the sense of benefiting a sufficient section of the community, even indirectly. A trust to educate your own children is not charitable: 'The public element . . . is not supplied by the fact that from the son's education all may benefit'. Nor do the courts accept a slightly wider pool of beneficiaries. A trust established to educate the descendants of three families with 28 living beneficiaries under the age of 26 was held not to be charitable because

the beneficiaries were defined by a personal relationship and in consequence it was not a public trust. If 28 people are not enough, what about 100,000?

In *Oppenheim* a trust was established for the education of the children of more than 100,000 employees of British American Tobacco. This was also held not to be a charity.

The key is that the ability to benefit must not depend on personal characteristics. Beneficiaries must not need to show that they are individuals A, B or C, nor that they are related to those people as by being their children or employees. On the same basis, a charity can be to further the education of pupils at a particular school, for those of a particular religion, for those working in a particular industry or for those in a particular village. The beneficiary group can be tightly defined, but not by relationship to particular people. However, there is no need for an educational charity to be for the benefit of the poor to the exclusion of the rich: 'Education and religion . . . do not require any qualification of poverty to be introduced to give them validity'.

Fee charging

The courts have expressly considered fee charging by modern charities. The charging of high fees is likely to be acceptable if no profit is made and the fees are based on high costs.

The Town and Country Planning Act 1947 exempted land held for 'charitable purposes' from certain charges. The court had to consider the position of a fee-paying school:

> 'The proposition, put shortly, was this: that an educational trust or an educational purpose is not charitable, unless it be for the promotion of education for persons who pay less than the full value of the services which they receive. That seems to me a proposition which might at one time have been acceptable to the courts, but it is several centuries out of date . . .'

The judge relied on *Attorney-General v Earl of Lonsdale* [(1868) LR 7 Eq 377], which concluded that 'the institution of a school for the sons of gentlemen is not, in popular language, a charily; but in view of the Statute of Elizabeth, all schools for learning are so to be considered'. The only schools which were not charities were those which 'exist purely as profit-making ventures'.

Much debate has focussed on *Re Resch's Will Trusts* [(1868) LR 7 Eq 377], concerning a dispute about a large bequest to St Vincent's Private Hospital. The hospital provided a vital overflow facility for the next door public hospital. It had never been conducted as a profit-making body, although it had made cash surpluses. It charged high fees based on the high cost of medical care. The Privy Council held that this was charitable. A gift for the general purposes of a hospital was prima facie charitable unless contrary factors existed, for example that it was carried on for profit or not available to the public. There was 'no warrant for adding to the condition of sickness that of poverty'.

This is clear: medical and educational charities can provide benefits to the rich. The concept of charity is not dependent exclusively on helping people with limited means. The difficulty arises in taking this one step further. Does the concept of charity require that people with limited means can benefit from the charity? If so, is it sufficient that they might benefit or must it be shown that they do benefit? Lord Wilberforce concluded that:

> 'To provide, in response to public need, medical treatment otherwise inaccessible but in its nature expensive, without any profit motive, might well be charitable: on the other hand to limit admission to a nursing home to the rich would not be so. The test is essentially one of public benefit, and indirect as well as direct benefit enters into the account.'

Lord Wilberforce suggested that the poor were not excluded – the only people excluded were those who had not paid sufficient insurance and could not get a dispensation from payment. This reads a little like saying that a charity has to be open to anyone in the way that the Ritz is open to anyone. Alternatively it suggests that it can be acceptable to exclude those of moderate means but admit the poor (by disapplying fees) and the rich (who pay).

Re Resch was applied by the Chancery Division in a case concerning a development of housing for pensioners to be let on long leases to those in need of the accommodation and able to pay a service charge. The judge rejected the argument that a charitable gift had to be by way of 'bounty rather than bargain', giving the example of fee-paying schools. Charging a fee was acceptable so long as no profits accrued to the provider of the service.

In *Re Resch* Lord Wilberforce found a 'general benefit to the community' from the relief to the beds and medical staff of the general hospital. The Charity Commission accepts that *Re Resch* allows high fees to be charged and that indirect benefits can be taken into account in assessing public benefit. However, it contends that the case also provides that the operation of a charity cannot be limited to the rich and that indirect benefit cannot alone be sufficient to show public benefit, because there is always some indirect benefit even from provision made exclusively for the rich. The Independent Schools Council (ISC) argues 'this reading of *Re Resch* is extremely strained'.

The Charity Commission and the guidance

The Charity Commission has to make the first attempt to apply the new law to the charitable sector. Conceivably it might proceed in one of three directions. It might conclude that the 2006 Act makes no difference. It might take charitable status away from schools that do not meet the 'public benefit' test. This is what schools are often concerned about, but there is a more radical third option:

> 'The privileges claimed by the schools are not nearly as ancient as their original obligations as charities . . . Withdrawing their charitable status would be privatization without compensation. The appropriate response is to enforce their charitable obligations as the Charity Commission has now decided.'

By s 4 of the 2006 Act the Charity Commission is required to issue guidance 'in pursuance of its public benefit objective'. It will certainly not fail to meet this requirement – there has been a torrent of guidance, supplementary guidance and legal guidance on charities, education, public benefit and fee-charging.

The guidance suggests numerous sub-principles to the over-riding principle of public benefit, for example that the benefit must be related to the aims and the beneficiaries must be appropriate to the aims. The opportunity to benefit must not be 'unreasonably restricted' by the ability to pay fees.

The guidance also explains the importance of the objects stated in the trust deed for assessing activities carried out by the charity. The public benefit of an educational charity which is limited to running one school will be assessed against this objective, whereas a charity with more general purposes will be assessed against those wider goals. At its simplest the consequence is that tangential activities such as fundraising at the school will not count towards the assessment of public benefit. At a more complex level this may have an impact on whether allowing the community to use the school's facilities is a relevant factor for public benefit.

The guidance on public benefit accepts that charging high fees is not inevitably blocked, but asserts that it can be if they are in effect a barrier to access and provides:

> '. . . people who are unable to pay those fees must, nevertheless be able to benefit in some material way related to the charity's aims. This does not mean that charities have to offer services for free. Nor does it mean that people who are unable to pay the fees must actually benefit, in the sense that they choose to take up the benefit. They must not be excluded from the opportunity to benefit, whether or not they actually do so . . . Fee charging charities are encouraged to be positive, innovative and imaginative . . .'

Annex C of the guidance on *Public Benefit and Fee Charging* gives a long list of methods of benefiting those who cannot pay fees including: (1) subsidised or free places; (2) developing links with grant-making trusts so as to provide free services; (3) lending equipment, staff or facilities; and (4) allowing state school pupils to attend certain lessons or events. The *Charities and Public Benefit* guidance also suggests that state schools might then be charged for these link-ups (which must raise the risk of creating a second subsidy in a circular justification of the first). Dame Suzi Leather, chair of the Charity Commission, has suggested further examples, including creating courses for maintained schools, inviting pupils to lessons or after school clubs and running summer schools. She has also confirmed that 'we absolutely recognise that what any charity can do when it comes to public benefit will depend on its resources'. In a similar vein Andrew Hind, chief executive, states that: 'Culls of the register are not on anyone's agenda'.

The ISC has lodged a thorough and fascinating response to the draft consultations. First, it argue that 'public benefit' is not, in its legal sense, a product to be delivered but a description of charitable purposes. It is the purposes which must be of benefit and open to a sufficient section of the public. It points out that the 2006 Act requires that 'purposes' are assessed, whereas the Scottish legislation refers to what is 'provided'.

Secondly, the key to public benefit is not those who can afford the fees, but those eligible to benefit from the charity. If 20,000 children meet the admission criteria then this is the relevant pool to determine public benefit, and not the sub-set who can afford the fees or the sub-set who in fact attend the school. The ISC may take this too far by arguing that the courts would not consider if the poor were excluded, but only whether the deed expressly excluded them. It seems that the court in *Re Resch* did indeed look at the practicalities of fee charging (although at a very superficial level).

Thirdly, the ISC suggests that focussing on those who cannot afford fees rather than on pupils might breach a trustee's legal duties and that the Charity Commission has therefore set up a potential conflict of duty.

The case for this process is as follows. At their best the reforms promise to weave communities more closely together and to increase access to schools which have much to offer. The process could reinvigorate the charitable mission of some of our largest charities and that surely is the purpose of the Charity Commission. Annual reporting alone will help to focus the attention of trustees on the charitable goal. The history set out above shows that schools have long operated in a legal context and shows that the legal system has previously been involved as an agent of change and a forum for debate.

Most people would agree, as *Oppenheim* states, that the claim to come within the privileged class of charities should be clearly established. The difficulty comes with agreeing the tests to apply to assess admission to that group.

Personal nexus

Section of the public and personal nexus

The provision of education for a limited class within society may be charitable, such as where education is provided in the form of a single-sex school. However, the general rule that the beneficiaries of a trust must not be defined by a personal nexus to an individual or an organisation applies in the context of trusts for the advancement of education, and indeed many of the cases where the personal nexus issue is discussed concern trusts where the purported beneficiaries are connected either to the testator (*In Re Compton*)[42] or to an organisation (*Oppenheim v Tobacco Securities*).[43]

[42] *In Re Compton, Powell v Compton* [1945] Ch 123.
[43] [1951] AC 297.

EXTRACT

Re Compton, Powell v Compton & Others [1945] Ch 123 at pp.131–137

Case facts

The case concerned a trust to provide scholarships for the children of three relatives of the deceased testatrix.

Lord Greene MR

I will postpone for the moment the consideration of what I have called 'the poor relations cases' and will now turn to the particular case of educational trusts. The references to such trusts in the preamble to the Statute of Elizabeth are as follows: 'the maintenance of schools of learning, free schools and scholars of universities; the education and preferment of orphans.' The references to scholars and orphans cannot be construed (at any rate nowadays) as referring to individuals. So to construe them would involve a departure from the principle that a trust in order to be charitable must be for the benefit of the community or a section of the community. It is no doubt true that the conception of an educational charity has been extended beyond the rather narrow classification in the preamble, but the authorities cited to show that a trust for the purpose of educating members of a specified family or specified families is a valid charitable trust do not, I think establish that proposition. In Tudor on Charities, pp. 30, 31, I find this statement: 'Bequests for the education of the donor's descendants and kinsmen at a school or college' are valid charitable bequests. The authorities cited are three and I must examine them. The first is *Spencer* v. *All Souls College* [(1762) Wilm 163]. That was a case in which Wilmot J. (as he then was) sat as an assessor to the Archbishop of Canterbury, the Visitor of the College, upon appeals by certain 'founder's kin' who claimed the right to be elected as fellows of the college against the decision of the warden and fellows who had elected other persons. The statutes of the founder, Archbishop Chicheley, laid it down that in all elections of fellows 'Principaliter et ante omnes alios, illi qui sunt vel erunt de Consanguinitate nostra & genere, si qui tales sint, ubicunque fuerint oriundi, dum tamen sint reperti habiles& idonei, secundum Conditiones superius& inferius recitatas, sine aliquo Probationis tempore, in veros dicti Collegii Socios ab initio eligantur& etiam admittantur: Quibus deficientibus,' etc. In other words, preference was to be given to the founder's kin, a very common provision in the case of ancient foundations. The college contended that the relationship of the appellants to the founder was so remote as not to fall within the 'consanguinitas et genus' prescribed by the founder. Wilmot J. in his opinion declined to accept the contention that a line ought to be drawn beyond which a candidate ought not to be regarded as founder's kin. The primary object of the founder in that case was to endow a college for the advancement of learning: the preference to his own kin was merely a method of giving effect to this intention. The validity of such dispositions had never been questioned from remote ages and was not questioned in the case. 'Founder's kin' fellowships in the Universities of Oxford and Cambridge were for the most part abolished under the powers conferred by the Oxford University Act, 1854, and the Cambridge University Act, 1856, respectively. The *All Souls* case, in my opinion, affords no support to the proposition for which it is cited in Tudor.

The next authority relied on by Tudor is *Attorney-General* v. *Sidney Sussex College* [(1869) 4 Ch App 722]. In that case a testator by his will, made in the year 1641, had devised certain lands to Sidney Sussex College, Cambridge, and Trinity College, Oxford, equally 'for the only use, education in pietie and learninge of foure of the descendants of my brothers and sisters, and three of the descendants of the brother and sister of my first wife, and three of the descendants of the brothers and sisters of my second wife, or, in default of such, to their next poor kindred.' Each of the colleges had, ever since the death of the testator, required that a person claiming the benefit of these educational trusts should become a member of the college. Sidney Sussex

College had always applied its share of the rents, in so far as they were not used for the education of persons referred to in the will, as part of the general funds of the college. Trinity College had in effect done the same thing down to the year 1826, since when its share of the rents had been used to provide exhibitions in the college. The proceedings were by way of information filed at the instance of a descendant of a brother of the testator's second wife, praying a declaration that the educational gift, and the gift to the poor kindred, were good charitable gifts. The case, on the relevant point, came first before Sir John Romilly M.R., who was of opinion that the trust was a good charitable trust 'in favour of certain poor persons,' and that subject to the rights of such persons, if any could be found, the property was given beneficially between the two colleges. The colleges, be it observed, had disregarded the possible claims of persons interested under the second branch of the trust, namely, that in favour of the poor relations, and the effect of the decision of the Master of the Rolls was that they were not entitled to do so. The actual declaration as reported was to the effect that the lands were held in trust to educate the descendants mentioned in the will, and that in default of such persons the poor kindred of the testator's wives were absolutely entitled. On appeal to Lord Hatherley L.C., Sidney Sussex College claimed that in default of descendants willing to become members of the college the college was entitled to the whole of the rents; while Trinity College argued that the only trusts were for education. The principal point which arose appears to have related to the claim of the colleges to require claimants to become members of the college, a claim which had been in effect negatived by the declaration made by Sir John Romilly. The order made by the Lord Chancellor declared that the two colleges were entitled to the property subject to a trust to educate the descendants according to the course and usage of instruction in the colleges (thus confirming the construction put forward by the colleges) with such limitations over as appeared in the will in default of such descendants. Two points deserve mention. First, the gift was construed as a gift to the colleges upon trust to educate the descendants at the colleges. Secondly, no one appears to have questioned the validity of the trust: the only controversy was as to its true meaning. When the facts of this case are examined it is, I think, clear that it does not support the general proposition laid down in Tudor. It was a very special case, and resembles in some respects the 'Founder's kin' cases.

The third case is the Irish case of *In re Lavelle, Concannon* v. *Attorney-General* [[1914] 1 IR 194] a decision of O'Connor M.R. in Ireland. There the bequest was to an educational body (called a college) the income to go to the education of the relations of the testator in that college. In this respect the case resembled the *Sidney Sussex* case. The only passage in the judgment which deals with the question is where the Master of the Rolls says: 'Gifts for the advancement of education are undoubtedly charitable and it has been decided that bequests for the education of the donor's descendants and kinsmen are charitable.' He then refers to the *All Souls* case and the *Sidney Sussex case*. It is clear that the Master of the Rolls was merely accepting the statement in Tudor, and I do not think that this case carries the matter any further. One further case was cited to us by counsel for the respondent, that of *In re Rayner* [(1920) 122 LT 577], a decision of Eve J. There were two bequests the validity of which was in question. That relevant for present purposes was a bequest to the governors of a commercial company of shares in the company with a direction to apply the income to the education of children of persons who, for five years and upwards, had been in the employment of the company. If the bequest should be held to be invalid the testatrix gave the shares to her executor absolutely. Eve J. did not have the advantage of any argument, since the only person interested in disputing the validity of the gift was the executor, who supported the view that it was a valid charitable gift. In a very short judgment Eve J. said that there was present an element which was wanting in his earlier decision, already quoted, *In re Drummond* [[1914] 2 Ch 90] in that the object of the gift was to promote education. He distinguished *In re Drummond* on the ground that in that case the gift was not restricted to the relief of poor people within the meaning of the statute, and said that in the case before him

the gift was for an object within the statute and was accordingly a charitable gift. He was of opinion that the gift was 'it is true limited to a section of the public, but the section intended to be benefited was sufficiently defined.' I do not regard this as a satisfactory decision. There was no argument; the learned judge without giving any reasons treated the gift as one in favour of a section of the public; and in distinguishing *In re Drummond* he apparently overlooked the fact that in that case the absence of the element of poverty was only one of the grounds of the decision. As I have already pointed out, the argument that the case fell within the fourth of Lord Macnaghten's classes was negatived on the ground that the trust in favour of the employees of the company was a trust not for public purposes but for private individuals. The decision, in my opinion, was wrong, so far as it dealt with the educational trust.

I must now refer to two more Irish decisions. The first is *Laverty v. Laverty* [[1907] 1 IR 9]. There the testator gave his estate on trust for the support and education of boys and men 'of the surname of O'Laverty or Laverty, O'Lafferty or Lafferty.' It was held that this was not a charitable gift. Barton J. said: 'In my opinion, a valid charitable trust might be created for the advancement of education, with a preference for persons of a particular surname, either by the endowment of or gift to a school or college' – this I may interpose, would resemble the 'founder's kin' provisions – 'or by a gift, as in the present case, to trustees, if sufficiently definite.' He then proceeded to hold that the gift was not of that character since it might have been intended to work as a matter of private bounty – for example, by employing a governess or tutor for some wealthy young Laverty. So in the present case the income in certain events might be applied in paying for a tutor for the Earl of Sandwich of the day, irrespective of his means. The other case, by the reasoning in which Cohen J. was clearly much impressed, is *In re McEnery* [[1941] IR 323]. There the testator made a bequest 'for enabling the sons and daughters and male descendants' of his brothers 'to obtain professions, each suitable student to receive 100l. yearly, for a reasonable time.' Gavan Duffy J. began by pointing out the public character of a legal charity. 'Courts of Equity' he said, 'have been consistently insistent on the public character of a legal charity, importing a benefit to the community or a section of the community.' He then pointed out the difference between an endowment to maintain two scholars in Oxford and Cambridge and a trust for the personal educational benefit of the heir for the time being of a testator for ever: and he went on to say that there was nothing public about the latter purpose, and that the prospective heirs would not constitute a section of the community for whom a charitable trust could be established. He explained the *All Souls* case, the *Sidney Sussex* case and *In re Lavelle* as showing no more than that the founder of a charity or a benefactor may lawfully associate his descendants with his bequest to a charitable institution, and thus enable them to participate in his liberality. He then expressed the opinion that the trust before him was too narrow to be charitable. The motive, he said, may have been charitable, but the intention was to benefit specific individuals. If I may respectfully say so, this reasoning appears to me to be unassailable. Even if my view that the necessity of founding a claim upon the fact of kinship to an individual precludes the possibility of regarding a gift as charitable is too widely stated, I am of opinion that a gift for the education of descendants of named persons must be regarded as a family trust and not as one for the benefit of a section of the community, on any fair view of what that phrase may mean. Such a purpose appears to me to be no more a public educational purpose than the purpose of enabling a body of individuals to perfect themselves by prayer and meditation is a public religious purpose (see *Cocks v. Manners* [(1871) LR 12 Eq 574)]. Moreover, as Morton L.J. has reminded me, if such a trust is held to be charitable a testator will be able to provide in perpetuity for the education of his kinsmen in a way which will avoid the payment of income tax on the trust income.

But it is suggested that even if this be true, the present case presents a feature which is sufficient to make the gift a charitable one, namely, the direction as to the kind of education

to be provided. It is said that it is beneficial to the community to have individuals so educated as to become God-fearing men and women and good citizens, and that a trust designed to increase the number of persons of that description, even if they are confined to the narrow limits of a particular family or particular families, must for that reason be regarded as charitable. I venture to suggest that in this sense education by itself, without reference to any particular kind of education, is in the same way beneficial to the community, and that it is to the benefit of the community to have as many educated persons among its members as possible. Again, there are many particular kinds of education which may be considered specially beneficial – for example, it is clearly to the advantage of the community to have a large number of trained scientists, and from the argument it would appear to follow that a trust to give a scientific education to the descendants of a testator's three brothers would be a valid charitable trust. The argument, moreover, would appear to lead to the conclusion that a gift to educate, for example, a number of named nephews and nieces of a testator, so as 'to fit them to be servants of God serving the nation' would be charitable by reason of that direction. In such a case there would, of course, be no question of perpetuity, so that it would not be necessary to regard the trust as charitable in order to support it in that regard. But if the property devised or bequeathed consisted of real estate or impure personality, the effect of holding the gift to be charitable would, in past days, have been to invalidate it under the Statute of Mortmain, and I cannot think that any court would have so regarded the gift as to produce that result. Moreover, if the argument is right, it would mean that a testator could provide for the education of his family in perpetuity, thus, incidentally, obtaining relief from income tax, merely by adding to his bequest a direction that the kind of education to be provided is to be such as will be calculated to make them God-fearing men and public-spirited subjects of the King – a direction which, as I have already pointed out, would cover the ordinary public school education.

Outcome

The trust was not charitable.

EXTRACT

Callman, J. (1993/94) 'Avoiding Being Personal: Public Benefit and the Personal Nexus in Educational Trusts' 2(3) *Charity Law and Practice Review* 203–209

The example

What of my example: 'a trust for the education of would-be pupils who are the descendants of old boys of my school'? Lord MacDermott in his dissent in *Oppenheim* stated:

> 'I have particularly in mind gifts for the education of certain special classes such, for example, as the daughters of missionaries, the children of those professing a particular faith or accepted as ministers of a particular denomination, or those whose parents have sent them to a particular school for the early stages of their training. I cannot but think that in cases of this sort an analysis of the common quality binding the class to be benefited may reveal a relationship no less personal than that existing between an employer and those in his service.'

With respect to Lord MacDermott, one can draw distinctions, albeit not absolutely persuasive ones. Focusing on my example, parents do contract with a private school to educate their

children. A contract of employment is. however, of a different nature. Parents purchase a service from a school, i.e., the education of their children. If the purchase of education was deemed 'personal', would that same logic not then apply to the purchase of goods? Could a trust for the education of those who shop at a particular High Street store be regarded as personal? Surely not. In an employment contract the 'purchase' is inverted, i.e., the employer purchases labour from the employee. The relationship is of a fundamentally different nature; employees 'sell' a part of themselves (their time and effort) to their employer. That is a very personal relationship. Furthermore, a school, unlike a company, does not have a separate legal identity.

In a trust for the benefit of the descendants of old boys, the relationship is once removed. The beneficiaries are 'would-be pupils' and not 'actual pupils'. In other words the class of beneficiaries is defined not by its relationship to the school, but by a relationship to an ancestor who is himself defined by his attendance at the named school. The first link, descendant-ancestor, is clearly personal; the second, ancestor-school, is not. Therefore, there is neither a direct contractual nexus nor a personal nexus between the potential pupil and either the named school or the grantor.

Size of the group

There is an additional question of the size of the group or class who are to be the beneficiaries. The general test establishes that the class qualifying must not be negligible. Nevertheless, the Courts have upheld trusts for such groups as the daughters of missionaries. The class of descendants of old boys of a particular public school is itself likely to be a not insubstantial group. Given the number of pupils who attend a school each year, the long history of many schools and the average number of descendants of each former pupil, one would expect a number amounting to several thousand. Furthermore, it appears from the logic applied in the cases, that the size of the class should be applied as a second stage of the test. If the trust is personal, then whether there be 10, 100, 1000, or 100,000 members of the class, the trust will remain non-charitable. This, of course, does not necessitate the opposite inference; if the trust is impersonal but the class is negligible, it will not be charitable. The difficulty of defining 'negligible' is a topic for another article.

Discrimination

There are particular rules additional to those considered earlier (in Chapter 19), to be considered in the context of sex discrimination and educational charities. Where the charity seeks to provide single-sex education at a specific establishment (for example a girls' school) it is possible for the trustees to make an application (either to the Secretary of State or to the Welsh Ministers) to remove the discriminatory element. However, where the charity arises from a trust or a gift, for example where a testator leaves a legacy to provide a scholarship that may only be awarded to a female student, the discriminatory element may not be removed until 25 years after the gift takes effect, unless the donor (in the case of an *inter vivos* trust) or his or her personal representatives (where the trust is contained in a will, or where the donor has died since the trust was created) give their consent in writing to the modification.[44]

[44] Equality Act 2010 Schedule 14.

(c) The advancement of religion

Charitable purpose

It is in relation to the advancement of religion that the Charities Act 2011 is likely to have the greatest impact, as this Act has made significant changes to the types of religious trusts that will be regarded as charitable and those that will not. The advancement of religion was identified as one of the four heads of charity prior to the Charities Act 2011. However, the Act has clarified the meaning of religion and, as a consequence of s.3(2), there is no longer a requirement that religion is monotheistic, and indeed a religion may include a belief that there is no god.

Religious belief

Firstly however it is necessary to define what is meant by religion. The term religion is often problematic, because although beliefs and values cannot be viewed as religions, there is also an awareness that the elements identified as being characteristics of religion (for example a belief in God) espouse a Christian perspective on those elements, with the result that the law would appear to exclude other forms of legitimate religious belief.[45]

The advancement of a form of belief, or of particular values, is not necessarily religious, and therefore political conviction or the promulgation of a non-violent way of life cannot be said to be a religious belief. In order for a belief system to be one that is religious, there is a need for the belief to be in a supreme being or in several supreme beings, and manifested by worship – or something equivalent such as meditation. This would appear to contradict the stipulation in s.3(2) Charities Act 2011 that religion can include a belief that there is no god. Nevertheless, the Charity Commission's interpretation of this is taken to mean that there does not have to be a belief in a personified deity, but that there does have to be some conception of a supreme being[46] because, as is explained by Dillon J in the case of *Barralet v Attorney General*:[47]

> Religion, as I see it, is concerned with man's relations with God, and ethics are concerned with man's relations with man. The two are not the same, and are not made the same by sincere inquiry into the question, what is God. If reason leads people not to accept Christianity or any known religion, but they do believe in the excellence of qualities such as truth, beauty and love, or believe in the Platonic concept of the ideal, their beliefs may be to them the equivalent of a religion, but viewed objectively they are not religion.

The distinction between belief and religion is also expounded by Lord Hanworth MR in *Keren Keyemeth Le Jisroel Ltd v Commissioners of Inland Revenue*:[48]

> The promotion of religion means the promotion of spiritual teaching in a wide sense, and the maintenance of the doctrines on which it rests, and the observances that serve to promote and manifest it – not merely a foundation or cause to which it can be related.

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[45] Charity Commission (2008) The advancement of religion for the public benefit. Annex A. https://www.charitycommission.gov.uk/detailed-guidance/charitable-purposes-and-public-benefit/charities-and-public-benefit/the-advancement-of-religion-for-the-public-benefit/. Site accessed 10 April 2014.

[46] Ibid.

[47] [1980] 3 All ER 918 at p.924.

[48] [1931] 2 KB 465 at 477.

Accordingly, it may be necessary for an organisation purporting to be for the advancement of religion to explain how the religion involves a belief in a supreme being, and that it is the object of worship.

The Charity Commission's guidance refers to the possibility of an adherence to a spiritual principle as being sufficient for the purpose of advancing religion, although this may be problematic in that it then becomes very difficult to distinguish between religion and other forms of belief – an issue that engendered considerable discussion when the Charities Bill was being debated in the House of Lords.

EXTRACT

Hansard HL 673 HL Official Report (5th series) cols 137–150 28 June 2005

Lord Wedderburn of Charlton moved Amendment No. 2

Our amendment pursues the question of policy which would make one paragraph of the list that has been referred to-the descriptions of charitable purposes-read, 'for the advancement of religion or belief'. There are three main headings to that argument. First . . . the Bill as it stands, which refers to 'the advancement of religion' full stop, arguably does not comply with Articles 9 and 14 of the European Convention on Human Rights on the right to manifest one's religion or belief and to have that right secured without discrimination . . . Of course, it is true that our law has in many areas come to regard freedom of religion and freedom of non-religious belief on a par. In the recent Communications Bill, the recent employment regulations and, above all, in the Equality Bill, which is going through your Lordships' House at the same time as this Bill, a key concept is that there should be a ban on, 'discrimination on grounds of religion or belief' – those words being explained as including lack of religion or lack of belief. In our submission, it is quite impossible that those words, which no doubt have a meaning, should not have the same meaning in this Bill – not by reading across from Bill to Bill, but because the object of there being no discrimination in regard to religion and belief, as the Long Title of the Equality Bill states, is the same as the object being discussed in this amendment.

The gap in the new Charities Bill is in leaving the advancement of religion not to be balanced by the advancement of non-religious belief. Of course I understand, as I am sure my noble friend will say, that the list in Clause 2(2)(a) to (k) [now s.3 of the Charities Acts 2011], which has been referred to in previous debates, does not exclude things that are analogous, as we shall come to.

There is new doubt in the Bill which is relevant to the argument on Amendment No. 2. Earlier this year on 20 January, in debating the old Bill, my noble friend Lord Bassam set out the common law notion of religion, as opposed to non-religion, in a formula which was acceptable to the commission, the Government and, indeed, the courts (Hansard col. 963). I have sworn not to cite many court cases at this stage of the new Bill, but I shall refer to one, that of the *South Place Ethical Society* [[1980] 3 All ER 918] in 1980. Mr Justice Vaisey used precisely the same words as my noble friend did when he said:

> 'To qualify as a religion under charity law, there has to be a belief in a supreme being and acts of worship of it'.

My noble friend cannot advance that argument now under the new Bill, which has very many differences from the old Bill. The old definition is no longer applicable because a new clause or a new paragraph of Clause 2 in this Bill expressly includes within 'religion' a religion that does

not involve belief in a god-one that does not have a supreme being. So that when it is said-and this is the second heading of our argument-that 'belief' is a vague term, that is now matched in the new Bill by the term 'religion', which receives no definition. To say that something is included adds to one's knowledge, but in this case it makes for more doubt about what 'religion' can include.

The same terms 'religion' or 'belief' are not only used with the same meaning in the Equality Bill; there is even a clause in the Equality Bill which expressly protects charities which benefit persons of a particular religion or belief. The parallel is quite clear.

In the new Charities Bill, non-religious belief is still excluded from mention in the list of descriptions-I say 'descriptions' advisedly-that get you halfway to the automatic tax-exempt status. That exclusion is in itself a material discrimination. The treatment is not even separate and equal.

It has also been argued that the term 'belief' is unacceptable because some beliefs might be evil, irrational and offensive. Again, that argument belongs not to the test of charitable purpose but to the question which is now the second hurdle in proving you are a charitable purpose-that of public benefit. Public benefit must now be proved, and we ask for no privilege from that. But offensive purposes would not normally be for the public benefit.

Another objection has been that 'belief' might include political beliefs. The Charities Commission has helped enormously in its paper RR12. It recently told charities promoting human rights that charities may properly adopt campaigning-it lists a number of things which are, broadly speaking, political methods-so long as these do not become 'dominant'. That perhaps is sufficient to exclude the argument on political beliefs, but Amendment No. 6 was meant to adopt that formula. However, because the amendment is defective in the form in which it appears, for which I am responsible, I shall not speak to it today.

More importantly, the Government have hitherto argued that all those arguments, even if they are wrong, are irrelevant, because an association to promote non-religious belief will always be charitable in practice under Clause 2(4), which was mentioned earlier. That is the so-called rag-bag clause, which validates any purpose

> 'regarded as analogous to, or within the spirit of'

an explicit purpose in Clause 2(2)(a) to (k).

If a fund is expressly stated to be not for the purpose of promoting religious beliefs, but for the promotion of secular beliefs, which are not 'within the spirit of' or 'analogous to' religion, it is manifestly impossible for the commission, the court or anybody else to declare that it is. One has to look for something else to which it can be analogous.

Whether it is analogous to something else in the list (a) to (k) depends on the facts. In the 1980 case of the South Place Ethical Society, it was found that further purposes were analogous to education.

This is the kernel of the case. If such a purpose for the promotion of non-religious belief is always at risk of being found not to be analogous to any express description in the list, it will not be for 'charitable purpose'. That is a risk that 'religious purposes', however they are defined, do not run. Those purposes proceed automatically across the first hurdle on to the second test of public benefit.

The balance of risk is manifestly unequal between religious and non-religious purposes. Our amendments invite the Government to remove that discrimination from the Bill.

Lord Phillips of Sudbury

I thank the noble Lord for giving way, as I am trying to help the debate, which is a difficult one. I wonder whether he has taken full account of the fact that there is a well-established branch of charity law, under what is called the fourth head, which is equivalent to Clause 2(2)(l), which is the promotion of moral or spiritual welfare, or the improvement of the community. There are many cases that validate that as an independent, stand-alone head of charity. Does the noble Lord not think that there is a secure basis on which philosophies of belief or ethics that are not traditionally religious can found and retain with confidence their charitable status?

Lord Wedderburn of Charlton

I am grateful to the noble Lord as two points arise immediately from his argument. I was about to sit down, but I shall answer them now.

First, the noble Lord begins with the proposition that a charitable purpose or the purpose in a fund, document or association that is not for religious belief explicitly, and which is not within his moral improvement formula, must prove in some other way that it is analogous. That may be very difficult to do. The noble Lord has put a limit on the analogy to suit his argument, finding it in the original deed.

It follows that there is an extra risk for the advancement of non-religious belief. It is that extra risk that creates discrimination. It is impossible not to see that there is something extra-a hoop that the purpose must go through-than what is expressly stated in the list. I beg to move.

The Earl of Onslow

When the noble Lord referred to a supreme being, was he implying that charity law applies only to religions that are monotheistic, or does it include Hinduism, which obviously is not? Does it exclude the present law of something like the National Secular Society? Perhaps he could tell me that for my education and possibly that of other Members of the Committee.

Lord Swinfen

I intervene on this amendment, although it might have been better had I intervened on Amendment No. 3 instead because I received a letter two days ago from a Mr Pravin Shah who is a Jain . . .

Mr Pravin Shah wrote to me that he was,

> 'particularly concerned to see that there is no discrimination against Jains and other religions which are similar to Jainism, but less well known in this country. I note that the new Charities Bill, while stating that one can have a religion that does not involve a belief in a god, does not actually contain any definition of religion or explain what criteria the Charity Commission are going to use in deciding whether something is a religion or not'.

He says that he is deeply worried about that. In his letter to the noble Lord, Lord Bassam, which he was kind enough to copy to me, Mr Pravin Shah says that he is pleased that the Bill includes a belief in more than one God. He continues:

> 'I was naturally therefore very pleased to see that the government have now put into the new charities Bill a provision that says that a religion does not have to involve a belief in a god. However I was surprised that there was no definition of a religion'.

He goes on to say:

> 'I would be grateful if you would kindly let been know how it is intended that the Charity Commission will now decide if something is or is not a religion?

> 'Is Jainism to be considered to be a religion after the passing of this Bill? What will happen to religions which are similar to Jainism, but are perhaps less well known in this country? What criteria will the Charity Commission apply?'

I would also like to know the answer to those questions. I have intervened at an early stage so that, if the Minister needs advice, he has time to get it . . .

Lord Borrie

I put my name down to this amendment to add my support. As we all know-or at any rate, as those who took part in the Grand Committee on the Bill before the election will know-the Government have since then sought to broaden the meaning of the vital phrase 'the advancement of religion' in the Bill by stating in the present drafting, which is different from before, that religion includes:

> '(i) a religion which involves belief in more than one god, and
>
> '(ii) a religion which does not involve belief in god'.

I welcome that to some extent, but I do not welcome the fact that the only belief that is specifically recognised is religious belief. The word 'belief' appears twice in the amended version, but only in the context of the word 'religion'. That is clear to all of us.

What is created for the advancement of non-religious systems, philosophies of belief or ethics should also be recognised as charitable, provided that they are for the public benefit, because one must establish those two points.

I particularly wish to mention the reference in Amendment No. 4 to the Equality Act 2005-which is a Bill at present, but we anticipate that it will be passed. It is provided because Part 2 of the Equality Bill forbids discrimination on the grounds of religion or belief.

Clause 45 of the Equality Bill very simply defines 'religion' as 'any religion'. It goes on to define the word 'belief' as,

> 'any religious or philosophical belief',

and adds,

> 'a reference to belief includes a reference to lack of belief'.

I favour the great simplicity of those phrases in the Equality Bill. It seems to me to be very odd, in two Bills that are likely to be passed in the same parliamentary session, that one expressly recognises 'belief' only if it is a religious belief and the other expressly recognises the significance of both religious and non-religious beliefs. I could refer to Article 9 of the European Convention on Human Rights but my noble friend Lord Wedderburn has already done so. I could also refer to the employment regulations 2003 in which religion or belief means,

> 'any religious belief or similar philosophical belief'.

It may be said, and I believe has already been said by the noble Lord, Lord Phillips of Sudbury, in his intervention-I hope he will speak further-that indirectly this Charities Bill recognises as charitable a body set up to advance non-religious beliefs by virtue of Clause 2(4)(a). That refers to current case law. As I understand it, current case law allows as charitable those bodies that are set up to improve the mental or moral welfare of the community, which is pretty broad. It is said that the Charity Commission must follow existing case law, but that can be so only because since the nineteenth century-let alone more recently-the courts have been imaginative under the residuary head of charity described by Lord Macnaghten in the leading case of *Pemsel* [[1891] AC 531] in 1891 as,

'other purposes beneficial to the community'.

Clause 2 of the Bill-this was also in the version of the Bill that we had before the general election-no longer prescribes the three well known specific purposes of charity that have been with us since the seventeenth century; namely, the relief of poverty, the advancement of religion and the advancement of education, and then a general clause. As Members of the Committee can see from Clause 2, we now have another eight specific heads of charity added on to those three. I shall not read them out as they are in the Bill.

My point is, as no doubt the Committee will have anticipated, why not expand slightly the head of charity 'the advancement of religion' by adding the words 'or belief' or have a separate specific head similar to that which my noble friend Lady Turner of Camden wants to discuss under an amendment soon to be moved? If we had a slight expansion of the head of the advancement of religion to cover belief more generally as proposed in this amendment, the amendment would be very simple. It would help many of those who may be puzzled when they look at this Act, as it will be shortly, and wonder what is allowed as charitable and what is not. In years to come that would assist the endeavours of many bodies.

Baroness Whitaker

I have a couple of points to make on the amendment which I support for all the reasons so eloquently deployed by my noble friends. That is because it seems to me that the law is not only, and perhaps not even primarily, for lawyers; it is for the citizens who intend to abide by it. Ordinary people, like me, do not understand that non-religion is included in the term 'religion'. It flies against sense. However, I am comforted by the fact that the Government share that view in numerous other pieces of legislation. I believe that we need joined-up government here. We should use the language of the European Convention on Human Rights. We should say 'religion or belief'. I am also comforted by the opinion of the Joint Committee on Human Rights, which stated:

> 'We remain of the view that protection of Article 9 rights on an equal basis could most effectively and clearly be ensured by provision on the face of the Bill, expressly extending clause 2(2)(c) to cover all religious and non-religious organisations which promote systems of belief'.

Finally, there is a question of parity: non-religion should be on a par with religion. It will not be so unless we adopt the internationally-recognised language of 'religion or belief'.

Lord Phillips of Sudbury

I am sympathetic to what I take to be the general thrust of argument of those in whose names the amendment stands. I would have supported it if the Bill had not contained the introduction of the public benefit test, which in future has to apply to all charities. Until it comes into force I concede that there is a discriminatory difference between religious charities and organisations such as the South Place Ethical Society mentioned by the noble Lord, Lord Wedderburn, which is not a religion in any conventional sense but is a body committed to the promotion of ethical principles.

As I said, at present there is discrimination against that sort of body because it has to prove public benefit, whereas religions of whatever sort – they are now extremely wide in the definition – do not. We are dealing with a Bill that is going to level that playing field. I am left wondering what advantage there is in the amendments. I agree with the noble Baroness, Lady Whitaker, that the Bill must be for laypeople and citizens, not for lawyers.

Ironically, as both a citizen and a lawyer – and indeed a charity lawyer – I think that the amendments will make life more rather than less confusing. As I said, there is a general public

sense of what is and what is not a religion. If we asked 100 men and women in the street about an organisation such as the South Place Ethical Society, whose objects are 'the study and dissemination of ethical principles and the cultivation of a rational religious sentiment'. I doubt that most people would view it as a religion. So to try and equate it with that is more confusing than clarifying.

Lord Borrie

The South Place Ethical Society was able to convince the court that it was charitable, not because it was a religion but because it advanced education. Because it happened to be able to do that it was charitable. Other societies for the promotion of beliefs in ethical conduct and so on may not have any educational role but they are there to advance a belief in good ethical conduct on a non-religious basis. Do they not appear to be excluded by the wording of the present Bill?

Lord Phillips of Sudbury

The noble Lord carried forward the argument that I was on the point of making: that the South Place Ethical Society was given charitable status, as he correctly says, not because it advances education but because by analogy it reels off the cases: *Re Price* [[1943] Ch 422], *Re Hood* [[1931] 1 Ch 240], *Re Scowcroft* [[1898] 2 Ch 638]; well known cases in this field-it was charitable under the fourth head as promoting the moral and spiritual welfare or improvement of the community.

It does not matter one whit whether one obtains charitable status on that basis or if it is a conventional religion under the religious heading. There is no difference. There is no extra hurdle to be leaped in getting charitable status on that basis. That is why I believe that the Bill moves the whole thing on and why I do not believe that the amendments will help at all.

Finally, many Members are aware of the Scientology case. After a particularly difficult application to the commission, the commission produced an extremely long and, I believe, well reasoned judgment, which was getting on for some 50 pages, in the course of which it said that,

> 'the Commission has regarded the concept of moral or spiritual welfare or improvement as a flexible basis upon which a wide range of purposes beneficial to the public may by analogy be recognised as charitable, particularly where it was apparent that the benefit flowing from the organisations' purposes and activities is readily and easily accessible to the public'.

The noble Lord, Lord Borrie, will recollect the case of Public Concern at Work, in which he was involved as chairman of the trustees and I as the solicitor. Eventually we got registration on the basis of the flexible head.

As I say, I would have taken a different view but for the public benefit introduction in the Bill. But given that it is coming, there is a solid, well established, broad-based and flexible ground on which all the organisations engaged in ethical issues-rationality and the rest of it-can find their charitable status.

The Earl of Onslow

My Lords, can the noble Lord educate me? He says that in the Bill, religion is promotable whether it has a public benefit purpose or not. Does that not lead us to the case of West African witchcraft, which is a religion of some sort and which is in my book morally reprehensible because it involves chopping people up? Are we allowing that sort of thing to have charitable status and consequential tax benefit, because there is no public benefit issue?

Lord Phillips of Sudbury

My Lords, I thank the noble Earl for his intervention. The point that I was making was that in future that sort of charity will not be a charity because it will not be able to satisfy the public

benefit test, which in future will apply to religions just like everything else. I believe that that makes my point.

Lord Bassam of Brighton

My Lords, I believed that this would be a lengthy discussion and I was not disappointed. I have listened very carefully to what my noble friend Lord Wedderburn and supporters of his amendments have said, and to other contributions during the course of the debate. It is important, not least because of that, that I explain as fully as I can the Government's position and thinking on this point.

First, non-religious belief systems which promote moral and spiritual welfare have been for some time, are now, and will continue under the Bill to be charitable. That is secured beyond doubt by subsections 2(l) and 4(a) of Clause 2. It is just worth reminding ourselves of the importance of the Southplace Ethical Society registration. It is more than some 40 years ago-or certainly 20 years-since the British Humanist Association was registered similarly. Since then, a number of other charities promoting humanist, rationalist and ethical and other non-religious belief systems have been registered.

Secondly, the Government do not accept that the Bill has any discriminatory effects between charities promoting religious or non-religious belief. The noble Lord, Lord Phillips, addressed that issue very well, with his usual forensic understanding of charity law and the intent behind this Bill. Again, this is something that we have looked at very carefully. If there were any discrimination we should have had an obligation under the European Convention on Human Rights to remove it, because the convention does not allow discrimination between religious and non-religious beliefs. In fact, an important effect of this part of the Bill is to level the playing field between religious and non-religious belief, as the noble Lord, Lord Phillips, said.

At the moment, religious organisations enjoy the presumption that they are for the public benefit, while all other organisations promoting non-religious beliefs do not. The Bill simply removes that presumption. This will mean that, after the Bill is enacted, religious beliefs and non-religious beliefs will be in exactly the same position of having to demonstrate public benefit in order to qualify for charitable status.

Thirdly, several Members of the Committee, including my noble friends Lord Borrie and Lord Wedderburn, have pointed to the Equality Bill, in which the Government have specifically mentioned non-religious belief alongside religious belief. It has been suggested that it is inconsistent of the Government to argue that non-religious belief need not have a specific reference in the Charities Bill while conceding that it needs a specific reference in other legislation. However, there is a good and, we believe, simple reason why a charge of inconsistency will not stick. It is that, without a specific reference in the Equality Bill, non-religious belief would be excluded from the scope of that legislation. In the Charities Bill, non-religious belief is present in the list of charitable purposes by virtue of subsections (2) (l) and (4) (a) of Clause 2. Those subsections bring in, from the underlying common law, everything which has already been recognised as charitable but which does not come under any of the other headings listed in Clause 2(2).

The noble Lord, Lord Wedderburn, described it as a 'catch-all ragbag', as if to suggest that it is somehow a second-class method of inclusion. We do not see it that way at all. They are not; and there is no sense in which the law gives belief systems any lesser treatment than any other charitable purpose.

The purposes covered by subsection (2) (l) are many and varied. The Charity Commission's commentary on the description of purposes in the Bill gives 15 examples, including not only moral and spiritual welfare, under which non-religious beliefs qualify, but also defence of the

realm; preservation of public order; relief of unemployment; rehabilitation of ex-offenders; promotion of industry and commerce; promotion of agriculture, and so on. Those are all very important areas of charitable endeavour today. But we cannot give everything that is charitable its own specific heading without making the list unmanageably long. Even if we had a very long list, we would still have to have a final category consisting of purposes which had not been specifically mentioned-to avoid the risk of removing, by default, charitable status from any other recognised purpose which was not mentioned in our long list.

No one, to my knowledge, has argued as a matter of principle that we should try to have a comprehensive list so that we did not need that final category. Once you have accepted that we should not go down the comprehensive route, either you must also accept that some existing charitable purposes will have to be placed together under a heading consisting of all the purposes not specifically mentioned, as the Government have done, or you must accept the risk that some current purposes might, by default, be excluded.

The Government do not want to run that risk. Nevertheless I entirely understand the very human tendency to want to see the forms of endeavour which are closest to your own heart given prominence, even if, as here, they would have only a symbolic prominence and would have no legal or practical effect at all.

Fourthly, by including the word 'belief' in the list in the terms proposed by my noble friend's amendment, we would bring in all sorts of beliefs-from, I would argue, the frivolous to the bizarre-that should have no place in charity. I am sure that many of these beliefs are sincerely held, and I do not propose to disparage anyone's sincerely held belief by naming any of them. I have heard the argument that it is safe to allow all belief systems or philosophies into the list, because those which really had no place in charity would be excluded from it by the public benefit test.

If that argument held water, we should be going for a definition of charity that did not have a list of headings of charitable purposes but simply said that anything that was for the public benefit was charitable. The great drawback of that approach is that it produces legislation that gives no clue as to the sorts of endeavour that are charitable purposes. For that reason, it was rejected both by the Strategy Unit in 2002 and by the Government since then. There has not at any stage been an appetite shown for it in any of the consultations that have taken place on the subject; nor has anyone, including the Government, yet been able to formulate a definition of 'belief' that would achieve what we wanted-by including those that should be included and excluding those that should not.

I hope that what I have said has persuaded Members of the Committee that we have thought about the issue seriously. I conclude by repeating that the Bill as currently drafted provides every possible assurance and safeguard that it will remain a charitable purpose to promote moral and spiritual welfare through non-religious belief . . .

In regard to that and to what the noble Lord, Lord Phillips, said, which I understand well, it is no answer to a suggestion that there is discrimination by omission on a charitable purpose list of descriptions. That is to say, 'Well, everyone is equal on public benefit'. If everyone is equal on public benefit, there is no discrimination at all. The discrimination inheres in the omission of a word that is acceptable everywhere else except in charity law. That is a prima facie case that has not been answered. The noble Lord wishes to intervene.

Lord Phillips of Sudbury

I am grateful to the noble Lord for giving way. The point surely is that which was made by the noble Lord, Lord Bassam-either you have the list that we have-which is 12 items long-or you go for a long list because there are lots of headings, of which he has mentioned one, that are not

there expressly but are there by analogy. That is the important point; that they are there, whether expressly or by analogy, and you certainly are there by analogy.

Lord Wedderburn of Charlton

I do not want a longer list; I have not asked for a longer list. I am asking for a level playing field-I almost said a level praying field. It is a fact that discrimination can be committed by omission; there are hundreds of examples. It is also a fact, if I may just address the point-I am sure the noble Lord, Lord Phillips, will agree-that Mr Justice Vaisey did find an analogy with education in the case of the South Place Ethical Society, as well as the other phrases that he used about moral improvement, which was analogous to the advancement of education. I do not have the judgment with me. If you have a fund or association which is explicitly not analogous to the list, then an extra barrier has been raised against you from a religious fund or association, because religion is expressly there and you are not. You have to rely on something extra, and that is an extra buffer which amounts to a discriminatory test.

I almost feel invited to go to the authorities that we discussed in Grand Committee on the earlier Bill, but I will not do so. However, that proposition is the kernel of the case. We will have to look carefully at what the noble Lord, Lord Bassam of Brighton, said to see whether the matter is closed. I have seen copies of the correspondence about Jainism and so on. I understand the point that is being made, but it is being made to the Government, not to my amendment. I beg leave to withdraw the amendment.

Amendment, by leave, withdrawn.

Baroness Turner of Camden moved Amendment No. 3

> Page 2, line 10, at end insert 'or other systems or philosophies of belief or ethics which are not included in subsection (3) (a)'

The noble Baroness said: My Lords, I support the amendments being made in this Bill to rationalise the law on charities and to define specific categories of charitable purpose to be covered by it. I have listened carefully to the preceding argument and, as we know, among the purposes listed is the 'advancement of religion'. Frankly, I still want to put this amendment before the Committee because it seems to me that, once again in this Bill, religions are sorted out as presumably deserving while non-religious bodies are not.

Here I must state my own interests. I am a vice-president of the Humanist Association and an honorary associate of the National Secular Society, formed as long ago as 1866 by Charles Bradlaugh MP-a well-known free thinker of his time. Most secularists adhere to a system of ethical beliefs. We believe that this life is the only one of which we have any knowledge and that human effort should be directed to improving it for humankind. We believe that morality is social in origin and application. Secularism aims at promoting the happiness and well-being of our fellow citizens. We also believe in the abolition of special privileges granted to religious organisations.

We accept that there may be some difficulty in arriving at a suitable form of wording. That is apparent from the discussion we have had this afternoon. It is difficult to define precisely what is meant by 'religion', and we have sought to come to terms with that argument. Our amendment seeks to spell out that,

> 'other systems or philosophies of belief or ethics which are not included in subsection (3)(a)',

should be covered by this section. Subsection (3)(a), as we have heard, says that,

> '"religion" includes-

(i) a religion which involves belief in more than one god, and
(ii) a religion which does involve belief in a god'.

This attempts to define secularism in a more precise way.

In our amendment, we have sought to come to terms with the argument that we could be opening the door to frivolous or unworthy beliefs. Our concern is that without some amendment to the list of charitable purposes set out in Clause 2, we shall once again be in the position where theistic religions have a respected and acknowledged place in the scheme of things, but secularists and humanists do not.

Nor is it acceptable in my view to refer to previous case law as an indication that the secularist case is covered. In some of the cases already quoted in the debate this afternoon, the circumstances were entirely different-a different environment, and different circumstances existed, circumstances in which religion was differently considered and always held to have an educational purpose. This is a new Charities Bill, and the position of secular organisations such as the NSS should be respected and acknowledged. I beg to move.

Lord Bassam of Brighton

We covered the ground introduced through the amendment thoroughly in the previous debate. Those arguments hold good for this amendment, as they did for the earlier one. I do not accept that secularism, as opposed to theistic beliefs, has second-class status in terms of this piece of legislation. We see them very much on an equal footing. I argued that case earlier and was supported very ably, as ever, by the noble Lord, Lord Phillips. In some respects, the Bill is ground-breaking and helps to create the level playing field.

On a personal level, I obviously have some sympathy with what the noble Baroness has to say. Clearly we do not want any form of discrimination in the way in which beliefs or non-beliefs are treated, but we have to ensure that we properly protect the charitable legal structure from applications by the frivolous and the bizarre. I am sure that she fully supports that; she made reference to it. The way in which we have organised and framed the legislation fully covers what she is arguing for.

Lord Wedderburn of Charlton

A question was raised in the previous debate that is touched on in this one. I support my noble friend Lady Turner on clarity in the Bill. However, when the old Bill was with us, my noble friend on the Front Bench offered a definition of religion, as I said in my speech. Is he not now offering the same definition in view of the new features of the new Bill?

Lord Bassam of Brighton

That is right; I offered a definition of religion, which holds good for this Bill as well.

Baroness Turner of Camden

I thank my noble friend for that explanation. As he rightly says, the ground was covered substantially in the previous debate. Of course, we will look carefully at what he has to say when it appears in Hansard but, in the meantime, I beg leave to withdraw the amendment.

Amendment, by leave, withdrawn.

What is seen here is that there was a reluctance to accept non-religious beliefs as being charitable. Accordingly, it is questionable whether the law will accept a spiritual principle as being sufficient for the purposes of s.3(1)(c). It is likely therefore that the law in this respect will continue to follow the pre-2006 precedents where there is a need for the

belief system to be religious. As Dillon J explains in *Barralet v Attorney General*,[49] beliefs that do not have their foundation in a belief in God cannot be regarded as religious beliefs:

> In a free country, and I have no reason to suppose that this country is less free than the United States, it is natural that the court should desire not to discriminate between beliefs deeply and sincerely held, whether they are beliefs in a god or in the excellence of man or in ethical principles or in Platonism or some other scheme of philosophy. But I do not see that that warrants extending the meaning of the word 'religion' so as to embrace all other beliefs and philosophies. Religion, as I see it, is concerned with man's relations with God, and ethics are concerned with man's relations with man. The two are not the same, and are not made the same by sincere inquiry into the question, what is God. If reason leads people not to accept Christianity or any known religion, but they do believe in the excellence of qualities such as truth, beauty and love, or believe in the Platonic concept of the ideal, their beliefs may be to them the equivalent of a religion, but viewed objectively they are not religion.

While it is accepted that the supreme being does not have to be a deity, it remains to be seen what the effect of the Charity Commission's guidance will be on expanding what is included under the umbrella of religion. The fact that a spiritual principle will suffice may lead to a broader range of trusts being accepted as religious for the purposes of the law of charities. On the other hand, the courts may prefer to adhere more strictly to earlier precedents and search for a belief in some form of supreme being.

In all probability, the future direction of the law will depend on the cases that come before the courts. It must be borne in mind that the law is contingent upon the cases that are brought before it. Therefore if the claim is brought by an organisation whose spiritual principles are regarded as being in accordance with public morality of what is 'good' then it is possible that the courts will accept that a spiritual principle is consistent with religion, with the result that, as a consequence, there will be greater scope for the term religion to include ethical as well as purely religious forms of belief. On the other hand, if the spiritual principle is one that is not regarded as acceptable to public morality, then it may be the case that the courts will place a greater emphasis on the need for a belief in some form of supreme being, thus curtailing the apparent expansion of the term religion that the Charity Commission envisages in its interpretation of the Charities Act 2011.

Activities that advance religion

Activities relating to the dissemination and teaching of religious doctrine may be one example of a valid means of fulfilling this charitable purpose. Saying masses has been held to be a valid charitable purpose[50] as has the distribution of Bibles,[51] running Sunday Schools[52] and in the case of *Trustees of the City of Belfast Young Men's Christian Association v Commissioner of Valuation for Northern Ireland*,[53] recreational activities which tended to promote 'bodily health, fitness, endurance and self-discipline' could also be regarded as being for the advancement of religion.[54]

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[49] [1980] 3 All ER 918 per Dillon J at p.924.
[50] *In Re Heatherington* [1990] Ch 1.
[51] *A-G v Stepney* (1804) 10 Ves 22.
[52] *R v Special Commissioners of Income Tax ex parte Essex Hall* [1911] 2 KB 434.
[53] [1969] NI 3.
[54] *Trustees of the Young Men's Christian Association of the City of Belfast v Commissioners of Valuation of Northern Ireland* [1969] NI 3.

A number of trusts whose objectives have been the maintenance of members of the clergy[55] or the maintenance of religious buildings[56] have been regarded as being charitable. Thus it is seen that as with other types of charitable purpose, a broad gamut of activities will be regarded as being for the advancement of religion, and it will be a matter for the organisation that is attempting to acquire charitable status to convince the Charity Commission or the court that the purpose being advanced is religious, and that the activities being undertaken have the effect of advancing the religious doctrines, teachings or beliefs.

Public benefit

As with other forms of trust, there is a need to demonstrate a public benefit. In the context of religion, this might mean that activities such as religious celebrations or public masses may be recognised as being charitable, but trusts for the benefit of closed orders will not confer a public benefit. In the case of *Gilmour v Coats*,[57] where the trust purported to confer a benefit on an order of cloistered nuns, Lord Simonds explains why there is a need to demonstrate a public benefit, and makes it clear that it is not the presence of a system of belief that is of primary importance, but rather the sense that the trust confers a benefit on the public:

> It is, no doubt, true that the advancement of religion is, generally speaking, one of the heads of charity. But it does not follow from this that the court must accept as proved whatever a particular church believes. The faithful must embrace their faith believing where they cannot prove: the court can act only on proof. A gift to two or ten or a hundred cloistered nuns in the belief that their prayers will benefit the world at large does not from that belief alone derive validity any more than does the belief of any other donor for any other purpose.[58]

Accordingly, while trusts for the dissemination of religious doctrine,[59] or for the distribution of religious books will be charitable,[60] as will trusts for the repair and maintenance of religious buildings and burial grounds[61] because there is a sense that the public will benefit from such activities, a trust for the members of a particular synagogue is not a trust for the benefit of the public[62] because as with *Oppenheim v Tobacco Securities*[63] the beneficiaries would be defined in this instance by some personal nexus.

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[55] *Dundee Magistrates v Dundee Presbytery* (1861) 4 Macq 228, *A-G v Parker* (1747) 1 Ves Sen 43.
[56] *Re Robertson, Colin v Chamberlin* [1930] 2 Ch 71, *Re King, Kerr v Bradley* [1923] 1 Ch 243.
[57] [1949] AC 426.
[58] Per Lord Simmonds at p.446.
[59] *Re Barnes, Simpson v Barnes* [1930] 2 Ch 80.
[60] *Thornton v Howe* (1862) 31 Beav 14.
[61] *Re Strickland's Will Trusts, National Guarantee and Suretyship Association Ltd v Maidment* [1936] 3 All ER 1027.
[62] *Neville Estates v Madden* [1962] Ch 832.
[63] [1951] AC 297.

EXTRACT

Neville Estates and Others v Madden and Others [1962] Ch 832 at pp.851–855

Case facts

The primary issue in this case was whether the Charity Commissioners' consent was needed in order to effect the sale of a plot of land by the trustees of the Catford Synagogue. If the trust was a private trust, then the Charity Commissioners' consent would not be required.

Cross J

If, as I have held, this £3,250 and the land bought with it was held by the trustees for the purposes of this synagogue, then the plaintiffs contend that the trust is not a charitable trust on two grounds. First, because the objects of the synagogue are not wholly religious. Secondly, because if the objects are wholly religious, a trust for the benefit of an unincorporated association of this sort is not a charitable trust but a private trust for the benefit of the members from time to time.

The chief purposes which a synagogue exists to achieve are the holding of religious services and the giving of religious instruction to the younger members of the congregation. But just as today church activity overflows from the church itself to the parochial hall, with its whist drives, dances and bazaars, so many synagogues today organise social activities among the members. A new clause added to the scheme of the United Synagogue in October, 1926, authorised, or purported to authorise, that body to establish, inter alia, halls for religious and social purposes, and the Catford Synagogue, as I have said, has erected a communal hall near the synagogue building in which social functions are held. The plaintiffs, fastening on these facts and on the wording of clause 2 of the trust deed, argue that the trust in this case is open to the objections which proved fatal to the trust for the foundation of a community centre which came before the court in *Inland Revenue Commissioners v. Baddeley* [[1955] AC 572]. But in my judgment there is a great difference between that case and this. Here the social activities are merely ancillary to the strictly religious activities. In the *Baddeley* case, on the other hand, no one sought to argue – indeed it was manifestly impossible to argue – that the trust was for the advancement of religion. No doubt it had a religious flavour in that the beneficiaries were confined to Methodists or persons likely to become Methodists, and the premises and the activities in which the beneficiaries were to engage were to be under the control of the leaders of a Methodist mission. Nevertheless the activities in themselves were directed predominantly to the social and not to the religious well-being of the beneficiaries.

In my judgment the purposes of the trust with which I am concerned are religious purposes – the social aspect is merely ancillary.

I turn now to the argument that this is a private, not a public trust. In an article which he contributed in 1946 to volume 62 of the *Law Quarterly Review*, Professor Newark argued that the courts ought not to concern themselves with the question whether or not a trust for a religious purpose confers a public benefit. Even assuming that such questions can be answered at all, judges, he said, are generally ill-equipped to answer them and their endeavours to do so are apt to cause distress to the faithful and amusement to the cynical. I confess that I have considerable sympathy with Professor Newark's views; but the decision of the House of Lords in *Gilmour v. Coats* [[1949] AC 426] has made it clear that a trust for a religious purpose must be shown to have some element of public benefit in order to qualify as a charitable trust. In that case it was held that a trust to apply the income of a fund for all or any of the purposes of a

community of Roman Catholic nuns living in seclusion and spending their lives in prayer, contemplation and penance, was not charitable because it could not be shown that it conferred any benefit on the public or on any section of the public. The trust with which I am concerned resembles that in *Gilmour v. Coats* in this, that the persons immediately benefited by it are not a section of the public but the members of a private body. All persons of the Jewish faith living in or about Catford might well constitute a section of the public, but the members for the time being of the Catford Synagogue are no more a section of the public than the members for the time being of a Carmelite Priory. The two cases, however, differ from one another in that the members of the Catford Synagogue spend their lives in the world, whereas the members of a Carmelite Priory live secluded from the world. If once one refuses to pay any regard – as the courts refused to pay any regard – to the influence which these nuns living in seclusion might have on the outside world, then it must follow that no public benefit is involved in a trust to support a Carmelite Priory. As Lord Greene said in the Court of Appeal: 'Having regard to the way in which the lives of the members are spent, the benefit is a purely private one.' But the court is, I think, entitled to assume that some benefit accrues to the public from the attendance at places of worship of persons who live in this world and mix with their fellow citizens. As between different religions the law stands neutral, but it assumes that any religion is at least likely to be better than none.

But then it is said – and it is this part of the argument that has caused me the greatest difficulty: 'But this is a case of self-help.' Suppose that a body of persons, being dissatisfied with the facilities for the education of small children provided in their district, form an association for the education of the children of members. A committee is formed; each member pays a subscription; the funds of the society are employed in hiring premises and paying a teacher; and the rules provide that the association cannot be dissolved by the members at any given moment but is to continue for the benefit of the members existing from time to time. No doubt the public benefits by the fact that the children of the members receive an education. But could it possibly be argued that the association was a charity and was entitled to the great fiscal advantages which a charity enjoys? Or would it make any difference if the committee allowed the children of non-members to attend the classes free of charge if there was room for them, in the same way as members of the public, though having no right to enter the synagogue, are not in practice refused admission?

I feel the force of this analogy; but, as Lord Simonds pointed out in *Gilmour v. Coats*, it is dangerous to reason by analogy from one head of charity to another. After the passing of the Toleration Acts, dissenting chapels sprang up all over the country. As can be deduced from the language of section 1 of the Trustees Appointment Act, 1850 (see Sir Morton Peto's Act), the chapel was normally vested in trustees for the particular congregation or society of dissenters in question. In course of time disputes sometimes arose between rival groups, some members alleging that others had ceased to hold the tenets laid down in the trust deed and were not entitled to its benefits. A typical example of such a dispute is to be found in *Attorney-General v. Bunce No one* [(1868) LR 6 Eq 563], so far as I know, ever questioned that trusts for such dissenting bodies were charitable trusts provided that the members for the time being could not put an end to them. What the position would be if the members for the time being could divide the property among themselves was expressly left open by Sir George Jessel M.R. in *Bunting v. Sargent* [(1879) 13 Ch D 330].

Section 4 of the Religious Disabilities Act, 1846, provided that Her Majesty's subjects professing the Jewish religion in respect of their schools, places of religious worship, education and charitable purposes and the property held therewith, should be subject to the same laws as Her Majesty's Protestant subjects dissenting from the Church of England were subject to and not further or otherwise. From that time it has, I think, always been assumed by lawyers that trusts for the benefit of a congregation of Jews attending a synagogue were charitable trusts.

It is, for example, obvious that Parliament and the Charity Commissioners assumed in 1870 that the four synagogues which became the constituent synagogues of the United Synagogue were charitable bodies. Yet it is equally clear from clause 6a of this scheme that the constituent synagogues have not been open to all persons of the Jewish faith, but were unincorporated associations with a list of members.

Generally speaking, no doubt, an association which is supported by its members for the purposes of providing benefits for themselves will not be a charity. But I do not think that this principle can apply with full force in the case of trusts for religious purposes. As Lord Simonds pointed out, the law of charity has been built up not logically but empirically, and there is a political background peculiar to religious trusts which may well have influenced the development of the law with regard to them.

Outcome

The trust was charitable.

(d) The advancement of health or the saving of lives

Charitable purpose

At the time of writing there have been no cases where discussion has taken place as to precisely what types of activities will be valid as charitable trusts under this heading. A trust will be charitable if it advances health or the saving of lives. Trusts under this section may exist in order to provide for the care or treatment of those who are sick, but may also serve to provide facilities for those who suffer from illness or disability, or those who are convalescing.[64] Prior to the Charities Act 2006, such trusts would have had to be either for the relief of poverty or for other purposes beneficial to the community. In *Income Tax Special Purposes Commissioners v Pemsel*[65] for example, Lord Macnaghten gives the example of funding a lifeboat as an illustration of a purpose other than the relief of poverty, or the advancement of education or religion that would be beneficial to the community.[66]

The advancement of health may also include safeguarding public health. An example of this type of trust is the case of *Scottish Burial Reform and Cremation Society v Glasgow City Corporation*.[67] This case concerned a not for profit organisation that aimed to provide affordable cremations and burials. Although it might be expected that a trust of this nature might seek charitable status on a religious basis (such as cemeteries and burial rites are religious in character), the organisation had no religious agenda, although it provided the means for religious observance for those who desired it. However, its charitable status was justified on the basis that the hygienic disposal of dead bodies provided a benefit to public health.

Research into medical treatment may also fall under this heading, although such trusts would also be regarded as fulfilling the educational purpose of charity discussed above. As Lord Morton explains in relation to the Royal College of Surgeons:

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[64] *Re Isabel Joanna James, Grenfell v Hamilton* [1932] Ch 25, for example, concerned a trust to provide a Home of Rest for Sisters of the Community, while *In Re Estlin* (1903) 72 LJ Ch 687 sought to provide a similar establishment for lady teachers. Both were held to be charitable trusts.

[65] [1891] AC 531.

[66] Page 584.

[67] [1967] 3 All ER 215.

> The object just stated may be regarded as being directed to the relief of human suffering or to the advancement of education or science or to all of these ends.[68]

The funding of emergency and rescue services would also fulfil the charitable purpose of this head of charity, as is shown by the case of *Re Wokingham Fire Brigade Trusts*,[69] where it was held that the fire brigade's funds could be regarded as being charitable. As with other forms of charitable trust, a broad range of activities may potentially be included, and again it will be a matter for the organisation to formulate a convincing argument as to why its activities fulfil the charitable purpose. Examples of organisations that have been registered as charities include the charitable funds of Local Health Boards and Health and Social Care Partnerships (for example the Bedfordshire and Luton Mental Health and Social Care Partnership Trust Charitable Fund) as well as educational bodies such as Education for Health.

Public benefit

As with the more general requirement of charity, there must be a public benefit. Accordingly, consideration will be given, as with the other heads of charity, as to whether or not the purported charity does advance health or the saving of lives, and also to whether the objectives are sufficiently apolitical. As with the other types of charity, it is necessary to demonstrate that a sufficient section of the public derives a benefit, and that the beneficiaries are not identified by a personal nexus to the donor or some other person or entity.

(e) The advancement of citizenship or community development

Charitable purposes

It is likely that charities falling within this head would have been included under the heading of other purposes beneficial to the community prior to the enactment of the Charities Act 2011. Accordingly, to date there has been no specific case law where consideration has been given to the types of activities that would be accepted under this heading, with the exception of the Boy Scouts and the Girl Guides where it was held by Vaisey J in *Re Webber*[70] that it is 'well settled and well understood that the objects of the organisation of boy scouts were educational, and none the less educational by reason of the fact that the education is, no doubt, of a very special kind.' However, the Charity Commission has issued guidelines providing examples of further types of activities that might be included under this heading.

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[68] *Royal College of Surgeons of England v National Provincial Bank and Others* [1952] AC 631 per Lord Morton at p.654.

[69] *Re Wokingham Fire Brigade Trusts, Martin and others v Hawkins and others* [1951] 1 All ER 454.

[70] *Re Webber (deceased) Barclays Bank Ltd v Webber and Others* [1954] 3 All ER 712 at 713.

EXTRACT

Commentary on the Description of Purposes in the Charities Act 2011

This section brings together our guidance, reports, key decisions and other resources that could help trustees understand the scope of 'the promotion of the efficiency of the armed forces of the Crown, or of the efficiency of the police, fire and rescue services or ambulance services'.

What is meant by 'the promotion of the efficiency of the armed forces of the Crown, or of the efficiency of the police, fire and rescue services or ambulance services'?

1. The armed forces exist for public defence and security. It is charitable to promote the efficiency of the armed forces of the Crown as a means of defending the country. That includes ensuring that those forces are properly trained and equipped during times of conflict. It also includes providing facilities and benefits for the armed forces. Similarly it is also charitable to promote the efficiency of the police, fire, rescue or ambulance services as they exist for the prevention and detection of crime, the preservation of public order and to protect the public. ('Fire and rescue services' means services provided by fire and rescue authorities under Part 2 of the Fire and Rescue Services Act 2004 (C.21).)
2. Examples of the sorts of charities and charitable purposes falling within this description include:
   - increasing technical knowledge of members of the services through the provision of educational resources, competitions and prizes;
   - increasing physical fitness of members of the services through the provision of sporting facilities, equipment and sporting competitions;
   - providing opportunities for service personnel to gain additional experience relevant to their jobs (e.g. aeroplane clubs for RAF personnel);
   - supporting messes (NCOs and Officers) and institutes (other ranks), including the provision of chattels (items of plate etc);
   - providing and maintaining band instruments and equipment;
   - promoting and strengthening bonds between allied units;
   - providing memorials to commemorate the fallen or victories;
   - maintaining chapels (e.g. regimental chapels in cathedrals) or churches;
   - researching the military history of a regiment or other unit, and publishing books about it;
   - maintaining a museum or other collection for the preservation of artefacts connected with a military unit or service and supporting military and service museums generally;
   - encouraging esprit de corps (loyalty of a member to the unit to which he or she belongs and recognition of the honour of the unit);
   - providing associations which support a unit and enable serving and former members to mix together;
   - providing facilities for military training (e.g. drill halls);
   - encouraging recruitment to the services (e.g. through exhibitions, air displays etc);
   - provision of an emergency air or sea rescue service and equipment.

Source: http://www.charitycommission.gov.uk/Charity_requirements_guidance/Charity_essentials/Public_benefit/charitable_purposes.aspx. Site accessed 16 January 2014.

Public benefit

Determining whether the trust confers a public benefit will need to have regard to the issues considered above, namely:

- Does the trust confer a public benefit?
- Does the trust benefit a sufficiently large section of the public that is not defined by a personal connection to an individual or organisation?
- Does the trust satisfy the restrictions on discrimination or, where a trust is discriminatory, can the trust be modified so that the discriminatory element is removed?

As with educational trusts, a particular concern will be to ensure that the trust is not political in character, and that it does not discriminate without justification.

(f) The advancement of the arts, culture, heritage or science

If one visits a museum or a heritage tourist attraction, it is likely that the visitor will be offered the opportunity to register their visit for the purposes of Gift Aid. The reason for this is because the attraction is a charity, and the charitable purpose that it fulfils under the Charities Act 2011 will primarily be the advancement of arts, culture, heritage or science. However, many of the activities that will now fall under this head of charity are likely to have been regarded as charities for the purposes of education prior to the enactment of the Charities Act 2006, and indeed charities now falling under the head of the advancement of the arts, culture, heritage or science may continue to have an educational objective. Accordingly, libraries and museums may be charitable under this head of charity, as will heritage attractions and organisations such as the National Trust. A number of pre-2006 cases have considered the charitable status of arts- and sciences-focused activities and thus 'the promotion of industry commerce and art',[71] 'presenting works of high class and gradually training people to like them in preference to works of an inferior class',[72] music,[73] drama,[74] languages,[75] archaeology,[76] and preserving historic buildings and artefacts[77] are all examples of the types of activities that will be regarded as being charitable.

However, trusts whose objective is the promotion of arts, culture, heritage or science, along with trusts for the purposes of undertaking or disseminating research, may also be included within this head of charity. Nevertheless, it is possible to argue that the advancement of the arts, culture, heritage or science may include a broader range of activities than would have been the case prior to the Charities Act 2006. In the case of *Re Shaw* for example, Harman J declined to accept that the increase of knowledge could be charitable unless it were provided within the context of some form of teaching or education.[78]

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[71] *Crystal Palace Trustees v Minister of Town And Country Planning* [1951] Ch 132.

[72] *Royal Choral Society v Commissioners of Inland Revenue* [1943] 2 All ER 101 per Lord Greene MR at p.105.

[73] *IRC v Glasgow Musical Festival Association* 1926 SC 920.

[74] *Re Shakespeare Memorial Trust, Earl of Lytton v A-G* [1923] 2 Ch 398.

[75] *A-G v Flood* (1816) Hayes & Jo App xxi at xxxviii.

[76] *Re British School of Egyptian Archaeology, Murray v Public Trustee* [1954] 1 All ER 887.

[77] *Re Cranstoun, National Provincial Bank Ltd v Royal Society for the Encouragement of Arts, Manufactures and Commerce* [1932] 1 Ch 537.

[78] *Re Shaw, Public Trustee v Day and Others* [1957] 1 All ER 745 at 752: 'In my opinion, if the object be merely the increase of knowledge, that is not in itself a charitable object unless it be combined with teaching or education.'

However, the expansion in the range of charitable purposes may mean that a charity may advance the arts, culture, heritage or science without necessarily fulfilling an educative function.

Public benefit

The issues considered earlier (in Chapter 19) will again be relevant here, and as with educational trusts one of the main issues for the court to consider will be the issue of whether the artistic activity being proposed does in fact confer a benefit on the public. The authority of *Re Pinion*[79] is probably as relevant to trusts for the promotion of the arts as to the advancement of education, with the result that works that have no artistic merit will not fulfil the public benefit element of this charitable purpose. It will be the case that the organisation seeking to convince the Charity Commission or the court of the artistic merits of its endeavours will have to adduce evidence of its value.

(g) The advancement of amateur sport

Prior to the enactment of the Charities Act 2006, the advancement of amateur sport was particularly problematic. Sport within the context of formal education was accepted as being charitable,[80] but where an educational context could not be shown, the courts had declined to recognise amateur sport as being a charitable purpose[81] largely on the basis that the cases that had come before the courts had concerned situations where the primary beneficiaries were defined by their personal connection to a sports club.[82]

However, the Charities Act 2006 sought to correct this anomaly, and now activities that promote amateur sport and trusts that purport to benefit amateur sport will be charitable. According to the Charity Commission, the emphasis is on 'healthy recreation'[83] and accordingly, it does not consider that activities such as angling, ballooning, parachuting or billiards, snooker and pool[84] could be recognised as charities, although it does not exclude the possibility that organisations involved with these activities could convince the Commission that this view is incorrect.

Public benefit

Determining whether the trust confers a public benefit will need to have regard to the issues considered above, namely a benefit to a sufficiently large section of the public in a way that is neither discriminatory nor defined by a connection to an individual or organisation.

Specific issues to consider in the context of trusts for the advancement of amateur sports is that violent or dangerous sports where the risk of injury is significant will not be regarded as conferring any public benefit, unless there is evidence to show that appropriate steps have been taken in order to minimise the risk of serious injury. The second requirement is that membership must be open to all members of the community that is

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[79] *Re Pinion, Westminster Bank v Pinion and another* [1964] 1 All ER 890.
[80] *Inland Revenue Commissioners v McMullen* [1981] AC 1.
[81] *In Re Nottage Jones v Palmer* [1895] 2 Ch 649.
[82] *Inland Revenue Commissioners v Baddeley and Others* [1955] AC 572.
[83] Charity Commission (2009) Charitable Status and Sport. Paragraph 1 http://www.charity-commission.gov.uk/Publications/rr11.aspx. Site accessed 16 January 2014.
[84] Ibid.

served by the organisation. Accordingly, the objective of the charity must be community participation rather than competition, and participation must be accessible in terms of affordability and the level of skill required. Accordingly, while restricting the number of participants for reasons of efficiency and safety will be acceptable, restricting participation on the basis of an absence of talent or skill will not be justifiable if the trust is to have charitable status. Accordingly, an organisation may legitimately limit the number of participants, and establish a waiting list for those who are unable to join at a given time. However, it will not be permissible for the organisation to limit membership to those who are eligible to be in a competitive team.

EXTRACT

Charity Commission (2009) RR11 Charitable Status and Sport paragraphs 14–35

Open membership

14. Open membership is essential if a club is to meet the requirement of public benefit that applies to all charities. A club that operates restrictions in its membership provisions (other than reasonable restrictions that are necessary to enable the club to operate effectively – see paragraphs 15–17 below) could not claim to be encouraging community participation.

Legitimate restrictions on membership

15. As far as is reasonably practical, a CASC will need to provide facilities for all who wish to play. That said, there are some circumstances in which certain restrictions on membership are reasonable and justified.
16. We accept that the facilities of some clubs are quite limited and that it is not always possible to accommodate everyone who wishes to become a member, on practical or health and safety grounds for example. In those circumstances, it is perfectly reasonable for a club to establish a waiting list for membership where they are oversubscribed, provided that the next available membership is offered to the person at the top of the waiting list (on a first come, first served basis) and not offered to someone lower down the list on the basis that they are a better player.
17. It is also reasonable for the constitution of a CASC to include provisions relating to the refusal or rescinding of membership. This is a standard provision in many charitable constitutions and allows the refusal or rescinding of membership for a good reason. The reason usually has to be properly explained to the individual, and the individual has the right to be heard, accompanied by a friend if necessary, before a final decision is made. Reasons for refusal of membership of a CASC might include, for example, an individual's physical or medical condition, or his or her failure to satisfy the CASC's child protection policy. (We expect all clubs providing facilities for children to have a policy that ensures that people who ought not to be allowed to come into contact with children are not given the opportunity to do so.)

What constitutes 'community participation'?

18. For membership to be open, membership subscriptions must be affordable for the majority of the community the club serves. Clubs that are able to offer discounted membership rates for people on low incomes or who are unemployed, for example, will find it easier to demonstrate that they are genuinely concerned with encouraging community

participation. However, we realise that not all clubs will be in a position to do this (especially smaller clubs) and we would not expect clubs to offer discounted membership where this clearly would not be financially viable for them. However, those clubs would need to keep this possibility under review in the event that their fortunes improve.

19. There must be no test of skill for admission to the club (although we accept that, once enrolled as members, participants will often be organised into team and competitive structures based on ability – see paragraphs 27–28 below). Where resources are insufficient to enable everyone to play, a CASC will be expected to maximise participation and hence it will not be able to focus its resources purely on the basis of ability to the detriment of less proficient members of the club.
20. 'Community participation' relates to 'the community' in its widest sense. Membership of the CASC will need to be available to all members of the public who wish to join. A CASC's constitution may or may not define the geographical area whose residents will be eligible to join. Where a geographical area is defined it must not be too narrowly drawn. It might be defined as the inhabitants of a particular town or village, for example, but a geographical area of just a few named streets is likely to be too restrictive. If the CASC doesn't limit its potential membership to the inhabitants of a particular area, anyone will be able to join, regardless of where they live (subject to any legitimate restrictions as discussed above). A CASC will not be able to give a preference for local people unless its constitution enables it to do so.

Participation by disabled or elderly people

21. Community participation entails that the club's facilities should be genuinely available to the public at large. However, it is not necessary that the sport in question should be one that all sections of the community are able to undertake. In order to be a charity, a CASC will not be required to provide facilities for elderly people or for people with a disability. That said, there should be no bar to participation by elderly people or people with a disability where the sport is suitable and the CASC's facilities can reasonably be used by these groups.

Dangerous sports

22. It may be that some sports, by their very nature, are bound to appeal only to a very limited part of the community. In itself that may not be problematic. However, where a sport is inherently very dangerous, there may well be an issue about whether it is really conducive to physical health.
23. We recognise that there are risks involved in playing any sport but some sports, such as what are known as 'extreme' sports for example, involve risks which go far beyond the usual risks of injury associated with energetic physical exercise.
24. If a club concerned with a dangerous sport applies to register as a charity on the basis that it is encouraging the community to participate in healthy recreation, we would need to consider medical evidence of the risks involved in the sport and details of the steps taken to minimise the dangers to personal safety. For example, some people have raised concerns about the risks of brain injury associated with boxing when undertaken at a professional level. Before we could register an amateur boxing club as a charity, we would need to be satisfied that sufficient steps had been taken to reduce those risks to an absolute minimum.
25. Even though some dangerous sports may have difficulty in meeting the healthy recreation criteria, it may be that an organisation uses that sport as a means of achieving a quite different charitable purpose. In that sort of case, the benefit to the public of the organisation's object may outweigh the dangers inherent in the sport.

Affordability

26. Clothing and equipment will also need to be affordable. Some sports plainly require a considerable outlay. There may therefore be difficulties in accepting that some 'expensive' sports, such as polo, motor racing or ocean yachting, for example, are genuinely forms of recreation that are available to the community at large. However, clubs that are concerned with such sports may be able to meet the requirements for community participation if their activities are genuinely geared to maximising participation, perhaps by providing equipment and facilities or by subsidising the cost to participants of modest means.

Competition and team structures

27. The competitive element in sport is an intrinsic and essential part of its appeal to players, whatever their level of skill. CASCs will need, and have, a wide freedom to run competitive teams, and other arrangements, such as leagues and ladders, based on competition and structured according to ability. The most skilled and dedicated players may want to devote more time to training and playing than the less committed, and facilities may be allocated so as to reflect this and to allow competitive teams to play, and prepare for, internal and external fixtures. This is all entirely in keeping with charitable status, provided only that the club's arrangements remain consistent with its charitable purpose of promoting community participation. In other words, the extent to which facilities and resources are devoted to competitive play must not damage the principle of genuinely open membership.

28. In practical terms, this means that a club which devotes a lot of its facilities to competitive matches and to members of its competitive teams, while still offering others appropriate and broadly equivalent opportunities to play, can be charitable. A club would not be charitable if the priority given to competitive teams and players resulted, for members who did not choose to play competitively, in materially worse opportunities to participate. The same would be true if it was similarly clear for other reasons that competitive success, and not community participation, was the true purpose of the club.

Coaching

29. A charitable CASC may or may not provide coaching for participants. If it does so, the coaching needs to be available to players at all levels of skill, not just the best players. It is permissible for the club to give assistance to better players (for example, to enable them to compete in regional, national or international events) where doing so provides an incentive for participation by all, but such assistance must not be given at the expense of other participants. We are not suggesting that a CASC must offer coaching, or that every member must be given coaching. However, where coaching is provided, the CASC must cater for the needs of less experienced players as well as the needs of more competent players.

30. It would be acceptable for a CASC to pay for a member of the club to obtain a relevant coaching qualification if, in return for that investment, that individual is then able to provide coaching at the club. It would also be acceptable for a CASC to pay for the use of a professional coach to coach its best players if those players then passed on what they had learned to the less able players.

Playing and non-playing members

31. To be charitable, a CASC would need to be able to show that it existed for the benefit of the public rather than for the benefit of its members. A CASC will usually adopt a membership structure, but only as a convenient vehicle for making its benefits available to the public. Hence all members would have to be playing members, or non-playing volunteers and helpers (this might include, for example, individuals still wishing to be associated with the club but who are unable to play for reasons of health or old age).

We recognise that volunteers can be a very valuable asset for a club. However, all activities of the club would have to be directed towards healthy recreation and ancillary matters. If the club provided refreshment, for example, it could do so only as a purely ancillary activity connected to actual participation in the sport concerned.

'Social' members

32. The provision of facilities for use by members intending only to take advantage of the club's social facilities is not charitable, so the club's constitution could not include a 'social' membership category.
33. This does not mean, though, that a charitable CASC cannot include social facilities, such as a bar, on its premises. It simply means that activities of this nature must be operated by a separate non-charitable organisation, such as a social club, to be run on an arm's length basis from the charity. This is the same basis upon which village halls and community centres, for example, operate social activities on their premises. The arrangements do not have to be onerous, and the income generated by those activities can still be used to support the financial viability of the club. (See paragraph 37, 2nd bullet point, below.)

What would a charitable CASC look like?

34. The guidance set out above means that, overall, in a charitable CASC:
    - the sport in question can be shown to promote physical health and fitness;
    - the club is open to anyone who wants to join, regardless of ability;
    - any special clothing or equipment is, where possible, provided free, or at reduced rates, by the club or is affordable;
    - more and less skillful or competitive players are, as far as reasonably practicable, treated even-handedly for access to facilities and other purposes;
    - no payments or private benefits are given to players;
    - no separate and distinct benefits (for example, social facilities) are provided for non-playing members;
    - refreshment and social facilities are provided only where they are ancillary to participation in healthy recreation.

What sort of sports clubs could not be regarded as charitable?

35. Our decision to recognise the promotion of community participation in healthy recreation as a charitable purpose does not mean that all sports bodies can be charitable. Those bodies which have a restricted membership (other than for the reasons set out in paragraphs 15–17 above), perhaps for social reasons or because they are concerned with professional or elite sport, for example, or which are not capable of improving physical health and fitness, would not be able to take advantage of our decision.

Source: http://www.charity-commission.gov.uk/Publications/rr11.aspx. Site accessed 16 January 2014.

ACTIVITY

Read the Charity Commission's guidelines RR11 Charitable Status and Sport. Imagine that you represent an organisation for the playing of pool, billiards and snooker. What arguments might you propose in favour of granting charitable status to the organisation either for the advancement of amateur sport, or for some other charitable purpose?

(h) The advancement of human rights, conflict resolution or reconciliation or the promotion of religious or racial harmony or equality and diversity

Charitable purpose

The advancement of human rights, conflict resolution or reconciliation, or the promotion of religious or racial harmony or equality and diversity is in many ways the most complex area in terms of establishing a valid charitable purpose. As with the advancement of the arts, culture, heritage or science, there is considerable overlap with the advancement of education in terms of what will be acceptable. The difficulty with this head of charity however is that it must not be political in its objectives, and the wording of the trust's objectives must be drawn up very carefully if the trust is to avoid failing on the basis that its objectives are overly political in character. The Charity Commission has issued guidelines regarding the types of activity that will be acceptable, and this includes monitoring abuses of human rights, research and education involving human rights, commenting on proposed legislation and raising public awareness of human rights.

EXTRACT

Charity Commission Guidelines: RR12 The Promotion of Human Rights

3. There are many ways in which a charity might seek to promote human rights, including:

- monitoring abuses of human rights;
- obtaining redress for the victims of human rights abuse;
- relieving need among the victims of human rights abuse;
- research into human rights issues;
- educating the public about human rights;
- providing technical advice to government and others on human rights matters;
- contributing to the sound administration of human rights law;
- commenting on proposed human rights legislation;
- raising awareness of human rights issues;
- promoting public support for human rights;
- promoting respect for human rights by individuals and corporations;
- international advocacy of human rights;
- eliminating infringements of human rights . . .

Monitoring abuses of human rights

17. A charity concerned with promoting human rights may engage in monitoring and reporting breaches of a country's human rights obligations, whether those obligations arise under domestic legislation or international standards.

Obtaining redress for victims of human rights abuse

18. A human rights charity may bring pressure to bear in individual cases (including through the mobilisation of public opinion) to encourage a government to respect its own human

rights legislation. A charity may provide support for attempts to obtain redress through the courts of the country concerned, whether by way of specialist legal advice and representation or by less direct means. The availability of that option will, of course, depend upon whether or not the country's legal code enables the victims of human rights abuse to obtain redress. Even if the legal code of the country in which the abuse takes place does not expressly provide redress, it may still be possible to attempt to obtain compensation or a public inquiry or an acknowledgement of responsibility. A human rights charity may also support the investigation and prosecution before international tribunals of individuals and organisations accused of human rights abuse.

Relieving need among the victims of human rights abuse

19. It is charitable to relieve needy 'prisoners of conscience' or their dependants. Assistance can include financial, educational and rehabilitational help. We have registered as charities bodies concerned with relieving the suffering and distress of individuals who have suffered human rights abuses. We have also accepted that it is charitable to provide financial assistance to victims of torture who are in financial need to enable them to obtain compensation or redress.

Research into human rights issues

20. Human rights are an appropriate subject for research. The Court has held that promoting and commissioning research into the maintenance and observation of human rights is a subject of study which is capable of adding usefully to the store of human knowledge.

Educating the public about human rights

21. Human rights is an established subject of study in schools and colleges. A human rights charity may advance education in human rights through support for such studies or through less formal types of education.

Technical advice to governments and others on human rights matters

22. A human rights charity may provide technical advice to governments, NGOs and other relevant bodies on the creation, improvement and implementation of legal, regulatory and administrative systems for the not-for-profit sector in countries abroad. A charity with appropriately-worded objects may also provide technical advice to governments and to domestic and foreign public authorities on the adoption and implementation of human rights legislation, including training for administrators in the application of that legislation.

Contributing to the sound administration of human rights law

23. A wide range of activities revolves around contributing to the sound administration of human rights law. This includes providing the essential material for the study of a country's human rights law (such as reports of judicial decisions). It also includes acquiring and passing on knowledge about what the law is at any given time, how it is developing and how it is being administered and applied

Commenting on proposed human rights legislation

24. A charity for the promotion of human rights may participate in government consultations about changes in the law. It may also recommend improvements in human rights law and provide objective comment on the adequacy of legislation to implement human rights (whether or not it is invited by government to do so). A charity can campaign for particular changes in a country's laws provided that the campaign falls within the principles discussed in paragraphs 33 to 36 below.

Raising awareness of human rights issues

25. A charity may raise awareness of human rights issues by facilitating debate and discussion. However, a charity established to promote human rights does not need to limit itself to balanced, educational activities. It can promote awareness of human rights issues by distributing material which does not present both sides of the argument but simply promotes its own point of view.

Promoting popular support for human rights

26. Cultivation of particular opinions or sentiments among the public is charitable where the reason for doing so is to promote mental or moral improvement. It is on this basis that we have accepted as charitable 'the promotion of ethical standards of conduct'. And on this basis promoting popular support for human rights is charitable.

27. In the last century, in the United States, the promotion of a 'public sentiment that will put an end to Negro slavery' was held to be charitable. The Court took the view that the bequest would not have been charitable had it been directed towards political agitation and attempts to alter the law. In fact, however, the method specified in the gift was to apply pressure not to government, but to private individuals with a view to obtaining voluntary manumission. That purpose was charitable by analogy with a line of cases that showed that the peaceable redemption or manumission of slaves in any manner not prohibited by law was charitable.

28. In this country, the Court has accepted that the exercise of moral influence and the cultivation of public sentiment in ways which do not involve seeking to change the law or government policy can be legitimate means of pursuing recognised charitable objects.

Promoting respect for human rights by individuals and corporations

29. Although human rights are defined primarily by reference to the appropriate treatment of individuals by the State, the concept of human rights also has implications for the way that individuals treat each other. Discrimination on grounds of race or religion, for example, may be combated by legislation or by trying to influence the way in which individuals treat each other. There seems to be no reason therefore why an organisation set up to promote human rights should not encourage individuals to respect each other's human rights.

30. The absence of effective human rights legislation in a country can be exploited by individuals and corporations for their own economic advantage. It is open to a human rights charity to address this issue and to challenge such exploitation, for example by campaigning.

International advocacy of human rights

31. Promoting human rights includes advocating adoption of, and compliance with, international and regional codes of human rights, the incorporation of human rights into domestic law is a legitimate objective of a charity promoting human rights. Advocacy of this kind is conducted primarily in international fora and depends on well-researched material for its effectiveness. It extends also to contributing to international and State-sponsored conferences and seminars concerned with the adoption and implementation of human rights. A political campaign to press the government of a particular country to adopt particular human rights legislation (or particular policies) would be open to a charity provided that it fell within the principles discussed in paragraphs (33 to 36) below.

Eliminating infringements of human rights

32. A charity may seek to eliminate infringements of human rights. Some of the means that may be available for doing so have been mentioned in this guidance, such as monitoring

and raising awareness of abuse, obtaining redress, and promoting respect for human rights among individuals and corporations. We have accepted that it is charitable 'to procure the abolition of torture by all lawful means' and to procure the abolition of torture, extra-judicial killing and 'disappearance'. We have also registered as charities organisations concerned with the elimination of slavery, the slave trade and other forms of unlawful forced labour. Infringements of human rights of this kind are, almost by definition, contrary to the domestic law of the country in which they take place (particularly when considered in the context of its international treaty obligations) and hence trying to eliminate them will not generally involve trying to change domestic law. However, even where a country's domestic law is inconsistent with international standards, a charity may campaign for legislation or changes in government policy provided that it does so within the principles discussed below.

Source: http://www.charity-commission.gov.uk/Publications/rr12.aspx#2. Paragraph 3 and 17–32. Site accessed 16 January 2014.

Public benefit

As with the other types of charity, the question of whether there is a benefit to the public must be addressed in the context of trusts under this heading, and the political nature of this head of charity means that the trust must be very carefully drawn up so as to avoid political activity. As the Charity Commission's guidelines explain:

> An organisation which has purposes which include the promotion of human rights by seeking a change in the law, or a shift in government policy, or a reversal of a government decision has (at least in part) political purposes and cannot be a charity.[85]

It is recognised that a charity for the advancement of human rights, conflict resolution or reconciliation, or the promotion of religious or racial harmony or equality and diversity necessarily involves some measure of engagement with the political process, with the result that to require such organisations to behave in a manner that is entirely apolitical would defeat the entire *raison d'être* of the organisation. Therefore, it is accepted that where the political activity does not dominate the charity's work and where the proposed activities will further the objectives of the charity, there can be no objection to the charity operating in a manner that is political in character.

However, furthering the interests of a specific political party, or procuring changes in the law or government policy, will be regarded as overly political, and will not therefore provide a public benefit for this head of charity, as Slade J explains in the judgment at first instance in the case of *McGovern v Attorney General*:[86]

> I extract the principle that the court will not regard as charitable a trust of which a main object is to procure an alteration of the law of the United Kingdom for one or both of two reasons. First, the court will ordinarily have no sufficient means of judging, as a matter of evidence, whether the proposed change will or will not be for the public benefit. Second, even if the evidence suffices to enable it to form a prima facie opinion that a change in the law is desirable, it must still decide the case on the principle that the law is right as it stands, since to do otherwise would be to usurp the functions of the legislature.

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[85] Charity Commission RR12 The Promotion of Human Rights. http://www.charity-commission.gov.uk/Publications/rr12.aspx#2. Site accessed 16 January 2014. Paragraph 33.

[86] [1981] 3 All ER 493 at p.506.

As with the other types of charitable purpose, the requirement that the charity must benefit the public or a sufficient section of the public that is not defined by any personal nexus is equally applicable here, as is the requirement that the charity does not operate in a manner that is discriminatory.

EXTRACT

Dunn, A. (2006) 'To Foster or To Temper: Regulating the Political Activities of the Voluntary and Community Sector' 26 *Legal Studies* 507–11

The current regulation

Current regulation of the political activities of voluntary and community organisations draws a distinction between charitable and non-charitable bodies. A charity in England and Wales is one which falls within the legal category of charity outlined by Lord Macnaghten as an organisation constituted for the purpose of relieving poverty, advancing education, advancing religion or for another purpose beneficial to the community (to be expanded under the Charities Bill). Such an organisation must also be for the public benefit and be wholly and exclusively charitable. Organisations awarded charitable status will have the benefit of taxation concessions. Partly as a result of these concessions and in addition to the general law, charities face specific rules regulating the type of political activities that they can legitimately undertake.

These will be briefly considered below before turning to an examination of the general regulations to which all sector organisations are subject.

Special regulation of charities

Regulation restricting the ability of charities to embrace fully the political process developed in the early part of the twentieth century with a general rule against the pursuit of political purposes laid down in *National Anti-Vivisection Society v IRC* [[1948] AC 31]. A more comprehensive prohibition was set out by Slade J in *McGovern v Attorney-General* [[1982] Ch 321]. Under the McGovern rule, charities may not pursue political purposes. Slade J expounded that an organisation would be political, and therefore not charitable, if it sought to further the interests of a political party or cause; procure changes in the law, the reversal of government policy or the decisions of governmental authorities in this or another country.' This is not an exhaustive categorisation. Nor is it a reined-in definition of the term 'political', which in subsequent case-law has proved to be an amorphous concept, exhibiting broader characteristics than the McGovern categorisation envisaged.'

The arguments which have been advanced for the restriction on political objectives of charities have both jurisprudential and practical nuances. None of the arguments is wholly convincing, though each contains a kernel of reason. The judiciary, it is argued, must remain politically neutral and not become embroiled in questions of political partiality. Neither the judiciary nor the Charity Commission are able to assess whether the essential requirement of public benefit attaches to any given political activity, and so it is impossible to accord a political purpose charitable status. Moreover, it is argued that it is solely within the remit of the legislature to determine if law reform is necessary, advisable or achievable, and legislative functions should not be usurped by a court or the Charity Commissioners according legitimacy to a group campaigning for law reform.' Additionally, there is a policy argument that the regulation of charities should protect donors and taxpayers, who may not wish their donations or taxation subsidies to be used for political purposes or to support partisan political acts. Whilst the

cogency of the rules and the arguments surrounding them have been debated extensively, there was little enthusiasm to lift the restrictions in recent reform proposals. Indeed, whilst political engagement was lauded as a hallmark of the sector's independence, it was noted that donor confidence and sector efficiency were higher regulatory priorities. But on that point, if closer monitoring and scrutiny of organisations is robust, safeguards should already be in place to secure donor confidence and protect against unacceptable political activities or exploitation. Given that the European Code specifically seeks to ensure a comprehensive and coherent oversight of the sector and its activities, and given that charities are already subject to a registration requirement under the auspices of the Charity Commission, there is an argument for affording charities greater rather than less political leeway, precisely because a higher level of protection via regular scrutiny is in place.

The tightening up of restrictions upon charitable purposes does not extend to an outright proscription of their activities. Whilst charities may not pursue political purposes, they are permitted some margin of autonomy and may partake in political activities where such conduct is subsidiary to and in furtherance of the main charitable purpose of the organisation. As a lobbying organisation, for example, would not be awarded charitable status if its sole purpose was to restrict, by legislation, the sale of fireworks, but a charity with the purpose of the protection of animals may, as a supplementary activity, lobby to seek the same restrictions where a legitimate connection can be made between the lobbying and the furtherance of the organisation's purpose. The difference between the two organisations may well be illusory in consequence, but the crucial distinction is that the second has a purpose readily identifiable and legitimated as benefiting the public (the protection of animals) and that purpose does not require the judiciary or the Charity Commissioners to become involved in questions of the cogency of policy, politics or changing the law, as the first organisation would. Using political activities as a means to a deemed charitable end is acceptable. Political activity as an end itself is not. The Charity Commission provides guidance to organisations on the distinction between a purpose and an ancillary activity. Even though it has accepted that the line between proper contribution to political debate and improper politicking is sometimes difficult to draw. Following criticism, this guidance has been revised to be more constructive and less cautionary in tone. A distinction is drawn within the guidance between campaigning, which concerns raising awareness and is generally acceptable, and political campaigning, which goes further by seeking to influence policy or legal process. The latter is a permitted activity only if it remains ancillary, and that before embarking on the activity the charity's trustees have fully considered 'achievement of objects and reputation'. According to the Charity Commission, this includes consideration of such issues as the risk to the charity's good name, the effect upon the confidence of donors and stakeholders, whether the activity is the most appropriate means by which to further the charity's purpose and the extent of human and economic resources necessary to undertake the activity. As a matter of governance such considerations are important in administering any organisation, but these are not legal requirements. In this jurisdiction, there is no financial limit upon charities undertaking political activities. The revision of the Charity Commission guidelines is welcome. One difficulty with previous guidelines (though still evident above and to be borne in mind if implementing the European Code) was that they reined in the legal principles tightly, effectively creating a second layer of 'quasi-regulation' on top of the existing rules. This, coupled with the powers of the Charity Commissioners to restrain activity via an injunction, or to freeze bank accounts during an inquiry,' had the potential to be a significant restriction, particularly for poorly resourced charities. Charities 'without experienced and robust trustees, or charities working in areas on the political margins, such as human rights. In this context, it remains essential for any regulator to have a progressive interpretative approach. The emphasis upon minimising risks and maintaining organisational credibility fits neatly with the aims of the European Code, although the Charity Commission' interpretative approach stands in sharp distinction to the code's tone.

The Charity Commission already has monitoring and investigatory powers, which have been exercised quickly and effectively in recent years against charities that have contravened or have been suspected of contravening the political boundaries. But there is no overt scrutiny of individual activities, or a heavy-handed examination of projects and programmes of action. Unless there is to be a more overt regulatory shift, it is difficult to see how the European Code would positively add to the current regulation of charities in England and Wales. Indeed, the reverse would be the case.

Regulation of the broader voluntary and community sector

Organisations within the wider voluntary and community sector do not have sector-specific regulation regarding their political activities.' These organisations are covered by the general law pertaining to the forum in which they chose to campaign; for example broadcasting, electioneering or bringing an action for judicial review. Although there are advantages to a lack of specific regulation, such as flexibility and equality of circumstance, it can present both regulators and organisations with some difficulties. From a regulatory point of view, it does not provide for a systematic or coherent approach to ensuring that voluntary and community organisations do not undertake unacceptable political activities, carry out or fund terrorist activities or other serious crimes, or are exploited by other parties so to do. Neither does it allow for the credibility of the sector to be ostensibly maintained at a regulatory level, nor systematically ensure that the sector's legitimate organisations, their members and donors, and the wider public are safeguarded. Alternatively from the sector perspective, it puts organisations on the same footing as private individuals, not necessarily as distinct parties who can assist in the development and delivery of policy. It neither accords specific recognition to nor necessarily encourages the check-and-balance function the sector can perform. This approach may also be viewed as at variance with the broader more favourable treatment of the sector from the government, and could be seen to embed a 'pull-push' dynamic, with the voluntary and community sector often pulled in as service deliverers but pushed out as campaigners. The regulatory shift evident in the European Code emphasises greater monitoring of the whole voluntary and community sector, and is in distinction to the generalised rules that currently apply. Present regulations of the forums of activity are not particularly onerous, coming into play upon potential infringement rather than monitoring at the outset all organisational activities. Five key themes can be discerned from the current regulation: there is primary encouragement for organisations to exercise their right to take part in debate and raise political issues; however, the recognition of activities of organisations must be balanced with the rights or needs of other parties; and, in addition, general support will not be given to moving from raising debate to resolving political issues; in some circumstances extra protection to raise issues and avert regulatory restrictions may be afforded through Art 10 of the European Convention for the Protection of Human Rights and Fundamental Freedoms 1950 ('the European Convention'); and, finally, there remains an ambiguity in determining the construct of the term 'political'. This latter point has particular significance for applying the European Code, which seeks to monitor political conduct. Overall, it is to be noted that these five themes largely emphasise that, whilst current regulation places restrictions on political conduct, it retains a positive focus on the importance of political activities, rather than a negative approach to scrutiny and supervision of parties.

For example, it is open to voluntary and community organisations, as with other organisations or persons where they have a sufficient interest, to challenge government, public bodies or parliamentary authority via actions for judicial review. This is so, even where the views of such groups may be thought to be 'disturbing, even distasteful' by many within the community Many choose to exercise this right, and their ability to do so in the public interest is championed as an indicator of a strong democracy and as an example of how the sector is well placed to exercise their expertise at the sharp end of need.

EXTRACT

McCarthy, R. (2008) 'Charities and Campaigning' *Private Client Bulletin* 235

Trustees' duties

In order to engage in campaigning, charity trustees must be satisfied upon reasonable grounds that the activities will be an effective means of furthering the purposes of the charity and that they will do so to an extent justified by the resources. Trustees must first consider whether and to what extent campaigning activities are permitted under the charity's constitution. For example, charities established with objects to advance education are obliged to be more balanced in the material that they produce than charities with non-educational objects. Whilst it is not always necessary to present both sides of an argument, education is about expanding the mind and allowing those who are educated to make their own decisions; it is not about indoctrination. In *Hopkinson (deceased)* [[1949] 1 All ER 346], *Re* Vaisey J. held that 'political propaganda masquerading as education is not education within the Statement of Elizabeth. In other words it is not charitable'.

When considering campaigning activities, charity trustees must consider the balance between the benefits to the charity and its beneficiaries and the risk to the charity, especially in terms of reputation. In particular, charity trustees are under a duty to identify and review the major risks to which a charity is exposed and to put systems in place to reduce that risk. Strategic control can be demonstrated by the trustees approving the role of campaigning in advancing the objects and achieving organisational goals. Operational control can be achieved by the trustees approving the delegation of authority to campaign managers and conducting evaluations of campaigns and audit reviews of campaign risks. Charity trustees must also ensure compliance with other laws which impact upon campaigning: for example media and advertising law, defamation, election and public order law.

Political campaigning

The key question that fuelled the recent debate on campaigning concerned the amount of resources that a charity can devote to political campaigning. It is well established that, subject to satisfying trustees' duties, a charity can use all of its resources to engage in non-political campaigning i.e. awareness rising to persuade the public or private businesses to change their behaviour on a voluntary basis. As regards political campaigning, the previous 2004 Charity Commission guidance stated that political activities could only be 'ancillary' and could not be the 'dominant' activity. However, there was a lack of clarity as to what constituted 'ancillary' political campaigning activity and this contributed to a reticence on the part of some charity trustees to approve political campaigning activities.

In order to understand the background to the ancillary/dominant demarcation and the distinction between political and non-political campaigning, it is necessary to consider the legal basis of the prohibition on charities having directly political objects. In the 19th century the courts took a relaxed view on whether trusts with political objects were charitable. Peter Luxton in *The Law of Charities* explains that the courts, when determining charitable status, did not distinguish between those trusts that had political purposes and those which did not. Indeed a number of charities with directly political objects were set up such as the Lord's Day Observance Society and the Anti-Slavery Society.

The 19th century approach to charitable trusts with political objects did not survive. A principle emanated from the House of Lords judgment of Lord Parker in *Bowman v Secular Society* that organisations with political purposes would not be viewed as charitable. Lord Parker held that:

> '. . . [A] trust for the attainment of political objects has always been held invalid, not because it is illegal, for everyone is at liberty to advocate or promote by any lawful means a change

in the law, but because the court has no means of judging whether a proposed change in the law will or will not be for the public benefit, and therefore cannot say that a gift to secure the change is a charitable gift.'

Lord Parker stated in the *Bowman* case that 'Equity has always refused to recognise such objects as charitable'. However, as discussed above, on the basis of the case law, Lord Parker considerably overstated the position and as Lord Porter noted in his dissenting House of Lords judgment in *National Anti-Vivisection Society v Inland Revenue Commissioners* 'it is curious how scanty the authority is for the proposition that political objects are not charitable'. Lord Parker relied upon the case of *De Themmines v De Bonneval* [(1828) 38 ER 1035], *Re* in which the judge held that a trust set up to distribute literature advocating the supremacy of the Pope over secular authority was not charitable.

Lord Parker's analysis in *McGovern v Attorney-General* [[1982] Ch 321] was that political purposes are not charitable because the courts have to presume that the law is correct. It is not for the courts to judge whether a change of the law will be for the public benefit (the touchstone of charitable status); that is the role of Parliament. If they cannot decide that a purpose will definitely be for the public benefit, they cannot decide it is charitable. It is indeed a moot point as to whether the court, is in fact, incapable of judging the public benefit of a political purpose. For example, in *National Anti-Vivisection Society* it was held that the object of the society to abolish vivisection was not of public benefit, because whilst abolishing vivisection might morally elevate humanity, this benefit was far outweighed by the damage caused to humans by the loss to medical science and research. Nonetheless, Lord Parker's analysis of why political purposes cannot be charitable and the inability of the courts to determine the public benefit of political purposes remains settled law.

What activities are viewed as falling within the definition of political purposes? The definition usually referred to is taken from the first instance decision of *McGovern* in which Slade J. held that a trust set up by Amnesty International was not charitable. Slade J. also held that political purposes are those directed at:

- furthering the interest of a particular political party; or
- procuring changes in the laws of this country; or
- procuring changes in the laws of a foreign country; or
- procuring a reversal of government policy or of particular decisions of governmental authorities in this country; or
- procuring a reversal of government policy or of particular decisions of governmental authorities in a foreign country.

The extremely wide definition of political purposes has caused consternation amongst some charity campaigners. In particular, it goes much further than activity which is party political and makes no distinction between a charity seeking to change the policy of Government or public bodies as distinct from legislation and no distinction between political activity which is in this country and political activity which is abroad. As regards the definition in *McGovern* being wider than party political activity, Lord Simmonds held in *National Anti-Vivisection Society* that Lord Parker had always meant 'political' to be wider than 'party political measures but would cover activities directed to influence the legislature'.

In relation to political campaigning by charities which is overseas, many human rights charities are of the view, that *McGovern* (which pre-dated the incorporation of the European Convention into domestic law and a plethora of international human rights instruments) is no longer correct. Under the *McGovern* definition, human rights charities are not able, as their main activity, to campaign for governments to incorporate international human rights treaties into domestic law, or for countries to abide by international instruments which are not part of their domestic law. As the Charity Commission has signalled its intention to review its guidance on charities working overseas, this is an area which may develop.

(i) The advancement of environmental protection or improvement

Charitable purpose

The advancement of environmental protection or improvement is a further head of charity that was introduced for the first time under the Charities Act 2006. Under this head of charity, activities such as plant and wildlife conservation will be valid charitable purposes.[87] This head of charity will also include educational purposes such as research into conservation, recycling and minimising damage to the environment.

EXTRACT

Charity Commission Guidelines: RR9 Preservation and Conservation

4. We have concluded that in order to be charitable, organisations for preservation and conservation will need to demonstrate that:
   (i) they satisfy a criterion of merit, ie:
   - for preservation charities, there is independent expert evidence that the building or site is of sufficient historical or architectural interest (see paragraphs A5–A9 below);
   - for species conservation charities, there is independent expert evidence that the species is worthy of conservation (see paragraphs A10–A13 below);
   - for charities for the conservation of the environment, there is independent expert evidence that the land or habitat is worthy of conservation (see paragraphs A14–A15 below); and

   (ii) they are set up for the benefit of the public, ie:
   - they are not used for non-charitable purposes, such as trading (see paragraph A16 below);
   - they provide sufficient public access, either by providing sufficient physical access or provide access by suitable alternative means (see paragraphs A18–A27 below);
   - any private benefit to individuals is incidental and properly regulated (see paragraphs A31–A35 below).
5. During the consultation, we received a number of representations that it was no longer appropriate to consider preservation and conservation as two separate areas. In particular, in a least some cases, building preservation might be an aspect of environmental conservation. This is a view to which we are sympathetic and which we plan to explore further.
6. Any organisations claiming charitable status under the Charities Act 1993 must have objects that are exclusively charitable. They must also possess the other essential characteristics of a charity, as set out in our publication *The Review of the Register of Charities* (RR1).

Preservation charities

7. For organisations set up to preserve buildings, we are maintaining our current policy which reflects the position adopted by the courts, that is, to be charitable such organisations must be set up for the advancement of the education of the public.

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[87] *London University v Yarrow* (1857) 1 De G & J 72, 26 LJ Ch 430.

Conservation charities

8. 'Conservation of the environment' now has a well-established meaning and we recognise it as a charitable purpose beneficial to the community. We will therefore register such organisations as charities provided that they satisfy the criteria set out in the Annex.
9. A possible object for such organisations is:
'to promote the conservation protection and improvement of the physical and natural environment'.
10. Following on from this, we also accept that an object 'to promote the conservation of the physical and natural environment by promoting biological diversity [or biodiversity[3]]' is charitable.
11. It is also acceptable for environmental charities to have an additional object of advancing the education of the public where appropriate.

Source: http://www.charity-commission.gov.uk/Publications/rr9.aspx. Site accessed 16 January 2014.

Public benefit

Although the public benefit element of this type of trust addresses broadly the same issues as the other heads of charity, one particular issue pertaining to public benefit in this context is the need to balance public accessibility with the objectives of the charity. For example, where the charity's objectives are aimed at preserving delicate ecosystems, or the breeding grounds of endangered species, it may be in the interests of furthering the charity's objectives to be able to exclude the public from such places on the basis that they are likely to damage the environment that the organisation is seeking to protect. Nevertheless, if there is no opportunity for access by the public, then the trust's claims of charitable status will fail.

In the case of *In re Grove-Grady*[88] for example, it was emphasised that the objective of animal welfare charities was not simply the protection of the animal itself, but rather, to discourage cruelty and brutality among humans. Accordingly, the welfare of an animal or the protection of an environment is not a benefit in itself – there must also be a benefit to the public. A benefit to the public must be demonstrated, and an organisation that seeks to exclude the public will not ordinarily confer a public benefit.

An organisation may overcome this by demonstrating a public benefit in a different way – it may be legitimate to exclude the public from a rare bird's breeding ground if arrangements may be made to provide a benefit to the public in other ways, such as by disseminating information about the organisation's activities, or where appropriate, to provide limited access to the area or opportunities to view the animals from a distance through the use of television cameras or telescopes.

(j) The relief of those in need by reason of youth, age, ill-health, disability, financial hardship or other disadvantage

Charitable purpose

It is clear that this head of charity will overlap considerably with the relief of poverty as well as with the advancement of health and the relief of sickness. Poverty is not the only

[88] *In re Grove-Grady, Plowden v Lawrence* [1929] 1 Ch 557.

need that is covered by this head of charity, with the result that trusts such as *Re Gwyon*[89] that may have failed on the grounds that they were not restricted to those who were poor may be more likely to succeed under this ground where it is possible to recognise need as arising from a broader range of factors than poverty. Accordingly, the prevention of cruelty to children may be a charitable purpose under this head,[90] although it would fail as a charity for the relief of poverty. As with the poverty charities however, there is a need to demonstrate that the charitable purpose offers relief, rather than merely a benefit to those who are young, elderly or suffering from ill health, disability, financial hardship or disadvantage. Accordingly providing accommodation,[91] treatment and care[92] will be charitable under this head of charity, but provision for general welfare may not.[93]

Public benefit

The public benefit question in relation to this head of charity may also prove to be problematic. As was seen above, charities for the relief of poverty may legitimately confer a benefit on persons defined by a personal connection to an individual or to an organisation. However, the authority of *Oppenheim v Tobacco Securities*[94] confirms that this cannot apply in relation to other types of charity – and in *Re Compton*[95] Lord Simonds classified the poor relations cases as being anomalous and inconsistent with the rest of the law on charities. Given the extent of the overlap between the relief of those in need and the relief of poverty, it will be interesting to see whether charities that fall under this head as well as – or instead of – the relief of poverty will be recognised by the Charity Commission where there is a personal nexus (thus expanding the poverty exception) or whether the preferred approach will be to use this head of charity as a means of restricting the scope for poverty charities where the beneficiaries are defined by a personal connection to an individual or organisation on the basis that the recognition of such charities is a historical anomaly that can no longer be justified.

(k) The advancement of animal welfare

Charitable purpose

This charitable purpose overlaps to a significant degree with charities whose objectives are environmental protection or improvement. However, whereas environmental protection or improvement may be more appropriate in relation to species that are endangered, the advancement of animal welfare may include the protection of animals that are not endangered as a species. Therefore the RSPCA[96] for example may fall within this head of charity, despite being unlikely to be involved with environmental protection in a significant way. Accordingly, animal sanctuaries[97] and animal rescue services[98] will be

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[89] [1930] 1 Ch 255.
[90] *Income Tax Special Purposes Comrs v Pemsel* [1891] AC 531 at 572.
[91] *Re Estlin, Prichard v Thomas* (1903) 72 LJ Ch 687.
[92] Ibid.
[93] *Re Cole, Westminster Bank Ltd v Moore* [1958] Ch 877.
[94] [1951] AC 297.
[95] *In Re Compton, Powell v Compton and Others* [1945] Ch 123.
[96] *Tatham v Drummond* (1864) 4 De GJ & Sm 484.
[97] *Re Douglas, Obert v Barrow* (1887) 35 ChD 472.
[98] *Re Herrick, Colohan v A-G* (1918) 52 ILT 213.

charitable purposes for the purposes of this head of charity, as will educational facilities (such as research and training – also covered under the charitable purpose of education) for the veterinary profession.[99]

Public benefit

In addition to the general considerations regarding public benefit, one issue of particular note with regard to trusts for the welfare of animals is to state that as with the protection of the environment, it is not the welfare of the animal that confers a public benefit, it is the fact that promoting the welfare of animals is beneficial to public morality. Accordingly, an organisation that aims to protect animal welfare will not be charitable if it fails to confer a benefit to the public. The case *of Hanchett Stanford v Attorney General and Others*[100] explains this.

EXTRACT

Hanchett Stanford v Attorney General and Others [2009] Ch 173

Case facts

The claimant represented an inactive unincorporated association called The Performing and Captive Animals Defence League. She attempted to argue that the association's objectives were charitable, and that the association's outstanding funds could be transferred to another animal welfare charity.

Lewison J

The key element of any charitable trust is that it exists for the benefit of the public. The benefit to the public may be direct or indirect. It is the indirect benefit to the public which has enabled the law to uphold as charitable trusts for the prevention of cruelty to animals. The Hobbesian view of humanity that underlies this (an innate tendency to cruelty) was explained in *In re Wedgwood* [1915] 1 Ch 113, 122:

> 'A gift for the benefit and protection of animals tends to promote and encourage kindness towards them, to discourage cruelty, and to ameliorate the condition of the brute creation, and thus to stimulate humane and generous sentiments in man towards the lower animals, and by these means promote feelings of humanity and morality generally, repress brutality, and thus elevate the human race.'

Accordingly, a trust that had as its sole object the prevention of cruelty to performing animals would be capable of being a charitable trust. The advancement of animal welfare is now expressly recognised as a charitable purpose by section 3(1)(k) of the Charities Act 2011. I do not, however, regard this as a significant change in the law.

However, as Mr Sims points out on behalf of the Attorney General, in principle where the purpose or one of the purposes of a trust is to change the law the courts have refused to recognise the trust as charitable. A number of reasons have been given for this approach. First, it has been said that the courts cannot evaluate whether the advocated change in the law would or would not be for the benefit of the public. In *Bowman v Secular Society Ltd* [1917] AC 406, 442 Lord Parker of Waddington said:

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[99] *London University v Yarrow* (1857) 1 De G & J 72 at 80 per Lord Cranworth LC.
[100] [2009] Ch 173.

> 'It is true that a gift to an association formed for their attainment may, if the association be unincorporated, be upheld as an absolute gift to its members, or, if the association be incorporated, as an absolute gift to the corporate body; but a trust for the attainment of political objects has always been held invalid, not because it is illegal, for everyone is at liberty to advocate or promote by any lawful means a change in the law, but because the court has no means of judging whether a proposed change in the law will or will not be for the public benefit, and therefore cannot say that a gift to secure the change is a charitable gift.'

However, this may be too dogmatic a view. *In National Anti-Vivisection Society v Inland Revenue Comrs* [1948] AC 31 the House of Lords did evaluate the competing arguments for and against the abolition of vivisection; and came to the clear conclusion that the benefits to the public in terms of scientific and medical research outweighed the harm caused by the suffering of animals that vivisection necessarily entailed. A second reason that has been given is that law cannot stultify itself by holding that it is for the public benefit that the law itself should be changed; and that each court must decide on the principle that the law is right as it stands. This was the reason put forward by both Lord Wright and Lord Simonds in the *National Anti-Vivisection Society* case. A third reason is that if the courts sanction asm charitable trusts with the purpose of changing the law, they would be trespassing on the role of the legislature, whose constitutional responsibility it is to evaluate the need for such changes. This was one of the reasons given by Slade J in *McGovern v Attorney General* [1982] Ch 321 and by Chadwick LJ in *Southwood v Attorney General* [2000] WTLR 1199. This last reason seems to me to be the most persuasive. But whatever the rationale, there is no doubt that the principle remains that a trust, one of whose purposes is to change the law, cannot be charitable.

That is not to say that it is unlawful for a charity to promote or oppose changes in the law, provided that its purposes are exclusively charitable. There is a distinction between the purposes or objects of a charity and the means by which it promotes those purposes or objects. Thus the Charity Commission is able to issue guidance to charities and charity trustees about the extent to which they can engage in campaigning, including campaigns to change the law. However, that guidance still takes as its bedrock the principle that an organisation set up for the purpose of changing the law cannot be a charity.

Looking at the statement of the league's objectives there can be little doubt, in my judgment, that at least one of its significant purposes was to change the law. It is true that it asserted that the particular acts of cruelty against which it was campaigning were already illegal as a result of the Protection of Animals Act 1911, but plainly its founders considered that that Act was not enough and that more legislation was needed. It seems probable that the members of the league had a wider conception of cruelty than the law did. The booklet also asserted that it was impossible to train any performing animal without cruelty and it is clear, in my judgment, that the league's aim was to ban performing animals completely (hence the reference to 'just compensation to the trade'). This would undoubtedly represent a change in the law just as much as banning fox-hunting or the farming of mink. In my judgment this has the consequence that at its inception the league was not a charitable organisation. Ms Maclennan, who appeared for Mrs Hanchett-Stamford, did not argue strenuously that the league was charitable at its inception. I think that there were pragmatic reasons behind her stance, but I must apply the law as I perceive it to be.

However, Ms Maclennan submits that even if the objects of the league were not charitable at its inception, they have since become charitable. She puts this argument in two ways. (i) The objects of the league have become charitable as a result of changes in the law; alternatively (ii) the objects of the league have become charitable, or its assets held on charitable trusts, as a result of the decision of Mr and Mrs Hanchett-Stamford to transfer those assets to the Born Free Foundation.

In support of the first argument she relies on the story of the General Medical Council ('GMC'). The question of the charitable status of the GMC arose in *General Medical Council v Inland Revenue Comrs* (1928) 97 LJKB 578 . . . The Inland Revenue decided that the GMC had not been established for exclusively charitable purposes and the GMC's appeal against that decision was dismissed both by Rowlatt J and by the Court of Appeal . . . However, in 2001 the GMC applied to the Charity Commission for registration as a charity; and this time the application succeeded.

The commission considered that there had been no major changes in the law, although they referred to other cases in which it had been held that the regulation of a profession could be charitable. However, the commission considered that there had been major changes to the GMC's own powers and functions with the result that the GMC was a body 'significantly different to the body constituted under the Medical Act 1858 and to the body considered in the GMC case'. It noted also that the introduction of the National Health Service had transformed the environment within which medical services were provided (no doubt diminishing the need for most medical practitioners to be able to sue for their fees), and also the general recognition that the regulation of professions was in the public interest. It was these cumulative changes that persuaded the commission to re-open the question of the charitable status of the GMC.

In the present case Ms Maclennan relies on the passing of the Animal Welfare Act 2006 as amounting to the necessary change. She also points to the explicit recognition of the advancement of animal welfare as a charitable purpose by section 3(1)(k) of the Charities Act 2011. As to this last point, as I have said, the advancement of animal welfare has long been recognised as a charitable purpose, for the reasons explained in *In re Wedgwood* [1915] 1 Ch 113. I do not regard this as amounting to any change in the substance of the law. The Animal Welfare Act 2006 does contain provisions which create offences of causing distress to animals; but it does not go so far as to prohibit performing animals. As is clear from its statement of policies in the 1962 booklet, the league believed that it was impossible to train performing animals without cruelty. It seems to me, on such exiguous evidence as I have, that the objectives of the league have not yet been fully attained. In other words, it still appears to be one of the objects of the league to change the law. The Charities Act 2011 has not changed the fundamental principle that if one of the objects or purposes of an organisation is to change the law, it cannot be charitable . . .

I cannot accept the first argument for asserting that the league became charitable.

Outcome

The trust failed.

Thus it is seen that a public benefit will be conferred where the trust can be seen to limit human cruelty, or where there is a public educational benefit through opportunities for public access. However, trusts that promote the welfare of animals in a way that does not provide a public benefit (such as with the situation in the case of *National Anti-Vivisection Society v IRC*[101] where animal welfare could not be promoted in a way that was detrimental to humans, and whose objectives were also political in character) will not be charitable.

[101] [1948] AC 31.

(l) The promotion of the efficiency of the armed forces of the Crown, or of the efficiency of the police, fire and rescue services or ambulance services

Charitable purpose

Although this head of charity appeared as a specific charitable purpose for the first time in the Charities Act 2006, the types of activities that may be recognised under s.3(1)(l) have been recognised by the courts as being 'other purposes beneficial to the community' under Lord Macnaghten's classification in *Income Tax for Special Purposes Commissioners v Pemsel*.[102] Examples of activities that might now be included under this head of charity include the teaching of shooting,[103] the maintenance of a library at an officers' mess[104] and the provision of a lifeboat,[105] which are all illustrations of activities that have been accepted as being charitable, and will be regarded as activities that fulfil the purpose of promoting the efficiency of the armed forces and the emergency services.

Public benefit

In *Harrington v Watts*[106] Farwell J accepted that 'anything that improves the efficiency of the army is charitable within the meaning of the Act, because it is for a public purpose – a purpose in which the public are interested.' As with the other types of charity however, regard will also need to be had to the other issues of public benefit. Accordingly trusts where the beneficiaries are defined by their personal connection to an organisation will not be charitable. For example, in the case of *Inland Revenue Commissioners v Glasgow Police Athletic Association*,[107] the trust could not be regarded as being charitable. Here although a public benefit might be demonstrated from the fact that the Athletics Association was a means of recruiting future police officers and developing the health and fitness of existing police officers, these objectives were nonetheless ancillary to the Athletic Association's primary aim, which was to provide recreational facilities for its members. Accordingly, no public benefit could be discerned.

EXTRACT

Inland Revenue Commissioners v Glasgow Police Athletic Association [1953] AC 380 at pp.395–396

Case facts

The Glasgow Police Athletics Association attempted to claim that it should be exempted from paying income tax on the basis that it was a charitable organisation.

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[102] *Income Tax Special Purposes Commissioners v Pemsel* [1891] AC 531.
[103] *Re Stephens, Giles v Stephens* (1892) 8 TLR 792.
[104] *Re Good, Harington v Watts* [1905] 2 Ch 60.
[105] *Johnston v Swann* (1818) 3 Madd 457.
[106] [1905] 2 Ch 60.
[107] [1953] AC 380.

Lord Normand

It would be unjust to the respondent association to represent it as having no purpose beyond the recreation and amusement of the individual subscribers constituting its membership. No one can read the rules without perceiving that the association was regarded as having an official importance and a public aspect. And in order to ascertain what the purposes of an association are, the court is not limited to consideration of its rules or its constituent documents. They are very important, and it would be difficult for an association to say that something declared in its rules to be its object was not one of its purposes. But it is quite in order for the association to prove by parol evidence that it had other purposes beyond that expressly set down in the rules. The Special Commissioners had evidence before them which entitled them to find that, among its purposes, were the encouragement of recruiting, the improvement of the efficiency of the force, and the public advantage. This is a purpose which the Special Commissioners were entitled to hold in law to be a public charitable purpose. But there remains the non-charitable purpose of providing recreation to the members. The question is whether this non-charitable purpose is incidental to the public charitable purpose. If not, it cannot be said that the association was a body established for charitable purposes only. This is not a matter of the motive of the members of the association or of the high police officials who took a part in furthering the association, though there is a natural probability that their motives agree with the purposes of the association. The question is what are the purposes for which the association is established, as shown by the rules, its activities and its relation to the police force and the public. And what the respondents must show, in the circumstances of this case, is that so viewed objectively the association is established for a public purpose, and that the private benefits to members are the unsought consequences of the pursuit of the public purpose, and can therefore be disregarded as incidental. That is a view which I cannot take. The private benefits to members are essential. The recreation of the members is an end in itself, and without its attainment the public purpose would never come into view. If the result of establishing the association had been that the members had, instead of being interested, found themselves involved in wearisome and lifeless activities, their efficiency would have suffered, the membership would have fallen off, and there would have been public detriment instead of public benefit. The private advantage of members is a purpose for which the association is established and it therefore cannot be said that this is an association established for a public charitable purpose only.

Outcome

The association's non-charitable purpose could not be separated from its charitable objective, and the trust failed.

(m) Any other purposes

Charitable purpose

The final head of charity is the catch-all 'any other purposes' clause. Under this heading will be included purposes that were charitable before the Charities Act 2006 came into force on 1 April 2008. The presumption of public benefit regarding the advancement of religion and the advancement of education has been removed, with the result that organisations that fulfilled the pre-2006 requirements may no longer be consistent with the law's definition of charity. Such trusts will continue to be charitable.[108] Similarly,

[108] Charities Act 2011, s.3(4).

trusts that do not have a specific purpose but which are for the benefit of the community, will be regarded as being charitable under this head,[109] as will trusts that have as their objective work that is of public utility – such as the repair of bridges.[110] Also included under this heading is the promulgation of morality in a way that is not connected to a particular political party.[111] Temperance,[112] socialism[113] and kindness to animals[114] may be charitable under this heading. Section 3(1)(m) also provides scope for the recognition of new types of charitable purpose that cannot be satisfactorily assimilated within the existing heads of charity.

Public benefit

Again the usual considerations regarding the establishment of a public benefit will apply here, and in the absence of specific cases on this head of charity, it is not possible to give more precise guidance on how these cases will apply. Given that this head of charity does not clearly identify a charitable purpose, it is likely that the emphasis in terms of establishing charitable status will be on demonstrating that the trust confers a benefit to the public, and issues such as whether the trust benefits a sufficient section of the public will be given particular heed.

What this chapter demonstrates therefore is that the pre-2006 case law is still extremely useful in defining what purposes are charitable, and the circumstances under which they will be charitable. This is particularly evident as regards the pre 2006 charitable purposes that continue to be charities under the statutory provisions of the Charities Acts 2006 and 2011 (poverty, education, religion and other). However, the pre-existing law is also useful in relation to the new charitable purposes, as many of the new heads of charity are extensions of the previous purposes – especially education, and other. Nevertheless, the current law also allows for charitable purposes to exist that might not have been charitable under the previous law. The regulation and operation of charities will be addressed later (in Chapter 21).

Chapter summary

This chapter may be useful for assessments and assignments on:

- Charitable trusts
- Trusts for purposes
- Public benefit.

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[109] *A-G v Earl of Lonsdale* (1827) 1 Sim 105.
[110] Referred to in the preamble to the Statute of Charitable Uses 1601.
[111] *Re Scowcroft, Ormrod v Wilkinson* [1898] 2 Ch 638 at 642.
[112] *Re Hood, Public Trustee v Hood* [1931] 1 Ch 240 at 250.
[113] *Russell v Jackson* (1852) 10 Hare 204.
[114] *Marsh v Means* (1857) 3 Jur NS 790.

Further reading

Chesterman, M. (1999) 'Foundations of Charity Law in the New Welfare State' 62(3) *Modern Law Review* 333.

Dunn, A. (2012) 'The governance of philanthropy and the burden of regulating charitable foundations' *Conveyancer and Property Lawyer* 114.

Green, N. (2010) 'Independence: a Legal Requirement or a State of Mind' *Governance* 4.

McKenna, A. (2010) 'Joining the Legal Review of Public Benefit in Independent Schools' *Charity Finance* 15.

Rahmatian, A. (2009) 'The continued relevance of the "poor relations" and the "poor employees" cases under the Charities Act 2006' *Conveyancer and Property Lawyer* 12.

Warburton, J. (2008) 'Charities and public benefit: from confusion to light' 10(3) *Charity Law and Practice Review* 1.

21

The regulation and administration of charities

Chapter outline

This chapter will cover:

- Regulating the operation of charities
- Enforcement of charities
- The benefits of charitable status
- Perpetuities and accumulations
- The cy-près doctrine.

Regulating the operation of charities

Having established that an organisation is charitable, it will be the subject of very stringent regulation by the law. Part II of the Charities Act 2011 governs the regulation of charities. This part of the Charities Act 2011 consolidates and amends the Charities Acts of 1992, 1993, 2006 and the Recreational Charities Act 1958.

The Charity Commission, the Charity Tribunal and the High Court

The Charity Commission was established under the Charities Act 1993.[1] Section 11 of the Charities Act 2011 provides that the Charity Commission still exists (the Charity Commission for England and Wales or, in Welsh, Comisiwn Elusennau Cymru a Lloegr) and defines its role in s.14 and s.15 of the same Act.

EXTRACT

Charities Act 2011, s.14 and s.15

14 The Commission's objectives

The Commission has the following objectives –

1 The public confidence objective
The public confidence objective is to increase public trust and confidence in charities.

2 The public benefit objective
The public benefit objective is to promote awareness and understanding of the operation of the public benefit requirement.

3 The compliance objective
The compliance objective is to promote compliance by charity trustees with their legal obligations in exercising control and management of the administration of their charities.

4 The charitable resources objective
The charitable resources objective is to promote the effective use of charitable resources.

5 The accountability objective
The accountability objective is to enhance the accountability of charities to donors, beneficiaries and the general public.

15 The Commission's general functions

(1) The Commission has the following general functions –

1 Determining whether institutions are or are not charities.

2 Encouraging and facilitating the better administration of charities.

3 Identifying and investigating apparent misconduct or mismanagement in the administration of charities and taking remedial or protective action in connection with misconduct or mismanagement in the administration of charities.

4 Determining whether public collections certificates should be issued, and remain in force, in respect of public charitable collections.

[1] (1993 c.10).

5 Obtaining, evaluating and disseminating information in connection with the performance of any of the Commission's functions or meeting any of its objectives.

6 Giving information or advice, or making proposals, to any Minister of the Crown on matters relating to any of the Commission's functions or meeting any of its objectives.

(2) The Commission may, in connection with its second general function, give such advice or guidance with respect to the administration of charities as it considers appropriate.

(3) Any advice or guidance so given may relate to –

(a) charities generally,

(b) any class of charities, or

(c) any particular charity,

and may take such form, and be given in such manner, as the Commission considers appropriate.

(4) The Commission's fifth general function includes (among other things) the maintenance of an accurate and up-to-date register of charities under sections 29 (the register) and 34 (removal of charities from register).

(5) The Commission's sixth general function includes (among other things) complying, so far as is reasonably practicable, with any request made by a Minister of the Crown for information or advice on any matter relating to any of its functions.

(6) In this section 'public charitable collection' and 'public collections certificate' have the same meaning as in Chapter 1 of Part 3 of the Charities Act 2006.

Accordingly, the Charity Commission has a regulatory role in terms of determining whether institutions are or are not charities, and by investigating apparent mismanagement. Accordingly, the Commission is able to suspend or remove trustees (Charities Act 2011, s.83), give specific directions for the protection of a charity (Charities Act 2011, s.84) and the power to direct how charity property is to be applied (Charities Act 2011, s.85). Other powers conferred by the Charities Act 2011 include the Charity Commission being able to determine membership of the charity (Charities Act 2011, s.111), and also to enter premises and seize documents (Charities Act 2011, s.48). However, its role is also advisory, as well as having a public relations function in that the Commission has a responsibility to encourage the better administration of charities and advises charitable trustees on how this might be best achieved.

In addition to the Charity Commission, the Charities Act 2011 also makes provision for a Charity Tribunal[2] (to be known as Y Tribiwnlys Elusennau in Welsh) whose role is to hear appeals against decisions by the Charity Commission.

The Register of Charities

The Charity Commission is required to maintain a register of charities under s.29 Charities Act 2011. The register is intended to provide an up-to-date list of extant charities. However, s.22 allows some charities to be exempted from registration either by the Charity Commission itself or by the relevant Secretary of State,[3] and for others to be exempt from registration. Small charities, whose gross income is below £5000, will also

[2] Charities Act 2011, s.315.

[3] Therefore, for example, it will be the Secretary of State for Education in England, or the Welsh Ministers in Wales who will be able to exempt an educational charity from the requirements of registration.

not be registered. The main exempt charities are universities and colleges in England, although specific museums, the Church Commissioners, and industrial and provident societies are also examples of charities that are exempt from the requirement of registration. The exempt charities are listed in Schedule 3 to the Charities Act 2011.

Charities and trustees

As with other forms of trust, a charity will have trustees. Charitable trustees will of course be subject to the same duties and obligations described earlier (in Chapter 11) as trustees of a private trust. However, the obligations of a charitable trustee are in many ways more onerous, and additional responsibilities are placed upon them. Primarily of course, the charitable trustee must ensure that the trust is administered with a view to ensuring that the charitable purpose is fulfilled for the benefit of the public. More specific duties include for example, the fact that a charitable trustee will be obliged to register the trust in accordance with s.35 Charities Act 2011. Furthermore, s.178 contains specific provisions regarding trustees who are disqualified from being charitable trustees.

EXTRACT

Charities Act 2011, s.35

35 Duties of trustees in connection with registration

(1) If a charity required to be registered by virtue of section 30(1) is not registered, the charity trustees must –

(a) apply to the Commission for the charity to be registered, and

(b) supply the Commission with the required documents and information.

(2) The required documents and information are –

(a) copies of the charity's trusts or (if they are not set out in any extant document) particulars of them,

(b) such other documents or information as may be prescribed by regulations made by the Minister, and

(c) such other documents or information as the Commission may require for the purposes of the application.

(3) If an institution is for the time being registered, the charity trustees (or the last charity trustees) must –

(a) notify the Commission if the institution ceases to exist, or if there is any change in its trusts or in the particulars of it entered in the register, and

(b) so far as appropriate, supply the Commission with particulars of any such change and copies of any new trusts or alterations of the trusts.

(4) Nothing in subsection (3) requires a person –

(a) to supply the Commission with copies of schemes for the administration of a charity made otherwise than by the court,

(b) to notify the Commission of any change made with respect to a registered charity by such a scheme, or

(c) if the person refers the Commission to a document or copy already in the Commission's possession, to supply a further copy of the document.

Also, where the objects of the trust fail, then a duty is imposed upon the trustee to apply for a cy-près scheme (discussed below) under the Charities Act 2011, s.61. The Charity Commission and the High Court are able to remove trustees, either because of a breach of trust or for other reasons, such as where a trustee is unable or unwilling to act.

Trading activities

A part of a charity's role may also require it to undertake trading activities. Trading by charities may take one of three forms – primary trading, ancillary trading or non-primary purpose trading. Primary purpose trading is characterised by the fact that trading is essential to fulfilling the purpose of the charity, such as where education is provided in return for payment of a fee. Ancillary trading occurs where the trading activity is ancillary to the purpose of the charity, such as where food and drink or gifts are sold at a performance venue or museum that operates as a charity. Thirdly, it is possible for charities to undertake trading activities that do not exist in order to fulfil the charity's primary purpose, but exist in order to raise funds for the charity. Shops selling goods (such as greetings cards or toys) in order to raise funds for the charity are a clear example of non-primary trading activities, although the sale of donated goods will not be classified as trading.

EXTRACT

Charity Commission (2007) CC35 Trustees Trading and Tax

C. Trading by charities

C1. What is trading?

The short answer

There is, unfortunately, no short answer. The sale of goods (including property) or services is an essential feature of any trade. However, there are cases in which charities may sell goods or services, without the activity being regarded as a 'trade', and without the income so arising being treated as trading profits. This distinction matters, for example, because trading profits may be taxable (see C4).

In more detail

Whether the sale of goods and services by a charity is 'trading' depends on a number of factors, including:

- the number and frequency of transactions;
- the nature of the goods or services being sold;
- the intention of the charity in acquiring the goods which are to be sold;
- whether the goods are capable of being used and enjoyed by the charity selling them;
- the nature and mechanics of the sales; and
- the presence or absence of a profit motive.

But the fact that the sale of goods, services and property furthers the objects of the charity, or that the trading profits are to be used for the furtherance of those objects, does not prevent an activity from being regarded as 'trading'.

The following activities are not generally regarded as 'trading', and the income derived from them is not regarded as trading profits:

- the sale or letting of goods donated to a charity for the purpose of sale or letting (see C3);
- the sale of investments;
- the sale of assets which the charity uses, or has used, for its charitable purposes; and
- the letting of land and buildings where no services are provided to the user.

Where a charity is trading, the trading profits are, in principle, subject to corporation tax (or income tax in the case of charitable trusts), other than as specifically exempted. See C4 for further information.

Further information

Please refer to the HMRC website guidance Trading and business activities for more information on trading by charities.

When a charity lets property, the trustees will normally need to obtain the advice of a qualified surveyor regarding a proper rent for the property: see the Commission guidance *Sales, leases, transfers or mortgages: What charities need to know about disposing of charity land* (CC28). If services are provided to the user, such letting may amount to a property business, which would be 'trading'.

C2. What kind of trading may charities carry on?

The short answer

Charities may carry on trading activities which contribute directly to the furtherance of their charitable objects, or (where the purpose is to raise funds for the charity) which do not involve significant risk.

In more detail

Charity law allows charities to trade provided that the trading falls into one of the following categories:

- 'primary purpose trading' (see C6);
- 'ancillary trading' (see C7); and
- 'non-primary purpose trading' that does not involve significant risk to the resources of the charity (see C8).

Note that the third category of trading listed above, 'non-primary purpose trading' that does not involve significant risk to the resources of the charity, is normally understood to include:

- the conduct of lotteries, subject to conditions (see C11); and
- trading within the terms of the 'small scale exemption' (see C12).

But it may also include other types of trading: it depends on the circumstances.

Further information

The Commission guidance *Providing Alcohol on Charity Premises* (CC27) gives further information on the sale of alcohol from charity premises.

C3. Is the sale or hiring out of donated goods 'trading'?

The short answer

No. The sale, or letting on hire, by a charity of goods donated to it with the intention that they should be sold (or let) is not normally 'trading'. The income so derived is not considered as

trading profits and is not liable to corporation tax (or income tax in the case of charitable trusts). Such sales are zero-rated for VAT purposes.

In more detail

The selling or letting of donated goods is not considered as 'trading'. It **is** a business activity for VAT purposes, and such sale or letting is within the scope of VAT. However, the sales are zero-rated if the goods are sold or let through charity shops, or through charity auctions or similar events, to the general public, disabled people, or people receiving certain specified benefits, or are exported. The sale or letting of donated goods by a trading subsidiary may also be zero-rated (see Part D, in particular D13).

If goods donated to a charity with a view to sale are substantially altered or improved prior to sale, for example by turning donated raw materials into finished, saleable goods, then the profits from such sales may be treated as trading profits, and the VAT treatment may be affected. However, sorting and cleaning items, or giving them minor repairs, does not make the profits obtained from their sale trading profits.

See also C10.

C4. Do charities have to pay tax on trading profits?

The short answer

Yes. Trading profits, and some charity income from other sources, are liable to corporation tax (or income tax in the case of charitable trusts) unless specifically exempted.

In more detail

Charity trading profits are exempt from corporation tax (or income tax in the case of charitable trusts) where the trading is:

- 'primary purpose trading' (see C6);
- 'ancillary trading' (see C7);
- within the terms of the 'small scale exemption' (see C12);
- a lottery (see C11); or
- connected with certain fund-raising events (see C13).

In all these cases the exemption is subject to the condition that the profits are applied solely to the purposes of the charity.

Also note that the sale or hiring out of goods donated for that purpose is not normally 'trading' and that income from this activity is not liable to income or corporation tax (see C3).

Most types of charity income – other than trading profits – are either not liable to income or corporation tax at all, or qualify for generally applicable exemptions, so long as the income is only applied for charitable purposes. But certain types of non-trading income (technically described as 'incoming resources from miscellaneous activities') are taxable. In some cases the 'small scale exemption' may be available, in others there is no exemption at all. Examples of such 'incoming resources from miscellaneous activities' include:

- income from the underwriting of shares (except where this is done on a regular basis, when this is likely to be treated as trading); and
- gains arising on the sale of land, which are treated for tax purposes as income rather than capital, because the land was acquired specifically with a view to obtaining a gain on disposal, or because the consideration for the sale is structured wholly or partly by reference to the profits of the subsequent development of the land by the purchaser.

It may be beneficial to a charity for it to carry on in a trading subsidiary such forms of business as are expected to produce incoming resources of this nature, since the subsidiary's liability to corporation tax may be reduced or eliminated as indicated in D4.

However this guidance is primarily about charities and trading, not about how charities can reduce their tax liabilities. Professional advice should be taken before a charity hives off non-trading activities of this nature to a trading subsidiary.

Further information

More information about the tax liabilities of charities can be obtained from the HMRC website.

C5. Do charities have to charge VAT on sales?

The short answer

Yes. Charities which are registered for VAT must charge VAT on standard/reduced rated sales in the same way as other organisations, but there are some specific provisions for zero-rating or exemptions, which apply to charities, or to some charities, but not to other organisations, or not to all other organisations.

In more detail

The sale of goods by charities is subject to VAT on the same basis as would apply to commercial organisations, unless specific provisions for zero-rating or exemption apply. There are a number of such provisions applying to some charities, to charities generally, or to a class of supplier which includes some charities or charities generally. The following are examples of the special treatments:

- the sale or hiring out of goods donated to charities for that purpose is zero-rated for VAT (see C3); and
- the sale of goods or services at certain charity fund raising events is exempt from VAT (see C13).

Further information

More information about the tax liabilities of charities can be obtained from the HMRC website. The area of VAT is a notoriously complex one, and any charity making sales should seek the advice of a taxation specialist.

C6. What is 'primary purpose trading'?

The short answer

'Primary purpose trading' is trading which contributes directly to one or more of the objects of a charity as set out in its governing document. For present purposes, it includes trading in which the work in connection with the trading is mainly carried out by beneficiaries of the charity, as that will normally be primary purpose trading. Whether it is so or not, both the charity law and the tax treatment are similar.

In more detail

Typical examples of primary purpose trading include the:

- provision of educational services by a charitable school or college in return for course fees;
- sale of goods manufactured by disabled people who are beneficiaries of a charity for the disabled;
- holding of an art exhibition by a charitable art gallery or museum in return for admission fees;

- provision of residential accommodation by a residential care charity in return for payment;
- sale of tickets for a theatrical production staged by a theatre charity; and
- sale of certain educational goods by a charitable art gallery or museum.

The profits from primary purpose trading are exempt from corporation tax (or income tax in the case of charitable trusts). This exemption from tax is only available if the profits are applied solely to the purposes of the charity. However the sales which have given rise to those profits will be regarded as a business activity for the purposes of determining liability to VAT.

Further information

HMRC Charities will advise trustees whether, in their opinion, a particular activity is within the definition of primary purpose trading. In case of any doubt or difficulty trustees may need to consult their own professional advisers as well.

C7. What is 'ancillary trading'?

The short answer

'Ancillary trading' contributes indirectly to the successful furtherance of the purposes of the charity. This is treated as part of 'primary purpose trading' for both charity law and tax purposes.

In more detail

An example of ancillary trading is the sale of food and drink in a restaurant or bar by a theatre charity to members of an audience. The level of annual turnover in trading which is said to be ancillary may have a bearing on the question whether the trading really is ancillary, but there is no specific level of annual turnover beyond which trading will definitely not be regarded as ancillary. Trading is not regarded as ancillary to the carrying out of a primary purpose of the charity simply because its purpose is to raise funds for the charity.

Further information

More detail can be found in the HMRC website guidance Trading and business activities within the 'Charities' section.

C8. What is 'non-primary purpose trading', and when may charities engage in it?

The short answer

'Non-primary purpose trading' is trading intended to raise funds for the charity, as distinct from trading which in itself furthers the charity's objects. Charities may engage in such trading only where no significant risk is involved.

In greater detail

Charity law permits charities to carry on non-primary purpose trading in order to raise funds, provided that the trading involves no significant risk to the assets of the charity.

The 'significant risk' to be avoided here is that the turnover is insufficient to meet the costs of carrying on the trade, and the difference has to be financed out of the assets of the charity.

Whilst this is not invariably the case, the trade creditors would normally have a right of recourse to any of the assets of the charity, whether those assets had any connection with the trading or not. The consequent depletion of the charity's assets could have the effect of preventing the charity from being able to continue serving the community as effectively as it might otherwise have done, or at all. Those who provided the charity's assets are likely to have expected that those assets would be used to further the charity's purposes, or invested

prudently, and would not be put at risk in trading activities the object of which was simply to raise further funds.

Whether or not the risk of non-primary purpose trading is 'significant' depends on a number of factors, including:

- the size of the charity;
- the nature of the business;
- the expected outgoings;
- turnover projections; and
- the sensitivity of business profitability to the ups and downs of the market.

Inevitably, the assessment of the significance of the risk will involve an element of judgment on the part of trustees and their advisers. In general, however, a lottery, or trading which qualifies for the 'small-scale exemption' (see C12) may be considered not to involve significant risk.

There is no general exemption from corporation tax (or income tax in the case of charitable trusts) on the profits of non-primary purpose trading carried on by a charity, even where the profits are all applied for the charity's purposes. However, some exemptions do apply, ie the lotteries exemption (see C11), the 'small-scale exemption' (see C12), and the fundraising exemption (see C13).

If charities wish to carry on non-primary purpose trading involving significant risk, they must do so through a trading subsidiary, as set out in Part D. This whether or not the trading profits would, if the trading were to be carried on by the charity itself, be tax exempt.

Source: http://www.charity-commission.gov.uk/publications/cc35c.aspx. Site accessed 17 January 2014.

Enforcement of charities

As was discussed earlier (in Chapter 8), one of the justifications for the law's need for certainty of objects in relation to trusts is because there is a need for someone who is capable of undertaking litigation in the event of a breach of trust. Because a charitable trust is for the benefit of the public at large however, it is not the beneficiaries who will litigate. Instead, it is the Attorney General, as the Crown's representative in forensic matters, who will undertake litigation on behalf of a charitable trust. Charity Corporations must have a visitor, whose role is to settle disputes, investigate activities and to address any irregularities that arise in relation to the charity's conduct. Universities for example will have a board of visitors who will undertake this role.

Charities, as s.1(1) Charities Act 2011 states, are subject to the jurisdiction of the High Court, and it is before this court that allegations of breaches of trust must be brought. The county court has some limited jurisdiction to enforce the execution of a charitable trust, and to make a declaration that a charitable trust exists. In all likelihood however, these functions will invariably be fulfilled by the High Court, and a county court's jurisdiction in this respect is seldom exercised.

The benefits of charitable status

It is clear from this chapter that acquiring charitable status, and fulfilling the law's definition of what constitutes charitable status is a complex issue. Once charitable status has

been acquired, it is also clear that the organisation is subject to a significant level of regulation. Accordingly, it is necessary to consider in this section what advantages there may be to charitable status.

Taxation

One of the primary advantages of acquiring charitable status is that charities will be exempt from various forms of taxation, because not only is charity seen to be socially valuable, it also means that the work of the charity does not have to be supported to the same extent by grants and subsidies. The exemptions and reliefs from taxation that are applicable in relation to charities are contained in ss.466–493 Corporation Tax Act 2010[4] (where the charity is a company) and in ss.521–536 Income Tax Act 2007,[5] where the charity is a charitable trust.

EXTRACT

Corporation Tax Act 2010

466 Overview of Part

(1) This Part makes provision about some gifts and payments made to charitable companies, including provision applying the charge to corporation tax on income and conferring exemptions (see sections 471 to 474).

(2) This Part also provides for some of the income of charitable companies and others to be exempt from corporation tax (see sections 475 to 477 and Chapter 3).

(3) In the case of a charitable company which has a non-exempt amount for an accounting period (see section 493), the exemptions under this Part are subject to restrictions (see section 492).

(4) The non-exempt amount for an accounting period depends on the charitable company's attributable income and gains for the period and its non-charitable expenditure for the period (see sections 493 and 496 to 517).

(5) See also Schedule 19 to FA 2008, which contains provision for transitional payments to charitable companies and certain other bodies in respect of gifts made in the tax years 2008–09 to 2010–11.

Gifts and other payments to charitable companies

471 Gifts qualifying for gift aid relief: income tax treated as paid

(1) This section applies if a gift is made to a charitable company by an individual and the gift is a qualifying donation for the purposes of Chapter 2 of Part 8 of ITA 2007 (gift aid).

(2) The charitable company is treated as receiving, under deduction of income tax at the basic rate for the tax year in which the gift is made, a gift of an amount equal to the grossed up amount of the gift.

(3) References in this section to the grossed up amount of the gift are to the amount of the gift grossed up by reference to the basic rate for the tax year in which the gift is made.

(4) The income tax treated as deducted is treated as income tax paid by the charitable company.

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[4] (2010 c.4).
[5] (2007 c.3).

472 Gifts qualifying for gift aid relief: corporation tax liability and exemption

(1) If a charitable company receives a gift from an individual and the gift is a qualifying donation for the purposes of Chapter 2 of Part 8 of ITA 2007 (gift aid), the grossed up amount of the gift is treated as an amount in respect of which the company is chargeable to corporation tax, under the charge to corporation tax on income.

(2) But the grossed up amount of the gift is not taken into account in calculating total profits so far as that grossed up amount is applied to charitable purposes only.

(3) References in this section to the grossed up amount of a gift are to the amount of the gift grossed up by reference to the basic rate for the tax year in which the gift is made.

(4) The exemption under subsection (2) requires a claim.

(5) . . .

[472A Gifts under payroll deduction schemes: corporation tax liability and exemption]

(1) [If a charitable company receives a gift from an individual and the gift is a donation for the purposes of Part 12 of ITEPA 2003 (payroll giving), the gift is treated as an amount in respect of which the charitable company is chargeable to corporation tax, under the charge to corporation tax on income.

(2) But the gift is not taken into account in calculating total profits so far as it is applied to charitable purposes only.

(3) The exemption under subsection (2) requires a claim.]

473 Gifts of money from companies: corporation tax liability and exemption

(1) If a charitable company receives a gift of a sum of money from a company which is not a charity, the gift is treated as an amount in respect of which the charitable company is chargeable to corporation tax, under the charge to corporation tax on income.

(2) But the gift is not taken into account in calculating total profits so far as it is applied to charitable purposes only.

(3) The exemption under subsection (2) requires a claim.

474 Payments from other charities: corporation tax liability and exemption

(1) Subsection (2) applies if a charitable company receives from another charity a payment which-

(a) is not made for full consideration in money or money's worth,

(b) is not chargeable to corporation tax apart from this section, and

(c) is not of a description which (on a claim) would be exempt from corporation tax under any of the exemptions conferred by this Part.

(2) The payment is treated as an amount in respect of which the charitable company is chargeable to corporation tax, under the charge to corporation tax on income.

(3) But the payment is not taken into account in calculating total profits so far as it is applied to charitable purposes only.

(4) In the case of a payment to which section 494 of ITA 2007 (discretionary payments by trustees) applies, the references in subsections (2) and (3) to the payment are to be read as references to the grossed up amount of the discretionary payment within the meaning of that section.

(5) The exemption under subsection (3) requires a claim.

475 Gifts qualifying for gift aid relief: income tax treated as paid and exemption

(1) This section applies if a gift is made to an eligible body by an individual and the gift is a qualifying donation for the purposes of Chapter 2 of Part 8 of ITA 2007 (gift aid).

(2) The eligible body is treated as receiving, under deduction of income tax at the basic rate for the tax year in which the gift is made, a gift of an amount equal to the grossed up amount of the gift.

(3) References in this section to the grossed up amount of the gift are to the amount of the gift grossed up by reference to the basic rate for the tax year in which the gift is made.

(4) The income tax treated as deducted is treated as income tax paid by the eligible body.

(5) The grossed up amount of the gift is not taken into account in calculating total profits.

(6) The exemption under subsection (5) requires a claim.

(7) . . .

(8) In the case of an eligible body which is a charitable company, this section applies instead of sections 471 and 472.

476 Gifts of money from companies: exemption

(1) If an eligible body receives a gift of a sum of money from a company, the gift is not taken into account in calculating total profits.

(2) The exemption under subsection (1) requires a claim.

(3) In the case of an eligible body which is a charitable company, this section applies instead of section 473.

Gifts to scientific research associations

477 Gifts of money from companies: exemption

(1) A gift of a sum of money that a body receives from a company is not taken into account in calculating total profits if the body receiving the gift qualifies as a scientific research association for the relevant accounting period.

(2) The exemption under subsection (1) requires a claim.

(3) In subsection (1) 'the relevant accounting period' means the accounting period for which the exemption is to be claimed.

(4) In the case of a body which qualifies as a scientific research association and is also a charitable company, this section applies instead of section 473.

. . .

Exemptions

478 Exemption for profits etc of charitable trades

(1) The income mentioned in subsection (2) is not taken into account in calculating total profits if the condition in subsection (3) is met.

(2) The income referred to in subsection (1) is –

(a) profits of a charitable trade carried on by a charitable company, and

(b) post-cessation receipts arising from a charitable trade carried on by a charitable company which are received by the company or to which it is entitled.

(3) The condition is that the profits are, or (as the case may be) the post-cessation receipt is, applied to the purposes of the charitable company only.

(4) In this section 'post-cessation receipt' means an amount that is a post-cessation receipt for the purposes of Part 3 of CTA 2009 (see sections 190 to 195 of that Act).

(5) The exemption under subsection (1) requires a claim.

480 Exemption for profits of small-scale trades

(1) The income mentioned in subsection (2) is not taken into account in calculating total profits if conditions A and B are met.

(2) The income referred to in subsection (1) is-

(a) the profits of a trade carried on by a charitable company, and

(b) post-cessation receipts arising from a trade carried on by a charitable company which are received by the company or to which it is entitled.

(3) Subsection (1) does not apply in respect of-

(a) profits of a trade that are, apart from this section, exempt from corporation tax chargeable under Part 3 of CTA 2009, or

(b) post-cessation receipts that are, apart from this section, exempt from corporation tax chargeable under Chapter 15 of Part 3 of CTA 2009.

(4) Condition A is-

(a) in the case of the profits of a trade, that the profits are profits of an accounting period in relation to which the condition specified in section 482 (condition as to trading and miscellaneous incoming resources) is met, and

(b) in the case of a post-cessation receipt, that it is received in such an accounting period.

(5) Condition B is that the profits are, or (as the case may be) the receipt is, applied to the purposes of the charitable company only.

(6) The exemption under subsection (1) requires a claim.

(7) In this section 'post-cessation receipt' means an amount that is a post-cessation receipt for the purposes of Part 3 of CTA 2009 (see sections 190 to 195 of that Act).

481 Exemption from charges under provisions to which section 1173 applies

(1) Any income or gains of a charitable company that is or are chargeable to corporation tax under or by virtue of any provision to which section 1173 applies is not or are not taken into account in calculating total profits if conditions A and B are met.

(2) Subsection (1) does not apply in respect of any income or gains that is or are chargeable to corporation tax by virtue of any of-

(a) section 818(1) (gains from transactions in land),

(b) section 1086(2) (chargeable payments connected with exempt distributions), and

(c) any other enactment specified in an order made by the Treasury.

(3) Subsection (1) does not apply in respect of any income that is, or gains that are, apart from this section, exempt from corporation tax chargeable under or by virtue of any provision to which section 1173 applies.

(4) Condition A is that the income is, or the gains are, for an accounting period in relation to which the condition specified in section 482 (condition as to trading and miscellaneous incoming resources) is met.

(5) Condition B is that the income is, or the gains are, applied to the purposes of the charitable company only.

(6) The exemption under subsection (1) requires a claim.

482 Condition as to trading and miscellaneous incoming resources

(1) The condition in this section is met in relation to an accounting period if-

(a) the sum of the charitable company's trading incoming resources and miscellaneous incoming resources for the accounting period does not exceed the requisite limit for the period, or

(b) the charitable company had, at the beginning of the period, a reasonable expectation that it would not do so.

(2) The charitable company's 'trading incoming resources' for the accounting period are-

(a) the incoming resources which are required to be taken into account in calculating the profits of, or losses made in, the period for any non-exempt trade carried on by the company, and

(b) the incoming resources which are post-cessation receipts arising from such a trade.

'Post-cessation receipt' has the meaning given by section 480(7).

(3) For the purposes of subsection (2) a trade is a 'non-exempt trade' if any profits of the trade would not, apart from section 480, be exempt from corporation tax chargeable under Part 3 of CTA 2009.

(4) The charitable company's 'miscellaneous incoming resources' for the accounting period are the incoming resources which are required to be taken into account in calculating non-exempt miscellaneous income or non-exempt miscellaneous losses for the period.

(5) In subsection (4)-

'non-exempt miscellaneous income' means income or gains chargeable to corporation tax under or by virtue of any provision to which section 1173 applies that is not, or are not, apart from section 480 or 481, exempt from corporation tax chargeable under or by virtue of that provision, and

'non-exempt miscellaneous losses' means losses arising from a transaction which is of such a nature that if income or gains had arisen from it the income would have been non-exempt miscellaneous income.

(6) The requisite limit-

(a) is 25% of the charitable company's total incoming resources for the accounting period, but

(b) must not be less than £5,000 or more than £50,000.

(7) If the accounting period is shorter than 12 months, the amounts of £5,000 and £50,000 mentioned in subsection (6)(b) are proportionately reduced.

483 Exemption for profits from fund-raising events

(1) The profits of a trade carried on by a charitable company are not taken into account in calculating total profits so far as they-

(a) arise from an event that is VAT-exempt in relation to the company, and

(b) are applied to charitable purposes or transferred to a charity.

(2) The profits of a trade carried on by a body to which subsection (3) applies are not taken into account in calculating total profits so far as they-

(a) arise from an event that is VAT-exempt in relation to the body, and

(b) are applied to charitable purposes or transferred to a charity.

(3) This subsection applies to any voluntary organisation that is a qualifying body for the purposes of Group 12 of Schedule 9 to the Value Added Tax Act 1994 (fund-raising events by charities and other qualifying bodies).

(4) The exemptions under this section require a claim.

(5) For the purposes of this section an event is VAT-exempt in relation to a person if the supply of goods and services by that person in connection with the event would be exempt from value added tax under Group 12 of Schedule 9 to the Value Added Tax Act 1994.

484 Exemption for profits from lotteries

(1) The profits accruing to a charitable company from a lottery are not taken into account in calculating total profits if conditions A and B are met.

(2) Condition A is that-

(a) the lottery is an exempt lottery within the meaning of the Gambling Act 2005 by virtue of Part 1 or 4 of Schedule 11 to that Act,

(b) the lottery is promoted in accordance with a lottery operating licence within the meaning of Part 5 of the Gambling Act 2005, or

(c) the lottery is promoted and conducted in accordance with Article 133 or 135 of the Betting, Gaming, Lotteries and Amusements (Northern Ireland) Order 1985 (SI 1985/1204 (NI 11)).

(3) Condition B is that the profits are applied to the purposes of the charitable company only.

(4) The exemption under subsection (1) requires a claim.

485 Exemption for property income etc

(1) Income which is chargeable to corporation tax under Part 3 of CTA 2009 (trading income) as a result of section 287 of that Act is not taken into account in calculating total profits so far as-

(a) it arises in respect of rents or other receipts from an estate, interest or right in or over land, and

(b) the estate, interest or right is vested in any person for charitable purposes.

(2) Income which is chargeable to corporation tax under Part 4 of CTA 2009 (property income) is not taken into account in calculating total profits so far as-

(a) it arises in respect of an estate, interest or right in or over land, and

(b) the estate, interest or right is vested in any person for charitable purposes.

(3) Distributions to which section 548 (Real Estate Investment Trusts: distributions) applies and which are chargeable to corporation tax under Part 4 of CTA 2009 are not taken into account in calculating total profits so far as they arise in respect of shares vested in any person for charitable purposes.

(4) Subsections (1) to (3) apply so far as the income is applied to charitable purposes only.

(5) The exemptions under this section require a claim.

486 Exemption for investment income and non-trading profits from loan relationships

(1) The income mentioned in subsection (2) is not taken into account in calculating total profits if-

(a) it is income of a charitable company, or

(b) it is required, under an Act (including an Act of the Scottish Parliament), court judgment, charter, trust deed or will, to be applied to charitable purposes only.

(2) The income referred to in subsection (1) is-

(a) profits which are charged to tax under section 299 of CTA 2009 (non-trading profits from loan relationships),

(b) a dividend or other distribution of a company, and

(c) income treated for the purposes of Chapter 5 of Part 10 of CTA 2009 (distributions from unauthorised unit trusts) as received by a unit holder from a scheme to which section 972 of that Act applies (unauthorised unit trust schemes).

(3) Subsection (1) applies, in relation to the income mentioned in subsection (2)(b), only so far as the income falls within, and is dealt with under, Part 9A of CTA 2009 (see section 931W of that Act as to provisions given priority over Part 9A).

(4) Subsection (1) applies, in relation to the income mentioned in subsection (2)(c), only so far as the income falls within, and is dealt with under, Part 10 of CTA 2009 (see section 982 of that Act as to provisions given priority over Part 10).

(5) Subsection (1) applies so far as the income is applied to charitable purposes only.

(6) The exemption under subsection (1) requires a claim.

487 Exemption for public revenue dividends

(1) Public revenue dividends on securities which are in the name of trustees are not taken into account in calculating total profits so far as the dividends are applicable and applied only for the repair of-

(a) a cathedral, college, church or chapel, or

(b) a building used only for the purposes of divine worship.

(2) In this section 'public revenue dividends' means-

(a) income from securities which is payable out of the public revenue of the United Kingdom or Northern Ireland, or

(b) income from securities issued by or on behalf of a government or a public or local authority in a country outside the United Kingdom.

(3) The exemption under subsection (1) requires a claim.

488 Exemption for certain miscellaneous income

(1) The income mentioned in subsection (3) is not taken into account in calculating total profits if-

(a) it is income of a charitable company, or

(b) it is required, under an Act (including an Act of the Scottish Parliament), court judgment, charter, trust deed or will, to be applied to charitable purposes only.

(2) Subsection (1) applies so far as the income is applied to charitable purposes only.

(3) The income referred to in subsection (1) is-

(a) non-trading gains on intangible fixed assets,

(b) annual payments charged to tax under Chapter 7 of Part 10 of CTA 2009, and

(c) qualifying income from intangible fixed assets.

(4) The exemption under subsection (1) requires a claim.

(5) In this section-

'intangible fixed asset' has the same meaning as in Part 8 of CTA 2009 (see section 713 of that Act),

'non-trading credit' has the meaning given by section 301 of CTA 2009,

'non-trading gain' has the meaning given by section 751 of CTA 2009,

'pre-FA 2002 asset' has the meaning given by sections 881 and 892 to 895 of CTA 2009, and

'qualifying income from intangible fixed assets' means income which-

(a) is in respect of intangible fixed assets which are pre-FA 2002 assets,

(b) is of a kind which, if the intangible fixed assets were not pre-FA 2002 assets, would fall to be brought into account under Chapter 6 of Part 8 of CTA 2009 as non-trading credits, and

(c) does not fall within subsection (3)(a) or (b).

489 Exemption for income from estates in administration

(1) If a charitable company is liable for any corporation tax charged under section 934 of CTA 2009 (charge to tax on estate income), the estate income is not taken into account in calculating total profits.

(2) Subsection (1) applies so far as the estate income is applied to the purposes of the charitable company only.

(3) The exemption under subsection (1) requires a claim.

(4) In this section 'estate income' has the same meaning as in Chapter 3 of Part 10 of CTA 2009 (see section 934 of that Act).

Restrictions on exemptions

492 Restrictions on exemptions

(1) This section applies if a charitable company has a non-exempt amount for an accounting period (see section 493).

(2) The exemptions mentioned in subsection (3) do not apply, and are treated as never having applied, to so much of any income of the charitable company for the accounting period as is attributed under section 494 to the non-exempt amount.

(3) Those exemptions are-

(a) the exemptions under this Part, and

(b) the exemption under regulation 31(1) of the Offshore Funds (Tax) Regulations 2009 (SI 2009/3001) (exemption from corporation tax in respect of certain offshore income gains).

(4) Section 256(4) of TCGA 1992 contains corresponding restrictions which apply in relation to section 256(1) of that Act (gains accruing to charities not to be chargeable gains).

493 The non-exempt amount

(1) A charitable company has a non-exempt amount for an accounting period if it has-

(a) non-charitable expenditure for the period (amount A), and

(b) attributable income and gains for the period (amount B).

(2) The non-exempt amount for the accounting period is-

(a) amount A, or

(b) if less, amount B.

(3) For the purposes of this Part-

(a) a charitable company's 'attributable income' for an accounting period is the charitable company's income for the period that is exempt from corporation tax as a result of any of the exemptions mentioned in section 492(3),

(b) a charitable company's 'attributable gains' for an accounting period are any gains accruing to the charitable company in the period that as a result of section 256(1) of TCGA 1992 are not chargeable gains, and

(c) a charitable company's 'attributable income and gains' for an accounting period is the sum of its attributable income for the period and its attributable gains for the period.

(4) In applying subsection (3)(a) ignore any restrictions on the exemptions under this Part which result from section 492(2).

(5) In applying subsection (3)(b) ignore any restriction on the exemption under section 256(1) of TCGA 1992 which results from section 256(4) of that Act.

Accordingly, supplying goods and services to charitable organisations will be exempt from income tax and corporation tax. Also, tax paid on donations may be reclaimed, provided that the donation is used exclusively for charitable purposes. Investment income and income from regular sources will also be exempt from taxation. Income received from trading activities will be subject to tax, although again certain exemptions are permitted. Furthermore it may be possible to separate the trading activities of the organisation from its charitable activities. Accordingly, the non-charitable section will pay tax on income made from sales, but may then donate the receipts to the charitable section, and the charity may then reclaim the tax that has been paid. Rental income will be exempt from tax, and charities will also be exempted from capital gains tax and stamp duty land tax. Charities will also receive an 80 per cent exemption from the amount of rates payable. The amount of value added tax (VAT) payable will also be limited in that relief from VAT may be available. The taxation implications for other forms of trust are significantly more onerous, and there are considerable advantages to acquiring charitable status wherever this is possible.

EXTRACT

Annex 1 Tax Exemptions for Charities

I.1 Introduction

I.1.1 Charities may claim exemption from tax on most forms of income and capital gains, if they are applied to charitable purposes.

I.1.2 Once a body has been accepted as being a charity for tax purposes, it normally retains its charitable status until such time as it ceases to exist either in its original form or altogether.

I.2 Main Statutory Exemption

I.2.1 The main statutory exemptions from tax for the income of a charity are contained:

- For charitable companies: – in sections 466 to 493 Corporation Tax Act 2010 (CTA 2010).
- For charitable trusts: – in sections 521 to 536 Income Tax Act 2007 (ITA 2007)

These exemptions relate to: –

- income from land (paragraphs I.3.1 to I.3.3)
- Bank interest, Gift Aid payments and other annual payments (paragraphs I.4.1 to I.4.3)
- trading income (paragraphs I.5.1 to I.5.2)

All charitable tax exemptions are subject to the condition that income is applied to charitable purposes.

I.3 Income from land

I.3.1 The profits of a property business carried on by a charitable company are chargeable to tax under section 209 Corporation Tax Act 2009 (CTA 2009). Section 485 CTA 2010 provides an exemption from tax for the income of a property business.

I.3.2 The profits of a property business carried on by a charitable trust are chargeable to tax under Parts 2 and 3 Income Tax (Trading and Other Income) Act 2005 (ITTOIA 2005). Section 531 ITA 2007 provides an exemption from tax for the income of a property business.

I.3.3 The exemption applies to income from property businesses both in the UK and overseas.

I.3.4 The exemptions do not apply to profits from buying and selling land or profits arising from the development of land.

I.3.5 If a charity is buying and selling land or property this may be treated as non-primary purpose trading. The profits of such a trade will be chargeable to tax under section 2 CTA 2009 or section 5 ITTOIA 2005. The detailed guidance on trading is at BIM20051 – Trade: general: overview.

I.3.6 If a charity sells land that has been held as an asset any gain will normally be a capital gain. Section 256 Taxation of Chargeable Gains Act 1992 (TCGA 1992) provides an exemption for capital gains provided the gain is applied to charitable purposes only. However, if a contract for the sale of land includes a provision for the charity to share in future profits from the development of that land any such profits received will not be exempt; they will be chargeable under Part 18 CTA 2010 (section 815 et seq) or section 755 ITA 2007. The detailed guidance on this is at BIM60300 – Land transactions.

I.4 Interest and other annual payments

I.4.1 Sections 475/476, 486 & 488 CTA 2010 and sections 532 & 534 ITA 2007 provide for an exemption to charitable companies and charitable trusts respectively in respect of:

- all interest, Gift Aid donations and other annual payments,
- any non-UK equivalent of such income which would otherwise fall to be assessed as foreign income.

I.4.2 Any payment from one charity to another charity is taxable income in the hands of the recipient charity – section 523 ITA 2007 (trusts) and section 474 CTA 2010 (companies) refer. But it is exempt from tax if it is applied for charitable purposes only.

I.4.3 Section 488 CTA 20101988 and Section 536 ITA 2007 provide for exemption from tax in respect of dividends and other distributions received by charitable companies and charitable trusts respectively from companies not resident in the UK.

I.5 Trading income

I.5.1 A charity is exempt from tax on the profits of any trade carried on in the United Kingdom or elsewhere provided its income is applied solely to charitable purposes and which is either

- exercised in the course of the actual carrying out of a primary purpose of the charity (section 478 CTA 2010 for charitable companies and section 524 ITA 2007 for charitable trusts)
- mainly carried out by beneficiaries of the charity (section 478 CTA 2010 and section 524 ITA 2007)
- a non-primary purpose trade the turnover of which falls below certain limits (section 480 CTA 2010 and section 526 ITA 2007)
- the profits arise from certain lotteries

I.5.2 The exemption from tax of a charity's trading income is considered in detail in Annex IV.

I.6 Capital Gains tax

I.6.1 Section 256 TCGA 1992 provides an exemption from tax on capital gains, provided the gains are applied for charitable purposes.

I.7 Foreign tax

I.7.1 Occasionally charities seeking to claim exemption from foreign tax from an overseas tax authority may request confirmation that they are subject to UK tax. Certain Double Taxation

Agreements provide that a resident of the UK will be entitled to exemption or relief from the foreign tax on certain types of income only if he or she is subject to tax on that income in the United Kingdom.

I.7.2 Charities should be aware that a person is not regarded as subject to tax in the UK if the income in question is statutorily exempt from tax.

I.8 Fund-raising events

I.8.1 Exemption from tax on the profits from fund-raising events is provided as follows:

- Section 483 CTA 2010 for charitable companies
- Section 529 ITA 2007 for charitable trusts.

Source: http://www.hmrc.gov.uk/charities/guidance-notes/annex1/annex_i.htm. Site accessed 17 January 2014.

Perpetuities

Although the trust is a useful and versatile tool, the separation of legal and equitable ownership does inhibit the utility of an asset. Accordingly, the law against perpetuities exists – in the form of the Perpetuities and Accumulations Act 2009[6] – in order to prevent the existence of infinite trusts. A trust of perpetual duration is therefore void. However, an exception to this rule exists in the case of charities, in relation to which a trust may exist in perpetuity.

Nevertheless, charities are subject to the ordinary law of trusts as regards the issue of remoteness of vesting. The Perpetuities and Accumulations Act 2009, s.5 prevents a gift to a trust (including charitable trusts) from vesting in the trust more than 125 years after its creation. For example, a settlor might create a trust that confers successive life interests (on children and grandchildren), and thereafter to be held on trust for some other purpose – such as a charitable cause. This would mean that the property is held on trust for an excessive period, and it is for this reason that the Perpetuities and Accumulations Act 2009 seeks to prevent this. In relation to charities however, there is an exception to this rule. This is called a gift over. A gift over arises where a testator directs that the trust fund, initially conferred on one beneficiary, is to be given to another beneficiary on the occurrence of a specified event. Gifts over of this nature are usually only permitted within the perpetuity period. However, where the initial beneficiary is a charity, the testator may direct that on the occurrence of a specific event – such as the charity ceasing to exist – the trust fund is to be given to a second charity. In this situation, the gift over may vest outside the perpetuity period, as is provided by the Perpetuities and Accumulations Act 2009 s.2(2). This exception does not apply however in relation to a private trust followed by a gift over to a charity, or to a charitable trust followed by a gift over to a private trust.

Charities are not exempted from the rule against accumulations however. Therefore s.14(3) Perpetuities and Accumulations Act 2009 prevents trustees from accumulating income for longer than the perpetuity period of 125 years. In essence, the rule exists in order to prevent the trust from being invested on an indefinite basis. Accordingly, as with a non-charitable trust, the fund must be paid to the beneficiaries within the perpetuity period.

[6] (2009 c.18).

The cy-près doctrine

One advantage of a charitable trust over other forms of trust is the cy-près doctrine. Cy-près (pronounced see-pray) comes from Anglo-French, and means 'as near as practicable.' In essence, therefore, the cy-près doctrine ensures that a gift to a charity does not fail where the intended benefit cannot be conferred – the fund is used for the nearest practicable purpose to the one intended in accordance with s.62 Charities Act 2011. The purpose of the cy-près doctrine is to allow the gift to be construed as being a gift for a charity with a similar purpose, with the result that the trust is saved from failure. The cy-près doctrine may be used:

- where a gift has been given to an unspecified charitable purpose, such as where a trust is created that simply states that it is for the benefit of the public;
- where a charity has ceased to exist;
- where a gift has been given to a specific, but mis-described, institution.

The cy-près doctrine is used in two situations. Its broadest application is in the context of trusts created usually by will, where the beneficiary has either never existed or has ceased to exist. Such a situation is unlikely to occur with an *inter vivos* trust, in that an attempt to give money to a non-existent charity would be unsuccessful, and no trust would have been created. Nevertheless, a cy-près scheme could potentially arise from an *inter vivos* trust where for example funds have been raised for a charity that goes into liquidation.

However, a cy-près scheme may also be applicable where an existing charity has fulfilled its purpose. For example, where funds are raised in response to a particular situation such as a natural disaster, or for a particular purpose, such as the repair of a church, there will come a time when the charity will have fulfilled its purposes, and will no longer need to exist. In such situations, it may be possible to devise a cy-près scheme in order that the remaining funds may be applied for a similar purpose, such as supporting other victims of another natural disaster. A common example is where funds have been raised by a community in order to provide treatment for a child with a serious illness. Often people's generosity exceeds the cost of the treatment, or, more unfortunately, the child dies before the treatment can be administered. In those situations, the fund is used to provide treatment for another child with a similar condition. What follows therefore is how the cy-près rules will be applied in relation to the different types of situation that may give rise to a cy-près scheme.

Gifts manifesting only a general intention to benefit charity

Where a gift has been given to an unspecified charitable purpose, the Crown, the Court or the Charity Commission's role will be to define how the trust fund will be used. The trustees cannot apply the fund cy-près without the cy-près scheme having been approved either by the High Court or by the Charity Commission. When deciding on whether to approve a cy-près scheme, the High Court or the Charity Commission will have regard to any indications as to how the trust fund is or is not to be used by considering the testator's interests, viewpoints or other clauses contained in the testator's will. For example, if the testator left other legacies to animal charities, then it may be considered that a charitable organisation promoting the welfare of animals might be an appropriate organisation to receive the fund. On the other hand, if the testator had no interest in religion, or was an atheist, then it may be considered that he or she did not intend for the trust fund to be

used to benefit a charity for the advancement of religion. However, where no intention can be discerned, then the trust fund will be distributed in accordance with the court's discretion.

EXTRACT

In Re Wilson (Twentyman v Simpson) [1913] 1 Ch 314

Case facts

The testator wrote a will, which contained the following clause: 'But if all die without issue I give and bequeath the whole principal of their fortunes, the interest to be given to a schoolmaster as a part of his salary. The school and his house to be erected by voluntary subscriptions from the landowners and proprietors of the parish of Aikton, and the school and house to be placed on a hill near to the gate that divided Biglands and Wampools Commons (now enclosed). The master to teach five days in a week and six hours each day, Saturday and Sunday excepted, to be able to instruct the pupils in Latin and Greek and all the elementary parts of mathematics, both pure and mixed, the Wampool scholars to go free, the rest to pay the master 2s. 6d. each at Midsummer and at Christmas as quarter pence.'

Parker J

For the purposes of this case I think the authorities must be divided into two classes. First of all, we have a class of cases where, in form, the gift is given for a particular charitable purpose, but it is possible, taking the will as a whole, to say that, notwithstanding the form of the gift, the paramount intention, according to the true construction of the will, is to give the property in the first instance for a general charitable purpose rather than a particular charitable purpose, and to graft on to the general gift a direction as to the desires or intentions of the testator as to the manner in which the general gift is to be carried into effect. In that case, though it is impossible to carry out the precise directions, on ordinary principles the gift for the general charitable purpose will remain and be perfectly good, and the Court, by virtue of its administrative jurisdiction, can direct a scheme as to how it is to be carried out. In fact the will will be read as though the particular direction had not been in the will at all, but there had been simply a general direction as to the application of the fund for the general charitable purpose in question. Then there is the second class of cases, where, on the true construction of the will, no such paramount general intention can be inferred, and where the gift, being in form a particular gift, – a gift for a particular purpose – and it being impossible to carry out that particular purpose, the whole gift is held to fail. In my opinion, the question whether a particular case falls within one of those classes of cases or within the other is simply a question of the construction of a particular instrument.

Outcome

Ultimately, Parker J concluded that the trust was too specific in its purposes, and could not therefore be applied for a general charitable intention.

In the case of *Biscoe v Jackson* (1886) 35 Ch D 460, for example, the testatrix left a sum of money in her will in order to establish a soup kitchen in Shoreditch. Although this was a specific purpose, and one that ultimately could not be fulfilled, it was found that she had manifested a general intention to benefit the poor of Shoreditch, and therefore the fund could be applied cy-près.

Charitable trusts that have fulfilled their objectives

Where a charitable trust has fulfilled its intended purpose, then the sum left over will usually be regarded as resulting back to the residuary estate of the settlor, and will be distributed accordingly. Often, the testator will have specified what should happen to the trust fund in this situation. This is known as a gift over. If the gift over is to a non-charitable cause, then it will fail if it falls outside the perpetuity period in operation when the trust was created (as discussed in Chapter 9). However, if the gift over is to another charity, the trust will continue to be valid, even if the trust comes into effect after the perpetuity period has lapsed.

Trusts to specific charities

The third possibility is that a gift is given to a specific charity that has either never existed or has ceased to exist.

A charity that ceases to exist after the death of the settlor

The situation where the charity ceases to exist after the settlor's death is comparatively straightforward. In such situations, the trust fund will be applied for the benefit of a charity that has similar objectives. For example, if the trust is established for the purpose of conferring research scholarships, and the institution at which the scholarships are to be awarded ceases to exist, the fund may be applied for the purposes of scholarships at another similar institution, in a similar locality. Accordingly, in the case of *Re Slevin* [1891] 2 Ch 236, the trust fund, once it had been given for a charitable purpose, could then be used for another charitable purpose once the orphanage had closed.

A charity that has ceased to exist before the death of the testator

More problematic is where the charity ceased to exist before the death of the testator. On the face of it, such a trust would fail because of an uncertainty of objects. Thus it is seen that the requirement that the trust should have certainty as to its objects is not entirely redundant in the context of charities, because it is difficult to identify a general charitable intention when a specific charitable purpose has been identified. In the case of *Re Harwood*,[7] Farwell J explains that it would be very difficult to discover a general charitable intention in such circumstances.

> I do not propose to decide that it can never be possible for the Court to hold that there is a general charitable intent in a case where the charity named in the will once existed but ceased to exist before the death. Without deciding that, it is enough for me to say that, where the testator selects as the object of his bounty a particular charity and shows in the will itself some care to identify the particular society which he desires to benefit, the difficulty of finding any general charitable intent in such case if the named society once existed, but ceased to exist before the death of the testator, is very great. Here the testatrix has gone out of her way to identify the object of her bounty. In this particular case she has identified it as being 'the Wisbech Peace Society Cambridge (which is a branch of the London Peace Society).' Under those circumstances, I do not think it is open to me to hold that there is in this case any such general charitable intent as to allow the application of the cy-près doctrine.

[7] *In Re Harwood, Coleman v Innes* [1936] Ch 285 at p.287.

However, the courts have also shown considerable ingenuity in their construction of gifts to charity, and have, on occasion, been willing to construe gifts to specific charities that have ceased to exist as being the manifestation of a more general charitable intention. Much will therefore depend on how the courts construe the words used, and how they interpret the manifestation of the testator's intention. For example in the case of *Re Satterthwaite*,[8] the testatrix's will provided legacies for a number of organisations concerned with the welfare of animals. Most of these organisations were valid charities that were still in existence at the time of the testatrix's death. However, one of the organisations was not a charity but rather, the business name of a veterinary surgeon. The Court of Appeal accepted in this case that the testatrix's intention was to benefit animal welfare charities, and that she had no intention of leaving any legacy to the veterinary practice. Russell LJ explains:

> If a particular mode of charitable application is incapable of being performed as such, but it can be discerned from his will that the testator has a charitable intention (commonly referred to as a general charitable intention) which transcends the particular mode of application indicated, the court has jurisdiction to direct application of the bequest to charitable purposes cy près. Here I have no doubt from the nature of the other dispositions by this testatrix of her residuary estate that a general intention can be discerned in favour of charity through the medium of kindness to animals.[9]

Accordingly, the trust was applied cy-près, and the fund was given to a nearby animal hospital that did have charitable status. Another example that may be applicable here is the case of *Biscoe v Jackson*.[10] Here a trust fund was created for the purposes of establishing a soup kitchen and a cottage hospital in Shoreditch. When this purpose could not be fulfilled, it was likely that the trust would fail. However, the court permitted a cy-près scheme on the basis that the broader intention of the testator was to confer a benefit on the poor of Shoreditch, and that the trust should not fail simply because the objective could not be fulfilled in the way that the testator intended. It may be possible, even where a charitable organisation has ceased to exist, to show that a more general charitable intention has been manifested and to apply the fund cy-près on that basis, particularly where there is evidence from the other legacies left by the testator of an intention to benefit charity.

EXTRACT

Re Satterthwaite's Will Trusts [1966] 1 All ER 919

Case facts

The testatrix wrote a will leaving the residue of her estate divided between nine animal welfare charities selected from the telephone directory. However, one of the organisations listed was not in fact a charity but rather a private veterinary's practice.

[8] [1966] 1 All ER 919.
[9] Per Russell LJ at p.925.
[10] (1887) 35 Ch D 460.

Russell LJ

In the present case there is not the slightest indication that the testatrix, when defining the object of her bounty as 'the London Animal Hospital', had any knowledge of the third defendant's establishment, let alone that it was an enterprise conducted for private profit. If, therefore, the bequest pointed to an activity established in South Lambeth Road, because blindly selected from, for example, the telephone directory, this can confer on the third defendant no right to assert either that the legatee named is merely a label for the third defendant, or (which would come to the same thing) that the money must be paid to the account of a business concern of which he is the sole owner. Accordingly in my judgment the third defendant's claim fails . . . In addition, however, the bequest here is the fourth of nine: and none of the other eight displays a benevolence towards individuals: on the contrary they display a benevolence towards animals . . . If the bequest cannot be a bequest to the third defendant personally (directly or through his business) what is the result? Plowman J has held that the language points to the animals' hospital run by the Blue Cross (and formerly by Our Dumb Friends League) in Hugh Street, Victoria, not far from Ebury Street where the testatrix lived, but the other side of the railway, basing himself on the affidavits of Mr Carpmael and Miss de Luzy. The former stated barely that since opening in 1906 the Hugh Street enterprise 'has been known as 'the Animals' Hospital' or 'the London Animals' Hospital'. Miss de Luzy more sweepingly said that from 1908 to 1952 (her employment by Our Dumb Friends League) it 'was generally and popularly known as the London Animals' Hospital'. Such evidence, without the slightest condescension to detail, is highly unsatisfactory on this sort of point, more particularly when the Blue Cross brochure (which was exhibited) commonly refers to the Hugh Street activity as 'the Victoria Hospital' or 'our Victoria Hospital', an appellation not mentioned by either deponent. Nothing is said of where it was known as the London Animals' Hospital, or why it should be so distinguished. There is no evidence that the testatrix contributed to that activity or otherwise showed any interest in or knowledge of it, and, if she ever walked past it, it would have been strange had she used the appellation 'London' instead of something more localised. Moreover, at the time of the will the facade had at its centre 'Our Dumb Friends League', the on either side being 'Animals' and 'Hospital' as, so to speak, supporters . . .

What is the result in law of this? I have already indicated that she is to be taken as intending to benefit a charitable activity; but the organisation picked by name was not such. Prima facie, therefore, the bequest would fail and there would be a lapse, with the result in this case in fact–owing to the incidence of liabilities and death duties–of mere relief of other residuary objects. My assumption, however, is that the testatrix was pointing to a particular charitable application of this one-ninth of residue. If a particular mode of charitable application is incapable of being performed as such, but it can be discerned from his will that the testator has a charitable intention (commonly referred to as a general charitable intention) which transcends the particular mode of application indicated, the court has jurisdiction to direct application of the bequest to charitable purposes cy près. Here I have no doubt from the nature of the other dispositions by this testatrix of her residuary estate that a general intention can be discerned in favour of charity through the medium of kindness to animals. I am not in any way deterred from this conclusion by the fact that one-ninth of residue was given to an anti-vivisection society which in law–unknown to the average testator–is not charitable. Accordingly in my judgment the correct answer in this case is that the one-ninth share in question is not payable to the third defendant but should be applied cy près and to that end the matter should be referred to chambers for settlement of a scheme.

A charity that has never existed

It is generally thought to be easier to show a general charitable intention where the organisation never existed, such as where a charity is misdescribed, because as Buckley J explains in *In Re Davis*,[11] the law favours charity, and will find a charitable intention wherever that is possible. The contrast between the two situations is displayed in the case of *In Re Spence* [1979] Ch 483.

EXTRACT

In Re Spence [1979] Ch 483

Case facts

The testatrix left the residue of her estate to The Blind Home, Scott Street, Keighley and the Old Folks Home at Hillworth Lodge, Keighley for the benefit of the patients. No institution by the name of 'The Blind Home' had ever existed at Keighley but a charity known as 'The Keighley and District Association for the Blind' had been in existence since 1907. The association had changed its name three times and had been running a blind home at Scott Street for over 25 years. There had been no other premises or association connected with the blind in Keighley, but the premises of the association were quite often called the 'Blind Home'. The association also carried on a home for the blind at Bingley.

Hillworth Lodge was built as a workhouse, and had then become an old people's home. It had been closed down completely some eight years before the testator's death, and had been converted into offices, while the elderly had been moved to other old people's homes.

Sir Robert Megarry VC

I shall first consider the gift to 'The Blind Home, Scott Street, Keighley . . . for the benefit of the patients.' I think it is clear that these last six words apply to the gift to the Blind Home as they apply to the gift to the Old Folks Home; and nobody contended to the contrary. The question is whether this gift carries a moiety of residue to the Keighley and District Association for the Blind and, if so, on what terms. That charity was founded in 1907 and, over the years, it has changed its name thrice. It has borne its present name for nearly 20 years, and is at present governed by a trust deed dated October 25, 1963. For over 25 years it has been running a blind home at 31 Scott Street, Keighley, which provides permanent accommodation for the blind in Keighley and district. Since 1907 there have been no other premises or associations connected with the blind in Keighley. The premises in Scott Street are often called 'The Blind Home'; and a memorandum of the appointment of new trustees made on June 9, 1970, refers to the meeting for that purpose held at 'The Blind Home Scott Street Keighley.' Other names are used. A board on the building calls it 'The Keighley and District Home for the Blind,' and a brochure in evidence calls it 'Keighley Home for the Blind.' It seems clear beyond a peradventure that the language of the will fits the home run by the charity at these premises.

In those circumstances, Mr. Gidley Scott felt unable to advance any argument that the gift of this moiety failed and passed as on intestacy; and in this I think he was right. That, however,

[11] *In re Davis, Hannen v Hillyer* [1902] 1 Ch 876.

does not dispose of the matter, since the charity also carries on a home for the blind at Bingley, and may of course expend some or all of its funds on this or other purposes within its objects. There is therefore the question whether the moiety should go to the charity as an accretion to its endowment, and so be capable of being employed on any of its activities, or whether it is to be confined to the particular part of the charity's activities that are carried on at The Blind Home in Scott Street, Keighley. I confess that but for the decision of the Court of Appeal in *In re Lucas* [1948] Ch. 424, I should have had little hesitation in resolving this question in the latter and narrower sense, confining the moiety to the particular Blind Home in Scott Street, Keighley. The question for me is whether on the case before me there ought to be a similar result, so that the moiety of residue would go to the Keighley and District Association for the Blind as an addition to its endowment generally, and would not be confined to the Blind Home in Scott Street, Keighley, carried on by the Association. . . .

Mr. McDonnell submitted that there were two substantial points of distinction between the present case and In re Lucas. First, the words of the will fitted the Blind Home far better than they fitted the Association. Indeed, although the Blind Home was from time to time described by different names, all the names used included both 'Blind' and 'Home': and, as I have mentioned, the appointment of new trustees in June 1970 uses the name 'The Blind Home Scott Street Keighley,' which is the precise expression used in the will. The title of the charity, 'The Keighley and District Association for the Blind,' is very different. True, it has the word 'Blind' in common with the title used in the will. There is also the word 'Keighley,' though this is used adjectively and not as part of the address. But otherwise there is nothing in common. In particular, there is not the use of the word 'Home' in both titles which the Court of Appeal in *In re Lucas* said was present in that case; and I think the words 'Home' and 'Association' are different in a real and significant sense.

Second, in the case before me, there are the words 'for the benefit of the patients' which follow and govern the expression 'The Blind Home Scott Street Keighley.' In *In re Lucas* there was no counterpart to this. Indeed, the absence of any reference to the upkeep or maintenance of the home in that case was, as I have indicated, one of the grounds on which the decision was based. Here, there is no reference to upkeep or maintenance as such: but I think 'patients' must mean 'patients of the Blind Home,' and the upkeep and maintenance of the home is an obvious means of providing a benefit for the patients in it.

In my judgment both these distinctions are valid and substantial. It therefore seems to me that the case before me is distinguishable from *In re Lucas*, so far as I have correctly understood that case. The testatrix was making provision for the benefit of the patients for the time being at a particular home, namely, the home usually known as The Blind Home at Scott Street, Keighley. She was giving the money not to augment generally the endowment of the charity which runs that home, with the consequence that the money might be used for purposes other than the benefit of the patients at that home, but was giving the money so that it would be used exclusively for the benefit of those patients. The only way in which this can conveniently be done is to give the money to the charity but to confine its use to use for the benefit of the patients for the time being at the home. That, I think, requires a scheme; but I see no need to direct that a scheme should be settled in chambers. Instead, I think that I can follow the convenient course taken by Goff J. in *In re Finger's Will Trusts* [1972] Ch. 286, 300. I shall therefore order by way of scheme (the Attorney-General not objecting) that the moiety be paid to the proper officer of the charity to be held on trust to apply it for the benefit of the patients for the time being of the home known as The Blind Home, Scott Street, Keighley.

I now turn to the other moiety of residue, given by the will to 'the Old Folks Home at Hillworth Lodge Keighley for the benefit of the patients.' Hillworth Lodge was built as a workhouse in 1858. Shortly before the outbreak of war in 1939 the West Riding County Council, in whom it had become vested, closed it down: but during the war it was used to house what were

generally but inelegantly called 'evacuees.' In 1948 it became an aged persons' home under the National Assistance Act 1948, and it continued as such until on January 28, 1971, it was finally closed down. There had been between 120 and 140 residents in it as late as 1969, but the numbers were then progressively run down, until in January 1971, just before it closed, only 10 residents were left; and these were transferred to another establishment in Pudsey. The aged of the area had over the years been increasingly accommodated in purpose-designed old people's homes which provided better accommodation for the aged than could the old workhouse, despite many improvements to it. Since the building ceased to house old people it has been used as divisional social services offices.

When the testatrix made her will in 1968 the building was accordingly still in use as an old people's home run by the local authority in accordance with their duty under the National Assistance Act 1948. As an old people's home it had no assets of its own, and residents contributed towards their maintenance in accordance with the Ministry of Social Security Act 1966, Part III. When the testatrix died on May 30, 1972, the building was no longer used as an old people's home, and was being used, or was soon to be used, as offices. The home had been run neither as nor by a charity. It formerly provided homes for those living in a large area of the West Riding, and not merely Keighley; and it has not been replaced by any one home. Instead, there are many old people's homes serving the area.

Now without looking at the authorities, I would have said that this was a fairly plain case of a will which made a gift for a particular purpose in fairly specific terms. The gift was for the benefit of the patients at a particular home, namely, the Old Folks Home at Hillworth Lodge, Keighley. At the date of the will there were patients at that home. When the testatrix died, there was no longer any home there, but offices instead; and so there were no longer any patients there, or any possibility of them. The gift was a gift for a charitable purpose which at the date of the will was capable of accomplishment and at the date of death was not. Prima facie, therefore, the gift fails unless a general charitable intention has been manifested so that the property can be applied cy-près. Buttressed by authority, Mr. Gidley Scott contended that the court would be slow to find a general charitable intention where the object of the gift is defined with some particularity, as it was here.

Outcome

The trust for the blind home could be applied cy-près, but the trust for the old people's home could not.

In the case of *Re Harwood* [1936] Ch 285 it was considered that although an organisation called the Peace Society of Belfast *may* have existed at some point, the testatrix had manifested a general intention to benefit a charity promoting peace, and the gift could be applied cy-près and given to the Belfast branch of the League of Nations. The distinction is drawn here between an intention to benefit a specific organisation, which fails if the organisation has ceased to exist, and a situation where it is not clear that the testatrix intended to confer a benefit on a particular organisation, although it was clear that there was an intention to benefit a particular purpose. Accordingly, where the court is able to identify a general charitable purpose, it will be easier for it to conclude that a cy-près scheme will be appropriate.

Cy-près: some conditions

Nevertheless, there are some caveats to the cy-près doctrine. In order for a cy-près scheme to be applied, it is necessary for the trust to be exclusively charitable. Accordingly

in *Chichester Diocesan Fund v Simpson* [1944] AC 341, a fund that had been left by the settlor to 'a charitable or benevolent' fund could not be applied cy-près because a benevolent fund was not necessarily charitable, and therefore the legacy was not regarded as having been given for an exclusively charitable purpose. Lord Macmillan explains:

> In construing a will it is proper to read the instrument as a whole. By doing so it may sometimes be found that a testator has used a word or a phrase in a sense of his own, different from its ordinary connotation. If a testator were to make a bequest in favour of benevolent objects, adding 'by which I mean charitable objects,' the bequest might well be held to be valid. In the present instance, however, I cannot find any context either in the words of the bequest itself or elsewhere in the will which would justify imparting to the testator's use of the word 'benevolent' any other than its ordinary wide signification. If the testator had written 'charitable and benevolent' instead of 'charitable or benevolent' the bequest would, on the authorities, have been sustained, for it would then have been read as in favour of such benevolent objects as are charitable or such charitable objects as are benevolent, charity in either way predominating. But again I find no warrant for reading conjunctively two words which the testator has expressly disjoined.

Yet, the courts have occasionally circumvented this. In *Guild v IRC* [1992] 2 AC 310, a clause detailing that the fund should be for 'some other purpose' was accepted as being one that could justify a cy-près scheme, while in *Re Clarke* [1923] 2 Ch 407 the court apportioned the fund between the charitable and the non-charitable purposes, with the result that the portion that was deemed to be charitable could be applied cy-près, while that which was not charitable failed for a lack of certainty of objects.

In these three chapters what has been demonstrated is the generally positive approach adopted by the legal system to the recognition of charities. A broad range of activities may be regarded as being charitable purposes, and a benefit to the public may be manifested in a number of ways. Once these elements have been demonstrated, there are considerable advantages – coupled with responsibilities – attached to charitable status. Accordingly, it is an extremely interesting and engaging area of law, about which much has been written, especially as the law appears to contain a number of extremely interesting anomalies and inconsistencies.

For example, it may be argued that much of the law on charities requires courts to make value judgments on whether the activity is a charitable purpose. For example, in relation to education, there is considerable subjectivity regarding what has educational value and what does not. It may be the case for example that George Bernard Shaw's 40-letter alphabet may have considerable educational value as it gives a reader the scope to distinguish between the 'a' sound in cat from the 'a' sound in base in a way that the 26-letter English alphabet does not. Similarly, religious charities may be seen to favour established and acceptable religions over other belief-systems and forms of expression.

Other interesting areas include the cy-près doctrine, and the courts' differing approaches towards identifying when a gift should be applied cy-près.

A further area is the increased governmental intervention in charitable trusts – or perhaps a reversion to government intervention in charitable trusts. There is therefore considerable scope to address whether charities are becoming over-regulated, and what the implications of this may be. The topic contains considerable potential for further exploration in a dissertation or an extended essay.

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The trust as a solution to a legal problem

Chapter outline

This chapter will cover:

- Resulting trusts
- Trusts presumed from conduct
- Constructive trusts
- Dishonest misappropriation creating a constructive trust
- Proprietary estoppel
- The *Pallant v Morgan* equity
- The remedial constructive trust
- The future of the constructive trust.

Chapter summary

This chapter may be useful for assessments and assignments on:

- Charities
- Certainty of objects
- Regulation of charities.

Further reading

Garton, J. (2007) 'Justifying the cy-près doctrine' 21(3) *Trusts Law International* 134.

Morris, C. (2010) 'The First-tier Tribunal (Charity): enhanced access to justice for charities or a case of David versus Goliath?' 29(4) *Civil Justice Quarterly* 491.

Introduction

As was demonstrated earlier (in Chapter 6), trusts may either be expressly created or they may arise by implication. An express trust is a trust that is deliberately created by the settlor. Therefore intentional *inter vivos* trusts are forms of express trusts, as are wills. However, a trust may also arise by implication either because the trustee has become the owner of property to which he or she is aware that he or she is not entitled, or because the mutual conduct of the trustee and the beneficiary indicates that the relationship between them is a trust (as is seen in Chapter 14 in relation to trusts of the family home). In this chapter, the different types and usages of the implied trust will be explained, along with the ways in which the general principles pertaining to trusts are modified in relation to implied trusts. In essence, the trust is imposed as a solution to a problem created by the law, and ensures that a person is not entitled to keep what is not rightfully theirs. Because the trust is implied, it is exempt from the usual formalities, such as the requirement of writing seen in relation to a trust of land.[1]

Trust property resulting back to the settlor

This is an example of an automatic resulting trust, as defined by Megarry J in *Re Vandervell (No 2)* [1974] Ch 269. The settlor transfers property to the trustee, but the trust fails for some reason, such as where there is a failure to identify the subject matter or the objects of the trust.

Clearly, the trustee cannot retain the property for him- or herself, as this would constitute a breach of trust. Therefore the trust property must return to the only place it can – to the settlor, or if the settlor has died, to the settlor's estate under what is known as a resulting trust. In fact, this may be the one thing that the settlor absolutely did not intend to happen, in that in creating an express trust, the settlor's intention is to transfer the trust property. However, a subsidiary intention is to make the recipient a trustee rather than the donee of a gift. Accordingly, there are many situations where a resulting trust will arise, including, where the trust property has not been defined with sufficient precision so that it is clear to the trustees what each beneficiary should receive – as in the case of *Boyce v Boyce* (1849) 60 ER 549 where one beneficiary was to select which house she wished to receive, and the other being given the house not chosen. Here, the trust failed for uncertainty of objects as regards the first beneficiary, in that she had died, and therefore there was no one to whom the trustees could give the property. It also failed for uncertainty of subject matter as regards the second beneficiary, as it was not clear which house she was to be given in the absence of a selection being made by the first beneficiary.

Another example of a resulting trust is where the settlor has failed to identify beneficiaries at all, or the beneficiaries refuse the gift, or they die before the settlor. Again, there has been a transfer of the trust property to the trustees but no one who may benefit from it. A resulting trust will also arise where a beneficiary witnesses the will of the testator. In this situation, s.15 Wills Act 1837 provides that the witness cannot benefit from the legacy, and therefore again the trust will fail and the trust property will revert back to the settlor's estate.

In a commercial context, a trust will fail in situations where an intermediary is employed by the seller and the buyer to receive the subject matter of the contract pending

[1] Law of Property Act 1925, s.53(2).

transfer, and to exchange the elements once both the goods and the consideration have been received. However, if the seller supplies the goods to the intermediary but the buyer fails to provide the payment, then the goods will be held on a resulting trust for the seller.

Resulting trust presumed from the conduct of the settlor/beneficiary

A presumed resulting trust[2] occurs where the settlor/beneficiary has contributed to the cost of buying some asset but vested in the name of another. There is a presumption here that the person in whose name the property is vested will hold it on trust for the benefit of the settlor/beneficiary. Therefore if Donna and Russ contribute equally to the purchase price of a house which is registered in Russ's name, Russ is presumed to own the house on trust for himself and Donna. The trust arises because it is presumed that Donna would not have contributed in this way if she was not intending to obtain a share of the proceeds of sale when the house is sold. Such a trust may be useful if Donna either does not wish to be registered as the proprietor of the land (for example where Donna wishes to cohabit with Russ after having separated from, but not divorced, from her spouse, and is therefore reluctant to have the house in which she cohabits with Russ to be included in the calculations for the financial settlement on divorce made under the Matrimonial Causes Act 1973)[3] or cannot be registered as a proprietor (by virtue of being below the age of 18 for example). This is summarised very clearly in the judgment of Lord Upjohn in *Pettitt v Pettitt* [1970] AC 777 at p812:

> in the absence of evidence to the contrary if the property be conveyed into the name of a stranger he will hold it as trustee for the person putting up the purchase money and if the purchase money has been provided by two or more persons the property is held for those persons in proportion to the purchase money that they have provided.

Nevertheless, the resulting trust is only a presumption, and can therefore be rebutted where there is evidence to the contrary, such as for example, where Donna's contribution was by way of either a gift or a loan to Russ.

Constructive trusts

Whereas resulting trusts look broadly at what the settlor intended – namely that the person to whom the property has been transferred should be a trustee rather than an absolute owner, a constructive trust focuses much more extensively on whether it would be unconscionable for a person to retain the property for him- or herself. This is not necessarily a different focus – after all, where a trust fails for a lack of certainty of objects, it is unconscionable for the trustee to retain the property for him- or herself. Similarly, where a person contributes to the purchase price of property with the expectation of an entitlement to a share, it may be said that for the trustee to retain the property for him- or herself would be equally unconscionable. The difference relates more specifically to when the trust arises. The resulting trust may be viewed as a form of alternative intention, i.e. that the primary intention is to create a trust, but that a subsidiary intention is to retain the property if the trust fails. The constructive trust looks more to the

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[2] *Re Vandervell (No 2)* [1974] Ch 269.
[3] (1973 c.18).

situation where a trust was not specifically intended, but is a necessary means of recognising the expectations arising from the parties' interactions with each other.

It is important to note that the constructive trust operates on the conscience of the trustee[4] and therefore there can be no trust unless the trustees know or ought to have known that they are not entitled to retain the property for themselves. The trust exists from the date upon which that situation occurs. Once the trustee knows, or should know, that the property is not owned for his or her own benefit, then he or she becomes a trustee, even though the litigation may not take place until some considerable time afterwards. The courts' role is to identify an existing trust, rather than impose a trust in order to confer a remedy – although the court's identification of the trust is of course the way in which the dispute is remedied.

A constructive trust would also be imposed where a trust has been created without observance of the correct formalities, as in the case of *Bannister v Bannister* [1948] 2 All ER 133. In this case, the claimant and the defendant made an oral agreement whereby the defendant would sell a cottage to the claimant, on the condition that the claimant could live rent free in the cottage for as long as she wished. However, over time, the claimant occupied most of the cottage, with the exception of one room, in which the defendant still lived. The claimant then argued that the defendant occupied the cottage under a tenancy at will, and could therefore be forced to quit the cottage. This argument failed on the basis that the cottage was conveyed to the claimant on a specific condition, and that it would therefore be unconscionable to the claimant to deny that condition.

Furthermore, the effects of resulting and constructive trusts are different. Therefore, under a resulting trust, the subject matter of the trust has, to some degree, been defined (even if there is inadequate identification of how much each beneficiary is to receive). Accordingly, under a resulting trust, it is that property that will form the subject matter of the trust. On the other hand, a constructive trust measures the degree of the trustee's unconscionability, and therefore the extent of the beneficiary's entitlement depends on the degree of the trustee's culpability.

Nevertheless, the constructive trust is not strictly a remedy – the court's role is to identify the conduct that gives rise to a trust, and declare that a trust existed from that point in time. It also searches for evidence of the parties' intentions as to the beneficiary's entitlement, and exists primarily in order to give effect to those intentions. The constructive trust in England and Wales is therefore said to be institutional rather than remedial (although declaring the existence of a trust may be what is required to resolve the dispute between the parties). In other common law jurisdictions, such as Canada, New Zealand and Australia however, the trust is more readily recognised as being a remedy. In other words, these jurisdictions will create a trust if that is appropriate as a way of compensating the claimant for the loss they have sustained as a consequence of the defendant's unconscionable conduct. In essence, these are two different ways of looking at the same thing. In Canada, Australia and New Zealand, the courts' approach is to find the unconscionable conduct and impose a trust in order to remedy that. In England and Wales however, the approach is to find that the defendant's conduct is unconscionable *because* he or she has acted in breach of trust. Therefore, under the law of England and Wales:

> the scenario where only one party has legal ownership the non-legal owner will first have to establish a constructive trust in their favour. If the party were unable to do this, then they would have no equitable ownership in the property.[5]

One common example of the constructive trust, as has been demonstrated in Chapter 14, is the constructive trust of the family home, where the courts have developed a number

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[4] *Westdeutsche Landesbank Girozentrale v Islington LBC* [1994] 4 All ER 890.

[5] Doyle, A. (2012) '*Jones v Kernott*: which road to Rome?' 2 *Trusts Law International* 96–105.

of guidelines to determine when a non-owning cohabitant will have a share in the home. However, there are other ways in which a constructive trust may arise. These trusts, as will be shown, utilise a broader concept of unconscionable conduct, and the constructive trust is more likely to be used as a means of resolving the dispute between the parties rather than arising when the parties have fulfilled certain actions. The categories of constructive trust are not closed, and therefore it is possible for the court to impose a constructive trust wherever it would be unconscionable for the person identified as a trustee to be allowed to keep the property for themselves.

Dishonest misappropriation creating a constructive trust

Although, as will be shown in the next section, the concept of the constructive trust in the context of the family home has been fairly strictly defined, the law's use of the constructive trust to correct fraudulent or unconscionable conduct is extremely flexible, and a constructive trust will be imposed wherever a person attempts to assert that he or she is the owner of something that rightfully belongs to another person. Therefore, for example, for the purpose of tracing in equity (and the increased flexibility it offers over tracing at common law), the thief[6] or the person who commits the torts of conversion of trespass to goods will be deemed to be a constructive trustee of those goods for the benefit of the rightful owner.

EXTRACT

Rochfoucauld v Bousted [1897] 1 Ch 196

Case facts

The claimant owned a number of coffee estates, which had been mortgaged before being sold to the defendant. The claimant argued that these coffee estates were sold to the defendant as a trustee for the claimant, and when the defendant sold the coffee estates, she should have repaid the proceeds of sale to the beneficiary. The defendant's argument was firstly, that the land had not been conveyed to her as trustee, but as the absolute owner, and even if a trust had been created, this was not done in writing, and could not therefore be proved.

Lindley LJ

According to these authorities, it is necessary to prove by some writing or writings signed by the defendant, not only that the conveyance to him was subject to some trust, but also what that trust was. But it is not necessary that the trust should have been declared by such a writing in the first instance; it is sufficient if the trust can be proved by some writing signed by the defendant, and the date of the writing is immaterial. It is further established by a series of cases, the propriety of which cannot now be questioned, that the Statute of Frauds does not prevent the proof of a fraud; and that it is a fraud on the part of a person to whom land is conveyed as a trustee, and who knows it was so conveyed, to deny the trust and claim the land himself. Consequently, notwithstanding the statute, it is competent for a person claiming land conveyed to another to prove by parol evidence that it was so conveyed upon trust for the claimant, and that the grantee, knowing the facts, is denying the trust and relying upon the form of conveyance and the statute, in order to keep the land himself.

Outcome

The claimant's appeal was allowed.

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[6] *Attorney General of Hong Kong v Reid* [1994] 1 AC 324.

Similarly, a person who has given some form of undertaking to act in a fiduciary capacity towards another will be construed as a constructive trustee if he or she fails to fulfil that obligation.[7] Therefore, a seller of land becomes a trustee for the benefit of the buyer once contracts have been exchanged, as Walton J confirms in the case of *Lake v Bayliss* [1974] 2 All ER 1114 at p.1116 where he states:

> one of the standing doctrines of the court that on a contract for the transfer of property being entered into the vendor or intending transferor becomes a trustee for the purchaser or transferee. Admittedly, it is a qualified trusteeship. It does not have all the usual incidents of a bare trusteeship for a cestui que trust, and of course the most glaring and most obvious departure from such normal incidents is that the trustee has his own interest, in the shape of the receipt of the purchase money, to protect. Of course he has a lien on the property until he has been paid his purchase money in the normal course of events. But, says counsel, as to the basic relationship in regard to the land contracted to be sold or transferred, no matter what may be the case in relation to other collateral matters, such as moneys paid under a contract of insurance or receipts under derequisitioning procedures, there is no doubt at all that the property itself is held as by a trustee.

By the same principle, a company director is also identified as a trustee and therefore the misappropriation of a company's funds by a director will be a breach of trust – a point that is confirmed by Buckley LJ in *Belmont Finance Corporation v Williams Furniture Limited (No 2)* [1980] 1 All ER 393, where he explains:

> I now come to the constructive trust point. If a stranger to a trust (a) receives and becomes chargeable with some part of the trust fund or (b) assists the trustees of a trust with knowledge of the facts in a dishonest design on the part of the trustees to misapply some part of a trust fund, he is liable as a constructive trustee (*Barnes v Addy* ((1874) LR 9 Ch App 244 at 251–252) per Lord Selborne LC).
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> A limited company is of course not a trustee of its own funds: it is their beneficial owner; but in consequence of the fiduciary character of their duties the directors of a limited company are treated as if they were trustees of those funds of the company which are in their hands or under their control, and if they misapply them they commit a breach of trust (*Re Lands Allotment Co* ([1894] 1 Ch 616 at 631, 638, [1891–94] All ER Rep 1032 at 1034, 1038), per Lindley and Kay LJJ). So, if the directors of a company in breach of their fiduciary duties misapply the funds of their company so that they come into the hands of some stranger to the trust who receives them with knowledge (actual or constructive) of the breach, he cannot conscientiously retain those funds against the company unless he has some better equity. He becomes a constructive trustee for the company of the misapplied funds. This is stated very clearly by Jessel MR in *Russell v Wakefield Waterworks Co* ((1875) LR 20 Eq 474 at 479), where he said:
>
> > 'In this Court the money of the company is a trust fund, because it is applicable only to the special purposes of the company in the hands of the agents of the company, and it is in that sense a trust fund applicable by them to those special purposes; and a person taking it from them with notice that it is being applied to other purposes cannot in this Court say that he is not a constructive trustee.'

[7] *Sinclair Investment Holdings SA v Versailles Trade Bank Finance Ltd (No 3)* [2007] EWHC 915 (Ch).

The finding of a constructive trust in light of a wrongdoer's misconduct usually derives from the fact that the wrongdoer knows that he or she is not entitled to keep the trust property for him- or herself. Thus a person who is aware that he or she is not entitled to inherit property may not keep the trust property for him- or herself even if he or she was not properly appointed to a trusteeship. In *James v Williams* [2000] Ch 1 for example, the claimant's father had bought a house, which had passed to the claimant's mother on his intestacy. The claimant's mother had then died intestate, and the claimant's brother and sister had continued to live in the house. When the claimant's brother died, he left the house in his will to the claimant's sister, who on her death, left it by will to her own daughter. The claimant therefore sued the defendant for a one third share of the house, to which she was entitled under her mother's intestacy. The claimant's brother had never applied to become the administrator of his mother's estate, and accordingly, at first instance it was held that, as he was not the personal representative, he could not be in breach of trust. However, it was held that he knew that he was not entitled to inherit the house, and therefore owned it as trustee for the benefit of himself and his two sisters, one of whom was the claimant. Aldous LJ explains:

> In the present case, William Junior [the claimant's brother] knew that the grandfather [the claimant's father] had purchased the house and that on his death the grandmother [the claimant's mother] had acquired his interest. He also knew that the grandmother had died intestate. In those circumstances, he could not have believed that he alone was entitled to the property. He must have known that the plaintiff was entitled to a share. If he had taken out letters of administration, then he would have become a personal representative and would have taken on the duties incident to that office. The result, in my view, would have been that there would have been a trust within the definition of section 68 of the Limitation Act 1980 and he would have owed a fiduciary duty to his sisters. It is the fact that letters of administration were not taken out that makes it possible for the defendant to contend that no fiduciary duty was owed. I accept that there is no duty upon a person to become a personal representative, but I believe that the failure by William Junior to take out letters of administration is relevant, when considering what is the equitable position in this case, as equity envisages that what should have been done has been done.
>
> In my view the circumstances of this case are such that the constructive trust arose in about 1972 on the death of the grandmother. William Junior knew that he was not solely entitled to the property. He took it upon himself to take possession of the property as if he owned it and assumed responsibility for its upkeep. In my view he was under an equitable duty to hold the property for himself and his sisters. Looking at the state of affairs as at the grandmother's death, the law envisaged that the property would be held upon a statutory trust for the children. It would be inequitable to allow William Junior and, through him the defendant, to take advantage of his decision not to take out letters of administration and to act as if he was the owner with the full knowledge that he was not.

Accordingly, when the claimant's mother died, the proceeds of the sale of the house should have been divided equally between the claimant, her brother and her sister. When the brother died, he could pass his share to his other sister and her daughter, and when the sister died, she could pass her share to her daughter, with the result that the sister's daughter (the defendant) should be entitled to her mother's and her uncle's shares of the house, and that the claimant remained entitled to the third share to which she had become entitled on her own mother's death.

The constructive trust mechanism is also used when one co-owner of land murders[8] the other. The rationale is that a person should not be entitled to benefit from his or her own crime, as Fry LJ explains in *Cleaver and Others v Mutual Reserve Life Association* [1892] 1 QB 147 at p.196. Therefore, whereas, ordinarily, a co-owner would take the legal title (and the beneficial title where he or she own as joint tenants) to the land by the right of survivorship when the other co-owner dies, the principle that a person should not be allowed to benefit from his or her crime means that the murderer will hold the property on a constructive trust, with one half for him- or herself and the other for the benefit of the estate of the deceased co-owner. Unfortunately, there is no authority from the courts of England and Wales that confirms this, although it would be a logical outcome of the public policy rule from *Cleaver*. However the case of *Schobelt v Barber* [1967] 1 OR 349, 60 DLR (2d) 519 from the High Court of Ontario indicates that this is how the Canadian courts are likely to address the issue.

Essentially therefore, the broad concept of the constructive trust is used where the defendant knows that he or she is not entitled to keep the property. Accordingly, the company director, the seller of land, the person whose knowledge makes him or her a trustee (as in *James v Williams*), as well as the thief, the converter and the trespasser will all be held to be trustees of property that they have wrongfully treated as their own. It may therefore also apply in the context of the mutual will. A mutual will arises where Bill and Ben write identical wills leaving everything to each other, and in the event that the other should predecease them, leaving everything to a third party. Such an arrangement might be common where a couple agrees to leave their estate to their spouse or partner, or if that person should die before them, they each agree to leave the estate to a specific beneficiary – a child or children for example. Such mirror wills are fairly common. However, a mutual will goes beyond that, in that there is also an agreement that the testators will not later amend their wills. In other words, each testator's will is contingent upon their co-testator's promise. The courts have held that where the agreement is contractual in nature,[9] any later will puts the trustees – and indeed the beneficiary of that will – in the position of being constructive trustees for the benefit of the beneficiary under the original will. Again, the emphasis is on whether the constructive trustee knows that he or she should recognise another person's entitlement.

Constructive trust created by intervention of third parties

A constructive trust is created where a person who is not a trustee intermeddles with the trust following authorisation from a person who is a trustee. Therefore, for example, a solicitor or an agent may become a constructive trustee if they assume or are given trustee functions beyond those of an agent, or if they dishonestly assist the trustees in perpetrating a breach of trust. In *James v Williams,* discussed above, for example, the claimant's brother was not a trustee of his mother's estate because he had not completed the letters of administration that would allow him to become the personal representative for the purposes of s.33 Administration of Estates Act 1925. However, he had assumed a trustee's role by dealing with the house as though he was the owner, and was therefore viewed as a trustee because he had acted in the way that a trustee would have acted in relation to property he controlled.

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[8] Other criminal conduct that causes death will also have the same consequences – for example manslaughter, causing death by dangerous driving, etc. Nevertheless, by virtue of the Forfeiture Act 1982, the court may modify the rule preventing a person from benefiting from their criminal conduct where death is caused by a criminal offence other than murder.

[9] *Goodchild v Goodchild* [1997] 3 All ER 63.

Other forms of constructive trust

Although the situations described above have focused on the unlawful conduct of the trustee, unlawful conduct is not always required. For example, where a person has acquired goods from an insolvent company, they may be regarded as a trustee of those goods even though they themselves had not acted unlawfully. For example, in the case of *FC Jones v Jones* [1997] Ch 159, the defendant was deemed to be a constructive trustee even though she had merely received a loan from the company. Similarly, the case of *Chase Manhattan v Israel British Bank* [1980] 2 WLR 202 concerned a situation where the same payment had been made twice. Again, there was no dishonesty in this case, but is was unconscionable for the Israel British Bank to treat the second payment as though it were its own money.

A constructive trust will also arise where the trustee has voluntarily assumed responsibility for the fund. A secret trust is viewed as a form of constructive trust because the trustee has agreed to hold the property on trust, even though the trust does not conform with the formalities required by the Wills Act 1837. Similarly, a mutual will uses the constructive trust, again on the basis that the trustee has voluntarily agreed to an obligation, and the settlor has relied on that promise by writing a will in specific terms – something that he or she would not have done if the trustee had not agreed to be bound. Accordingly the trust is imposed because the trustee has made a promise, and it would therefore be unconscionable for him or her to go back on that.

Proprietary estoppel

There are many different types of estoppel, both at common law and in equity. However, the most wide-ranging is proprietary estoppel, which, like the constructive trust, focuses on unconscionability and detriment – the former on the part of the wrongdoer, and the latter on the part of the claimant. The concept of proprietary estoppel overlaps in many ways with the constructive trust, as Lord Walker explained in the case of *Yaxley v Gotts* [2000] Ch 162 at p.180:

> A constructive trust of that sort is closely akin to, if not indistinguishable from, proprietary estoppel. Equity enforces it because it would be unconscionable for the other party to disregard the claimant's rights.

However, the concepts of the constructive trust and proprietary estoppel are subtly but significantly different. Estoppel is premised on the idea that the defendant knows that the claimant has a mistaken belief in an entitlement to property, and the claimant has either encouraged that belief, or has failed to correct that belief, with the result that the claimant has acted to his or her detriment on the expectation. Therefore, whereas the constructive trust relies on a common intention regarding the ownership of property, the emphasis with estoppel is on one person's belief.[10] Any kind of representation will suffice, including inaction or silence by not correcting a mistaken belief, as in *Covell v Sweetland* [1968] 2 All ER 1016.

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[10] *Re Basham* [1986] 1 WLR 1498.

EXTRACT

Covell v Sweetland [1968] 2 All ER 1016

Case facts

The claimant and the defendant were a married couple who separated in September 1956. They later agreed upon a maintenance agreement for the benefit of the wife. However the agreement did not indicate how long it was to last or the circumstances under which it would come to an end. In 1960, the wife filed for divorce, and after the decree nisi was issued, the husband's solicitors argued that the maintenance agreement should become void upon decree absolute, and that a new maintenance agreement should be drawn up. This was not done and a decree absolute was granted. The defendant stopped making maintenance payments but later agreed to pay maintenance to his ex-wife up to the date of her remarriage. The claimant then claimed for maintenance from the date of the decree absolute to the date upon which the writ was issued. The court held that the claimant was estopped from claiming maintenance after the date of the decree absolute because the correspondence between the claimant and the defendant indicated that she did not expect her ex-husband to pay maintenance to her after her remarriage. Accordingly, even though the original maintenance agreement did not give any indication that it would end on the wife's remarriage, the fact that she had led the defendant to believe that this would be the case meant that she could not then claim that she was entitled to continued maintenance.

Hinchcliffe J

Out of respect for the careful arguments addressed to the court by both learned counsel I would say this, that all the cases which have been cited, including the New Zealand one of *P v P* [[1957] NZLR 854], which seems to me to have been rightly decided, show that a representation can constitute an estoppel, but it must be one of fact-in this case, I think, the representation was of mixed law and fact-it must have been made with the intention that it would be acted on and it must have been acted on to the detriment of the person to whom it was made. Certainly in this case the defendant has been prejudiced in that he took no steps to vary the agreement – no steps to protect himself – and he failed to put any money aside to pay the maintenance. Therefore, it seems to me that if the plaintiff by her solicitors' letters allowed the defendant to believe for a number of years that the true position as to maintenance was as represented, and the defendant did so believe and acted to his detriment, then the plaintiff is estopped from denying that the facts were as represented.

In my judgment the plaintiff is estopped, having regard to all the circumstances of the case; that is to say that the agreement was intended to be for the duration of the marriage, and it only came to an end by the decree absolute. The plaintiff in the letters written on her behalf never suggested that the maintenance should be paid after she re-married and the first suggestion of this was 22 March 1965, when this writ was issued. I have no doubt at all that it would be grossly unfair to the defendant if he should be ordered to satisfy the plaintiff's claim after so many years of delay during which he was lulled into a sense of false security into believing that the maintenance for the plaintiff certainly ended after she had re-married on 21 December 1960 and no claim for continuing the maintenance was ever made until the issue of the writ. Therefore, in my judgment, the plaintiff is estopped from asserting that the defendant is indebted to her in the agreement in respect of maintenance. There will be judgment for the defendant.

There are therefore three elements to proprietary estoppel. Firstly, there must be an assurance.[11] In *Gillett v Holt* [2001] Ch 210, the claimant had been repeatedly assured that he would inherit a farm belonging to a long-term friend. In *Thorner v Major* [2009] 1 WLR 776, the 'assurance' was far less explicit – the settlor had given the claimant a life assurance policy which had been taken as meaning that the settlor was intending for the claimant to inherit the farm after his death.

The second element is reliance. In other words, there must be a sense that the claimant has relied on the assurance, and that they have not treated it as empty talk. Accordingly, in *Lissimore v Downing* [2003] 2 FLR 308, although the claimant argued that she had been led to believe that she had an equitable interest in her lover's house, she was not considered to have relied upon this – she had continued to live her life as before. As a result, there was no indication that she had relied on the assurance.

The third requirement is detriment. Detrimental reliance commonly takes the form of expenditure of money, although this is not the only form of reliance that will suffice, provided that it is substantial.[12] Accordingly, giving up accommodation,[13] or working for little or no money[14] or paying for improvements to the property[15] are all examples of detriment. The defendant cannot then rely on his or her strict legal entitlement to deny the claimant their rights[16] if doing so would be unconscionable. In *Gillett v Holt* [2001] Ch 210 at p.232, Walker LJ concluded that unconscionability means 'Whether the detriment is sufficiently substantial is to be tested by whether it would be unjust or inequitable to allow the assurance to be disregarded.'

However, whereas with a constructive trust, the claimant is entitled to be regarded as a beneficiary of the trust property, estoppel permits the court to determine the appropriate remedy, which according to the case of *Crabb v Arun DC* [1976] Ch 179 at 198 is 'the minimum equity to do justice to the [claimant]'. In many cases, the appropriate remedy will be to order the delivery of that which was initially promised – after all, that is the cause of the claimant's detrimental reliance. The remedy may therefore take the form of a share in the property, as under a constructive trust.[17] However, the equity may also be satisfied by way of repayment of the money given,[18] a right to occupy the property under a licence,[19] or an easement.[20]

A further significant difference is that under a constructive trust there must be an express or implied common intention, whereas the proprietary estoppel may be based more on a broader notion of what the claimant was led by the defendant to believe, or that the defendant did not disabuse the claimant of a mistaken belief. Thirdly, whereas the claimant may claim a constructive trust as a cause of action, proprietary estoppel exists as a defence to prevent the owner from relying on his or her strict legal rights, although the rule appears to be relaxed somewhat[21] where the owner has made representations to the other party that they are entitled to an expectation relating to the land.

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[11] *Sinclair v Sinclair* [2009] EWHC 926.
[12] *Van Laetham v Brooker* [2005] EWHC 1478.
[13] *Jones v Jones* [1996] 3 WLR 703.
[14] *Jennings v Rice* [2003] 1 P & Cr 100.
[15] *Inwards v Baker* [1965] 2 QB 29.
[16] *Re Basham* [1987] 1 All ER 405.
[17] *Hussey v Palmer* [1972] 3 All ER 744.
[18] *Neesom v Clarkson* (1845) 4 Hare 97.
[19] *Parker v Parker* [2003] EWHC 1846 (Ch).
[20] *Crabb v Arun District Council* [1976] Ch 179, [1975] 3 All ER 865.
[21] *Shipping Co v Baltic Shipping Co* [1999] 2 Lloyd's Rep 159.

The *Pallant v Morgan* equity

A further concept that is linked to the notion of the constructive trust and proprietary estoppel is that which is termed the '*Pallant v Morgan* equity' – derived, unsurprisingly, from the case of *Pallant v Morgan* [1953] Ch 43.

EXTRACT

Pallant v Morgan [1953] Ch 43

Case facts

The claimant and the defendant were two neighbouring landowners. Immediately prior to an auction for the sale of a piece of land that both of them wished to acquire, their agents agreed that the claimant's agent would not bid at the auction, in order to ensure that the purchase price was not driven up by them bidding against each other. However, they agreed that after the auction, they would divide the plot of land between them according to a specific formula. At the auction therefore, the claimant's agent did not bid, and the defendant was therefore able to buy the land for £1000. After the auction, the parties could not agree on how the land was to be divided, and therefore the defendant retained it in its entirety. The claimant sued for breach of contract. It was held, however, that the subject matter of the contract was insufficiently precise to give rise to an order for specific performance, but that to allow the defendant to retain the land for himself would amount to fraud. It was therefore decided that he held the land on trust for himself and the claimant.

Harman J

Can, then, the plaintiff have a specific performance of the agreement so reached? In my judgment he cannot, for there is too much left undecided . . . Is the result then that the plaintiff must fail? In my judgment not so. To allow the defendant to retain lot 16 under these circumstances would be tantamount to sanctioning a fraud on his part, and I find the following in *Fry on Specific Performance*, 6th ed., p. 184, para. 386, at the end of the chapter in which the author is dealing with what he styles the 'uncertainty of the contract': 'The same certainty,' he says, 'will not be required in cases where there is any element of fraud, as in simple cases of specific performance of a contract. Thus where A agreed with B in effect that if B would not try to buy a certain estate, A would try to buy, and in case of success would cede a portion of the estate to B at a certain price: and B acted on his bargain and allowed A to purchase: and A having purchased refused to perform his part and set up the uncertainty of the part to be ceded: the court held that the defence could not avail and directed an inquiry to ascertain the portion to be given up and the price. It seems that if this could not have been ascertained, B might have claimed the whole estate.'

The case on which that paragraph is based is *Chattock v. Muller* 8 Ch.D. 177 . . . Malins V.-C. gave judgment as follows: 'In a case like this, where the defendant has acquired the estate or part of it by a fraud on the plaintiff, I think that the court would be bound, if possible, to overcome all technical difficulties in order to defeat the unfair course of dealing of the defendant, and I should not, in my opinion, be going too far if I compelled the defendant to give the whole estate to the plaintiff at the price given for it, rather than that he should succeed in retaining it on account of any uncertainty as to the part which the plaintiff is entitled to have . . .'

> The present case is if anything stronger than that one, but I do not follow the Vice-Chancellor in his suggestion that the defendant could become bound to hand over the whole property to the plaintiff at the price he gave for it. In my judgment, the proper inference from the facts is that the defendant's agent, when he bid for lot 16, was bidding for both parties on an agreement that there should be an arrangement between the parties on the division of the lot if he were successful. The plaintiff and the defendant have failed to agree on a division, and the court cannot compel them to agree. The best it can do is to decree that the property is held by the defendant for himself and the plaintiff jointly, and if they still fail to agree on a division the property must be resold, either party being at liberty to bid, and the proceeds of sale divided equally after repaying to the defendant the £1,000 which he paid with interest at 4 per cent . . .
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> It is true that the suggested agreement would have involved the transfer to the plaintiff of a portion of lot 15, but, in default of an agreement, he cannot obtain that, for his agent had no instructions to bid for that lot in any event.

Essentially therefore, the *Pallant v Morgan* equity arises where there is an agreement that the defendant will buy property for the benefit of both him- or herself and the defendant. The equity arises where the defendant acts inconsistently with that agreement. Its significance is that, although it relies on there being an agreement between the parties, a contract is not necessary, and indeed, if a contract existed, the law of contract is likely in many cases to offer a sufficient remedy. The elements are firstly, that prior to acquisition, there should be some agreement that one party will acquire the property for the benefit of both, and secondly, that the non-acquiring party does something that confers an advantage on the other – such as not bidding against him or her at auction. The key features are set out by Chadwick LJ in *Banner Homes PLC v Luff Developments Ltd* [2000] Ch 378 at p.392:

> Equity must never be deterred by the absence of a precise analogy, provided that the principle invoked is sound. Mindful of this caution, it is, nevertheless, possible to advance the following propositions.
>
> (1) A *Pallant v. Morgan* equity may arise where the arrangement or understanding on which it is based precedes the acquisition of the relevant property by one party to that arrangement. It is the pre-acquisition arrangement which colours the subsequent acquisition by the defendant and leads to his being treated as a trustee if he seeks to act inconsistently with it. Where the arrangement or understanding is reached in relation to property already owned by one of the parties, he may (if the arrangement is of sufficient certainty to be enforced specifically) thereby constitute himself trustee on the basis that 'equity looks on that as done which ought to be done;' or an equity may arise under the principles developed in the proprietary estoppel cases. As I have sought to point out, the concepts of constructive trust and proprietary estoppel have much in common in this area. *Holiday Inns Inc. v. Broadhead*, 232 E.G. 951 may, perhaps, best be regarded as a proprietary estoppel case; although it might be said that the arrangement or understanding, made at the time when only the five acre site was owned by the defendant, did, in fact, precede the defendant's acquisition of the option over the 15-acre site.
>
> (2) It is unnecessary that the arrangement or understanding should be contractually enforceable. Indeed, if there is an agreement which is enforceable as a contract,

there is unlikely to be any need to invoke the *Pallant v. Morgan* equity; equity can act through the remedy of specific performance and will recognise the existence of a corresponding trust. On its facts *Chattock v. Muller*, 8 Ch.D. 177 is, perhaps, best regarded as a specific performance case. In particular, it is no bar to a *Pallant v. Morgan* equity that the pre-acquisition arrangement is too uncertain to be enforced as a contract–see *Pallant v. Morgan* [1953] Ch. 43 itself, and *Time Products Ltd. v. Combined English Stores Group Ltd.*, 2 December 1974–nor that it is plainly not intended to have contractual effect–see *Island Holdings Ltd. v. Birchington Engineering Co Ltd.*, 7 July 1981.

(3) It is necessary that the pre-acquisition arrangement or understanding should contemplate that one party ('the acquiring party') will take steps to acquire the relevant property; and that, if he does so, the other party ('the non-acquiring party') will obtain some interest in that property. Further, it is necessary that (whatever private reservations the acquiring party may have) he has not informed the non-acquiring party before the acquisition (or, perhaps more accurately, before it is too late for the parties to be restored to a position of no advantage/no detriment) that he no longer intends to honour the arrangement or understanding.

(4) It is necessary that, in reliance on the arrangement or understanding, the non-acquiring party should do (or omit to do) something which confers an advantage on the acquiring party in relation to the acquisition of the property; or is detrimental to the ability of the non-acquiring party to acquire the property on equal terms. It is the existence of the advantage to the one, or detriment to the other, gained or suffered as a consequence of the arrangement or understanding, which leads to the conclusion that it would be inequitable or unconscionable to allow the acquiring party to retain the property for himself, in a manner inconsistent with the arrangement or understanding which enabled him to acquire it. *Pallant v. Morgan* [1953] Ch. 43 itself provides an illustration of this principle. There was nothing inequitable in allowing the defendant to retain for himself the lot (lot 15) in respect to which the plaintiff's agent had no instructions to bid. In many cases the advantage/detriment will be found in the agreement of the non-acquiring party to keep out of the market. That will usually be both to the advantage of the acquiring party–in that he can bid without competition from the non-acquiring party–and to the detriment of the non-acquiring party–in that he loses the opportunity to acquire the property for himself. But there may be advantage to the one without corresponding detriment to the other. Again, *Pallant v. Morgan* provides an illustration. The plaintiff's agreement (through his agent) to keep out of the bidding gave an advantage to the defendant–in that he was able to obtain the property for a lower price than would otherwise have been possible; but the failure of the plaintiff's agent to bid did not, in fact, cause detriment to the plaintiff–because, on the facts, the agent's instructions would not have permitted him to outbid the defendant. Nevertheless, the equity was invoked.

(5) That leads, I think, to the further conclusions: (i) that although, in many cases, the advantage/detriment will be found in the agreement of the non-acquiring party to keep out of the market, that is not a necessary feature; and (ii) that although there will usually be advantage to the one and correlative disadvantage to the other, the existence of both advantage and detriment is not essential-either will do. What is essential is that the circumstances make it inequitable for the acquiring party to retain the property for himself in a manner inconsistent with the arrangement or understanding on which the non-acquiring party has acted. Those circumstances

may arise where the non-acquiring party was never 'in the market' for the whole of the property to be acquired; but (on the faith of an arrangement or understanding that he shall have a part of that property) provides support in relation to the acquisition of the whole which is of advantage to the acquiring party. They may arise where the assistance provided to the acquiring party (in pursuance of the arrangement or understanding) involves no detriment to the non-acquiring party; or where the non-acquiring party acts to his detriment (in pursuance of the arrangement or understanding) without the acquiring party obtaining any advantage therefrom.

The remedial constructive trust

Commonwealth jurisdictions have adopted a more remedial approach to the constructive trust than the courts in England and Wales. They have therefore shown greater willingness to adopt the constructive trust as a remedy – although, as has been shown, the courts in England and Wales have tended to view proprietary estoppel and the *Pallant v Morgan* equity as being more appropriate remedial instruments. Canada was the first jurisdiction to expand the concept of the constructive trust, but it has also developed in Australia and New Zealand.

The Canadian approach has been to consider the issue as one of unjust enrichment, and to consider whether the constructive trustee has obtained something that he or she would otherwise have had to spend money on in order to acquire. The emphasis is therefore on the gain made by the trustee, rather than the detriment suffered by the beneficiary. The advantage of the Canadian approach is that a trust is not necessarily the outcome of a finding of unjust enrichment; instead the courts' approach is to consider what form of compensation would be adequate for the gain that has been made.

Canada

EXTRACT

Newman, C. and Friedman, P. (2000) 'Remedial Constructive Trusts: Where to Next Part 1?' *Trusts and Trustees* 20

Of the Commonwealth jurisdictions, Canada was the first to recognise and accept a general remedial constructive trust. The Supreme Court of Canada in *Pettkus v Becker* (1980) 117 DLR (3d) 257, departed from the principles of constructive trust developed in England and held that a constructive trust was an appropriate remedy to redress unjust enrichment. Unjust enrichment is therefore the cause of action for which the constructive trust is available. It is important to note that the introduction of the remedial constructive trust as a remedy for unjust enrichment did not displace other types of constructive trusts known to Canadian law prior to the decision in *Pettkus v Becker*. Dickson CJ emphasised the importance of *Pettkus v Becker* in the Supreme Court of Canada's decision in *Hunter Engineering Co v Syncrude Canada Ltd* [1989] 1 SCR 426 where he stated at p471 as follows: 'The constructive trust has existed for over two hundred years as an equitable remedy for certain forms of unjust enrichment . . . Until the decision of this Court in *Pettkus v Becker*, the constructive trust was viewed largely in terms of the law of trusts, hence the need for the existence of a fiduciary relationship. In *Pettkus v Becker*, the Court moved to an approach more in line with

restitutionary principles by explicitly recognising constructive trust as one of the remedies for unjust enrichment.' Once liability is established by demonstrating an unjust enrichment which calls for restitution, the court may exercise its discretion to award either a proprietary remedy by imposing a constructive trust or other remedies such as monetary damages. McLachlin J explained this remedial flexibility in *Rawluk v Rawluk* (1990) 1 SCR 70 at pp185–6 as follows: 'The significance of the remedial nature of the constructive trust is not that it cannot confer a property interest, but that the conferring of such an interest is discretionary and dependent on the inadequacy of other remedies for the unjust enrichment in question. The doctrine of constructive trust may be used to confer a proprietary remedy, but does not automatically presuppose a possessory property right. Thus, even where the tests for constructive trust are met – unjust enrichment, corresponding deprivation, and no juridical justification for the enrichment and justification – the property interest does not automatically arise. Rather, the court must consider whether other remedies to remedy the injustice exist which make the declaration of a constructive trust unnecessary or inappropriate.' As La Forest J stated in *LAC Minerals Ltd v International Corona Resources Ltd* (1989) 61 DLR (4th) 14 at p48: 'The constructive trust does not lie at the heart of the law of restitution. It is but one remedy, and will only be imposed in appropriate circumstances.' and then at page 51: 'The constructive trust awards a right in property, but that right can only arise once a right to relief has been established. In the vast majority of cases a constructive trust will not be the appropriate remedy – a constructive trust should only be awarded if there is reason to grant to the plaintiff the additional rights that flow from recognition of a right of property. Among the most important of these will be that it is appropriate that the plaintiff receive the priority accorded to the holder of a right of property in a bankruptcy.' Recently, Canadian courts have expressed approval for a constructive trust which may be imposed, as Lord Denning advocated in England (see below), 'where good conscience so requires'. Thus courts in Canada recognise the availability of constructive trusts for both wrongful acts which have occurred in the absence of unjust enrichment, such as fraud and breach of duty and for unjust enrichment. The court may exercise its discretion to give the remedial constructive trust so created either retroactive or prospective effect. Thus, in accordance with the flexible nature of the remedy, the date at which a constructive trust arises is said to be the date upon which the duty to make restitution occurs, and not vice versa.

Australia

The approach taken in Australia has been to address whether the absence of a trust would be unconscionable under the circumstances. There is no reliance on common intention as there is in relation to constructive trusts in England and Wales, merely a consideration of whether it would be unconscionable to deny that there is a trust. On the one hand this may appear to be looser than the law in England and Wales, although it is equally possible to consider that England and Wales also looks to the issue of unconscionability, and concludes that the only grounds upon which it is unconscionable to deny a person a share is where there is an express or implied common intention between them regarding shared ownership. Nevertheless, the advantage of the Australian law is that it may consider what unconscionability means on a case by case basis rather than attempting to fit the facts of the situation as they are presented to the court to the structures of the law.

EXTRACT

Hayton, D. (1988) 'Remedial Constructive trusts of family homes: an overseas view' *Conveyancer and Property Lawyer* 259

The recent decision of the High Court of Australia in *Baumgartner v. Baumgartner* [(1987) 11 Fam LR 915], allowing an appeal from the New South Wales Court of Appeal, may well have significant implications for the development of English law. All five judges held that there is a general doctrine of remedying unconscionable conduct that justifies the imposition of a constructive trust. The co-habitees had no express or inferred common intention to create a trust of the house in the man's name, so there was no informal unenforceable express trust which could be enforced under the guise of a constructive trust, but this did not dispose of the woman's claim to a share in the house. In all the circumstances the man's conduct in asserting 100 per cent. ownership was so unconscionable as to attract the intervention of equity and the imposition of a constructive trust in favour of the woman as to 45 per cent . . . In the leading joint judgment delivered by these three judges it was emphasised that M and F had pooled their earnings with a view to meeting all the expenses and outgoings arising from their living together in the unit and then the house. F's contributions had been paid neither by way of gift nor by way of rent or mesne profits.

The case is one in which the parties have pooled their earnings for the purposes of their joint relationship, one of the purposes being to secure accommodation for themselves and their child. Their contributions to the acquisition of the land, the building of the house, the purchase of furniture and the making of their home, were on the basis of, and for the purposes of, that joint relationship. In this situation the appellant's assertion, after the relationship had failed, that the Leumeah property, which was financed in part through the pooled funds, is his sole property, is his property beneficially to the exclusion of any interest at all on the part of the respondent, amounts to unconscionable conduct which attracts the intervention of equity and the imposition of a constructive trust at the suit of the respondent. . . . We consider that the constructive trust to be imposed should declare the beneficial interest of the parties in the proportions 55 per cent. to the appellant and 45 per cent. to the respondent' (p.34) . . . The imposition of a constructive trust to remedy unconscionable conduct was based on a general principle of equity to be deduced from rules which entitle a fixed term partner to a proportionate refund of his premium and a contractual joint venturer to a proportionate repayment of his capital contribution on the premature dissolution of the partnership or collapse of the joint venture. A common intention constructive trust seems to be an informal, valid but unenforceable, express institutional trust which is vindicated by the imposition of a constructive trust which recognises the earlier existence of a trust independently created by the parties. This is not the case for the remedial constructive trust imposed by the court at the date of the court order to prevent unconscionable conduct or unjust enrichment. The remedial constructive trust thus does not have far-reaching implications for third parties who earlier acquire some interest in the disputed property, unless their actual knowledge is such that they may be placed under in personam obligations.

A common intention constructive trust requires a positive finding of an express or inferred subjective common intention. Some judges may find it difficult to progress from negating certain other intentions to inferring a positive co-owning intention. It can be difficult for an appellate court to decide whether what the trial judge stigmatised as a fictional phantom was really an instance of inferred common intention or whether the inferred common intention found by the judge was really a fictional intention imputed to the parties. In fact-finding reality, is not the distinction illusory? Casuistry has led the Court of Appeal to find an express common intention where M does not intend F to have a half share but gives F some excuse for not putting the property in joint names. Since it is the expectations created by M that are significant in leading F to act to her detriment it may be that equitable proprietary estoppel principles will provide a more realistic basis of relief for F in the future.

New Zealand

The courts in New Zealand also favour the remedial approach, dismissing the more institutional approach in England and Wales as being too strict. Accordingly, rather than imposing a trust once specific criteria are met, the New Zealand courts consider whether a trust is the most appropriate remedy. However, it may be seen to be as restrictive as the law in England and Wales in some respects, as a constructive trust will only exist where other remedies are inadequate.

EXTRACT

Richardson, N. (2002) 'Remedial Constructive Trusts in New Zealand' 1 *Trusts Law International* 53–55

The distinction between institutional and remedial trusts is part of New Zealand law and Glazebrook J quoted Tipping J in the Court of Appeal decision of *Fortex Group Ltd (In Receivership and Liquidation) v MacIntosh* [[1998] 3 LRC 586] who stated:

> 'An institutional constructive trust is one which arises by operation of the principles of equity and whose existence the Court simply recognises in a declaratory way. A remedial constructive trust is one which is imposed by the Court as a remedy in circumstances where, before the Order of the Court, no trust of any kind existed. The difference between the two types of constructive trust, institutional and remedial, is that an institutional constructive trust arises upon the happening of the events which bring it into being. Its existence is not dependent on any Order of the Court. Such order simply recognises that it came into being at the earlier time and provides for its implementation in whatever way is appropriate. A remedial constructive trust depends for its very existence on the Order of the Court; such order being creative rather than simply confirmatory.'

In *Chodar* [*Commonwealth Reserves I v Chodar* (2000) 3 ITELR 549] the court noted that the Court of Appeal in *Fortex* left open the question whether a remedial constructive trust should be 'confirmed' as part of New Zealand law . . . It was held that there were two potential triggers for the exercise of the court's discretion to grant a remedial constructive trust: unjust enrichment and unconscionability. It was noted that New Zealand judges have used both concepts. Henry J in *Fortex* accepted unjust enrichment and Cooke P used unconscionability in *Elders Pastoral Ltd v Bank of New Zealand* [[1990] 1 WLR 1090] . . .

Even if the court does have jurisdiction to award this remedy in cases of unconscionability and unjust enrichment Glazebrook J held that it was not inevitable that a remedial constructive trust would be awarded:

> 'Reliability and certainty are primary considerations of any system of property rights, and the unprovoked alteration of those rights is to be avoided where possible. This is all the more true in a commercial rather than a domestic context. The Court must carefully examine the reasons why other forms of relief are inadequate, the interests of any third parties and the other circumstances of the case, and consider whether proprietary relief can be justified.
>
> In cases where the interests of third parties would be prejudiced by a proprietary remedy, particularly if those third parties are in a substantially similar position to the plaintiff, or where the plaintiff has accepted the risk of the defendant's insolvency, then proprietary relief is likely to be inappropriate.' . . .

The court held that it had the jurisdiction to award a remedial constructive trust . . . Secondly, it was stated that a remedial constructive trust should only be imposed where other available remedies were inadequate . . .

ACTIVITY

Consider the following questions. You may find it useful to discuss your answers with other students. However, it is also useful to consider why you have come to a particular conclusion, and to justify that point of view.

1. What form of constructive trust do you consider to be most satisfactory – the institutional constructive trust in England and Wales, or the remedial approaches in Canada, Australia and New Zealand? Argue the case from both viewpoints.
2. With the exception of constructive trusts of the family home, to what extent do you consider the existing law on constructive trusts in England and Wales to be remedial in its approach?
3. Why do you think there is a difference between the different types of constructive trust? Is this justified?
4. What are the differences between constructive trusts and estoppel?
5. Do you consider it necessary for both constructive trusts and estoppel to exist?

The future of the constructive trust

Although this chapter has identified specific situations where a constructive trust will exist, such as the shared ownership of the family home, and has also identified fairly precise criteria for establishing a constructive trust in those situations, it is emphasised that these are not closed categories. Therefore it is possible that, as circumstances require it, equity will apply the constructive trust to new, and hitherto unconsidered, situations, just as it did during the 20th century in response to the new need to apportion property between cohabitants. Accordingly, as Millett J explained in *Lonrho v Al-Fayed (No 2)* [1991] 4 All ER 961 at p.969:

> It is, as Lonrho submits, the independent jurisdiction of equity, as a court of conscience, to grant relief for every species of fraud and other unconscionable conduct. When appropriate, the court will grant a proprietary remedy to restore to the plaintiff property of which he has been wrongly deprived, or to prevent the defendant from retaining a benefit which he has obtained by his own wrong. It is not possible, and it would not be desirable, to attempt an exhaustive classification of the situations in which it will do so. Equity must retain what has been called its 'inherent flexibility and capacity to adjust to new situations by reference to mainsprings of the equitable jurisdiction': see Meagher, Gummow and Lehane *Equity: Doctrines and Remedies* (2nd edn, 1984) para 1207. All courts of justice proceed by analogy, but a court of equity must never be deterred by the absence of a precise analogy, provided that the principle invoked is sound.

Consequently, there is scope for equity to expand the contexts in which constructive trusts may apply, in essence as a means of ensuring that a person does not deny another that which the latter has a legitimate entitlement to expect.

ACTIVITY

Using the electronic resources available at your institution (LexisNexis/Westlaw) search for journal articles using the following key words:

'Resulting trust'

'Constructive trust'

'Proprietary estoppel'

'Remedial constructive trust'.

Read some of the articles that are retrieved by the search, and consider the ways in which the current law may expand in future.

The law of implied trusts is a fascinating area of law, and one that continues to generate considerable debate. As has been shown, a number of issues arise, such as the distinction between constructive trusts of the family home and other types of constructive trusts. Nevertheless, this area of the law does demonstrate that although the trust is in some ways a legitimised form of relationship in law, in the same way as contract, agency and bailment, it also has a continued role in acting on the conscience of the wrongdoer, and correcting situations where a person has acted to the detriment of another.

Chapter summary

This chapter may be useful for assessments and assignments on:

- Implied trusts
- The distinction between constructive trusts and proprietary estoppel
- Equity's role in acting on the conscience of the wrongdoer.

Further reading

Balen, M. and Knowles, C. (2011) 'Failure to estop: rationalising proprietary estoppel using failure of basis' *Conveyancer and Property Lawyer* 176.

Barker, K. [1998] 'Rescuing Remedialism in Unjust Enrichment Law: Why Remedies Are Right' 57 *Cambridge Law Journal* 301–327.

Birks, P. (2000) 'Rights, wrongs and remedies' 20(1) *Oxford Journal of Legal Studies* 1.

Chambers, R. (2002) 'Constructive Trusts in Canada: Part I' 15 *Trusts Law International* 214–232.

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Etherton, T. (2008) 'Constructive Trusts: A New Model for Equity and Unjust Enrichment' 67 *Cambridge Law Journal* 265–287.

Etherton, T. (2009) 'Constructive trusts and proprietary estoppel: the search for clarity and principle' (2009) *Conveyancer and Property Lawyer* 104–112.

Harpum, C. (1997) 'The uses and abuses of constructive trusts: the experience of England and Wales' *Edinburgh Law Review* 437.

Hemsworth, M. (2000) '"Constructive trusts" and "constructive trustees" – what's in a name?' 19 *Civil Justice Quarterly* 154.

Hickes, A.D. (2005) 'Conceptualising the constructive trust' 56 *Northern Ireland Legal Quarterly* 521.

Sloan, B. (2009) 'Estop me if you've heard it' 68 *Cambridge Law Journal* 518–520.

Swadling, W. (2008) 'Explaining resulting trusts' 124 *Law Quarterly Review* 72.

Part 4

Varying and terminating the trust

23

Variation of trusts

Chapter outline

This chapter will cover:

- The grounds for varying a trust
- Variation of the trust by adult beneficiaries
- Variation by statute
- Variations sanctioned by the court
- Illegality/impossibility.

Introduction

In the context of family trusts in particular, it occasionally becomes necessary to vary the terms of a trust. In some cases there may be a sense of necessity – or at least urgency – that drives the variation, such as where the settlor has created a trust of a house which is falling into disrepair. It may be necessary in such circumstances to vary the trust, for example by selling the trust property and investing the proceeds, in order to prevent the fund from being exhausted by costly repairs to the property. A variation may be required for other reasons, such as the more effective management of the trust fund. In yet other situations, variation may not be necessary, but may nevertheless be expedient, such as where it is considered appropriate to delay the age at which the beneficiaries will become entitled to the trust fund, to allow them time to acquire greater maturity and prudence in financial matters.

Ordinarily, any variation would be regarded as a breach of the trust – the trustee(s) have not acted in accordance with the settlor's expressed wishes. However, it is acknowledged that it may be necessary to vary the terms of the trust, either as a means of realising the settlor's overarching intentions or in order to ensure that the trust fund is not tied up in a manner that is unnecessarily restrictive.

The grounds for varying a trust

The law permits the variation of a trust on one of four grounds, namely:

- if the variation is sanctioned by all the beneficiaries: in order to be able to sanction a variation, the beneficiaries must all be *sui juris*, i.e. all of adult age, and have the capacity to understand and to give valid consent to the proposed variation;
- if the variation is sanctioned by statute;
- if the variation is sanctioned by a court;
- if the terms of the trust are either illegal or impossible to carry out.

Each of these will be considered below.

Variation by adult beneficiaries

The rule known as the '*Saunders v Vautier* principle' ([1835–42] All ER Rep 58) allows the terms of the trust to be varied by beneficiaries who are *sui juris*. Provided that all the beneficiaries give their consent to the variation, there will be no breach of trust on behalf of the trustees if they carry out the beneficiaries' wishes. The reasoning behind this principle is that the trustees' obligation is to the beneficiaries. Adult beneficiaries who are not suffering from any incapacity are able to determine for themselves what their best interests are. Accordingly, they may vary the terms of the trust, and even require that the trust be terminated.

EXTRACT

Saunders v Vautier [1835–42] All ER Rep 58

Case facts

The testator created a will whereby his great-nephew, Daniel Vautier, would receive company stocks once he reached the age of 25. He also gave the residue of his estate to Daniel Vautier

and his wife for their lifetime and thereafter to their children. Daniel Vautier, however, died during his great-uncle's lifetime, and his son sought to vary the trust so that it could be transferred to him before he reached the age of 25.

Lord Cottenham LC

It is argued that the testator's great-nephew, Daniel Wright Vautier, does not take a vested interest in the East India stock before his age of twenty-five, because there is no gift but in the direction to transfer the stock to him at that age. But is that so? There is an immediate gift of the East India stock; it is to be separated from the estate and vested in trustees; and the question is whether the great-nephew is not the cestui qua trust of that stock. It is immaterial that these trustees are also executors; they hold the East India stock as trustees, and that trust is to accumulate the income till the great-nephew attains twenty-five, and then to transfer and pay the stock and accumulated interest to him, his executors, administrators or assigns. There is no gift over; and the East India stock either belongs to the great-nephew or will fall into the residue in the event of his dying under twenty-five. I am clearly of opinion that he is entitled to it. If the gift were within the rule, there would be circumstances to take it out of its operation. There is not only the gift of the intermediate interest . . . but a positive direction to separate the legacy from the estate, and to hold it on trust for the legatee when he shall attain twenty-five . . . It was observed that the transfer is to be made to the great-nephew, his executors, administrators or assigns. It is true that the addition of those words does not prevent the lapse of a legacy by the death of the legatee in the lifetime of the testator, but they are not to be overlooked when the question is whether the legacy became vested before the age specified; because, if it were necessary that the legatee should live till that age to be entitled to the legacy, then there would be no question about his representatives at that time.

I am, therefore, of opinion that the order of 1835 was right, and that the petition of re-hearing must be dismissed, and with costs; which I should not have ordered, if the Master of the Rolls had recommended the parties to adopt that proceeding on a view of the merits of the case, but which I am now informed was not the case. The order for a transfer of the funds on the regular evidence of the legatee having attained twenty-one will follow this decision on the construction of the will.

Variation by statute

Two statutes permit the variation of a trust, and these are of very precise application. The first of these is s.7 Lands Clauses Consolidation Act 1845,[1] which relates to the right to sell land that is the subject of a compulsory purchase order. In the case of a trust whose subject matter is land, a compulsory purchase order would necessarily vary the terms of the trust. Accordingly, because this is permitted by the Lands Clauses Consolidation Act 1845, no breach of trust will arise from such a variation.

The second statutory provision that permits a variation of a trust is s.108 Settled Land Act 1925.[2] This section provides that where there is a conflict between the terms of a settlement and the terms of a trust, the terms of the settlement would prevail, and accordingly, a variation in the terms of the trust to give effect to this would be valid. A settlement is an arrangement whereby land is given to a person under a limited form of trust such as a fee tail, a life interest or a contingent fee simple. Under such a trust, the beneficiary

[1] (1845 c.18).
[2] (1925 c.18).

would never become the absolute owner of the trust property. No new settlements can be created after 1 January 1997,[3] although settlements created before this date will continue to be valid.

Variation sanctioned by the court

Historically, the courts have displayed a singular reluctance to sanction the variation of a trust, although they do have an inherent jurisdiction to vary the trust where necessary, such as in the case of *Re Jackson* (1882) 21 Ch D 786, where the trust was varied in order to allow the trust fund to be used to repair a building that was the subject of the trust.

Nevertheless, unless the trust instrument prevents the adequate administration of the trust, the courts have been reluctant to vary trusts. The prevailing attitude was that a court should not override the settlor's intentions. Accordingly, in *Re New* [1901] 2 Ch 534, Romer LJ's view was to emphasise that the court should only intervene and sanction a variation of a trust where some emergency necessitated such conduct.

EXTRACT

Re New [1901] 2 Ch 534

Case facts

The three settlors (New, Leavers and Morley) in this case each created trusts consisting of shares in a company called the Wollaton Colliery Company, Limited. Some years after the trusts were created the directors of the Wollaton Colliery Company, Limited decided to wind that company up voluntarily and to create a new company called 'The Wollaton Collieries Company, Limited', and to issue shares and debentures to all the shareholders of the old company. The company's shareholders, including the trustees of the three trusts, agreed to this scheme. However, the trustees were concerned that the beneficiaries of the trusts they were responsible for administering, could not, because of their age and capacity, all consent to the proposal. Accordingly, they applied to the court for approval of the scheme.

Romer LJ

As a rule, the Court has no jurisdiction to give, and will not give, its sanction to the performance by trustees of acts with reference to the trust estate which are not, on the face of the instrument creating the trust, authorized by its terms . . . But in the management of a trust estate, and especially where that estate consists of a business or shares in a mercantile company, it not infrequently happens that some peculiar state of circumstances arises for which provision is not expressly made by the trust instrument, and which renders it most desirable, and it may be even essential, for the benefit of the estate and in the interest of all the cestuis que trust, that certain acts should be done by the trustees which in ordinary circumstances they would have no power to do . . . Of course, the jurisdiction is one to be exercised with great caution, and the Court will take care not to strain its powers. It is impossible, and no attempt ought to be made, to state or define all the circumstances under which, or the extent to which, the Court will exercise the jurisdiction; but it need scarcely be said that the Court will not be justified in sanctioning every act desired by trustees and beneficiaries merely because it may appear

[3] Trusts of Land and Appointment of Trustees Act 1996, Schedule 4.

beneficial to the estate; and certainly the Court will not be disposed to sanction transactions of a speculative or risky character. But each case brought before the Court must be considered and dealt with according to its special circumstances . . .

On this basis, the court considered it appropriate for the variation of the trust to be sanctioned.

Nevertheless, it has been emphasised that although the court is willing to vary the terms of a trust so that it continues to fulfil the settlor's expressed objectives – as in the case of *Re New*, above, there is no justification in disregarding or rewriting the trust, as was shown in *Chapman v Chapman* [1954] AC 429.

EXTRACT

Chapman v Chapman [1954] AC 429

Case facts

A number of trusts were created. However, the way in which they were worded made it likely that a considerable amount of tax would be payable because of two clauses in the trust instrument that provided for the maintenance of the children of one of the beneficiaries. Accordingly, a scheme was devised that would legitimately allow this to be avoided, by removing the maintenance clauses. This would provide the beneficiaries identified in the trusts with a larger portion of the trust fund, by avoiding the estate duty that would become payable on the death of the settlors. The court was required to consent to the variation on behalf of all those beneficiaries who could not consent to the variation on their own account, namely those who were children, and future beneficiaries not yet born.

Lord Simonds

We are as little justified in saying that a court has a certain jurisdiction, merely because we think it ought to have it, as we should be in declaring that the substantive law is something different from what it has always been declared to be, merely because we think it ought to be so. It is even possible that we are not wiser than our ancestors. It is for the legislature, which does not rest under that disability, to determine whether there should be a change in the law and what that change should be.

My Lords, I have indicated what is, in my view, the proper approach to the problem and do not propose to traverse the ground which has been so ably covered by the majority of the Court of Appeal and will be explored again by my noble and learned friends. The major proposition I state in the words of one of the great masters of equity. 'I decline,' said Farwell J. in *In re Walker* [[1901] 1 Ch 879], 'to accept any suggestion that the court has an inherent jurisdiction to alter a man's will because it thinks it beneficial. It seems to me that is quite impossible.' It should then be asked what are the exceptions to this rule. They seem to me to be reasonably clearly defined. There is no doubt that the Chancellor (whether by virtue of the paternal power or in the execution of a trust, it matters not) had and exercised the jurisdiction to change the nature of an infant's property from real to personal estate and vice versa, though this jurisdiction was generally so exercised as to preserve the rights of testamentary disposition and of succession. Equally, there is no doubt that from an early date the court assumed the power, sometimes for that purpose ignoring the direction of a settlor, to provide maintenance for an infant, and, rarely, for an adult, beneficiary. So, too, the court had power in the administration of trust property to direct that by way of salvage some transaction unauthorized by the trust instrument

should be carried out. Nothing is more significant than the repeated assertions by the court that mere expediency was not enough to found the jurisdiction. Lastly, and I can find no other than these four categories, the court had power to sanction a compromise by an infant in a suit to which that infant was a party by next friend or guardian ad litem. This jurisdiction, it may be noted, is exercisable alike in the Queen's Bench Division and the Chancery Division and whether or not the court is in course of executing a trust.

This brings me to the question which alone presents any difficulty in this case. It is whether this fourth category, which I may call the compromise category, should be extended to cover cases in which there is no real dispute as to rights and, therefore, no compromise, but it is sought by way of bargain between the beneficiaries to rearrange the beneficial interests under the trust instrument and to bind infants and unborn persons to the bargain by order of the court.

My Lords, I find myself faced at once with a difficulty which I do not see my way to overcome. For though I am not as a rule impressed by an argument about the difficulty of drawing the line since I remember the answer of a great judge that, though he knew not when day ended and night began, he knew that midday was day and midnight was night, yet in the present case it appears to me that to accept this extension in any degree is to concede exactly what has been denied. It is the function of the court to execute a trust, to see that the trustees do their duty and to protect them if they do it, to direct them if they are in doubt and, if they do wrong, to penalize them. It is not the function of the court to alter a trust because alteration is thought to be advantageous to an infant beneficiary. It was, I thought, significant that counsel was driven to the admission that since the benefit of the infant was the test, the court had the power, though in its discretion it might not use it, to override the wishes of a living and expostulating settlor, if it assumed to know better than he what was beneficial for the infant. This would appear to me a strange way for a court of conscience to execute a trust. If, then, the court has not, as I hold it has not, power to alter or rearrange the trusts of a trust instrument, except within the limits which I have defined, I am unable to see how that jurisdiction can be conferred by pleading that the alteration is but a little one.

Accordingly, the House of Lords did not consider that it could consent to the variation on behalf of the beneficiaries who were not *sui juris*.

Exercise of the courts' inherent jurisdiction to vary trusts

The only ways in which a court has exercised its inherent jurisdiction to vary the terms of a trust is either to change a minor's property[4] or in order to arrange a compromise between minors and future beneficiaries. An example of compromise may be seen in the case of *Re Lord Hylton's Settlement*.[5] Here, a trust was created which provided an income for one of the beneficiaries (Lord Hylton) for his lifetime, and thereafter on a discretionary trust for Lord Hylton's wife and children. Lord Hylton sought to vary the trust so as

[4] In the case of *In Re Jackson; Jackson v Talbot* (1882) 21 Ch D 786, the testator created a trust of his house in favour of an infant beneficiary. The house was falling into disrepair, and therefore the trustees applied to the court to sanction a variation in the terms of the trust that would allow them to mortgage the house in order to pay for the cost of repairing it. The court allowed the variation, but only to the extent of covering the costs of repairs that were absolutely necessary.

[5] *Re Lord Hylton's Settlement; Barclays Bank v Jolliffe and Others* [1954] 2 All ER 647.

to confer the fund in its entirety on his eldest son – the appellant. The court was therefore required to consent to this variation on behalf of the younger children who were not of age to give consent. By the time the matter had come before the Court of Appeal, the parties had agreed on a compromise arrangement, whereby a portion of the trust fund was reserved on trust for the benefit of Lord Hylton's wife and younger children, with the rest being given immediately to the eldest son.

Although the Court of Appeal accepted that this varied the beneficial interests under the trust, they accepted that they had the jurisdiction to sanction the variation because a compromise necessitates a dispute between the parties. If there is such a dispute therefore, the court is not acting to alter the trust because, according to Lord Moreton in *Chapman v Chapman*, the existence of the dispute means that the trusts are still in doubt and the beneficial interests cannot be ascertained until the matter is resolved by the court:

> Where rights are in dispute and the court approves a compromise it is not altering the trusts, for the trusts are, ex hypothesi, still in doubt and unascertained.

Accordingly, in *Re Lord Hylton's Settlement* there was a dispute because the parties could not agree whether the trust could be varied in its entirety or whether only the interest in remainder could be varied. On the other hand, there was no such dispute in *Chapman v Chapman*, and therefore the court could not intervene.

The court will exercise its inherent jurisdiction in order to effect the appropriate management of the trust property, or in the case of emergency or a need to salvage the trust property. Accordingly, in the case of *Re New* [1901] 2 Ch 534, Romer LJ explains:

> As a rule, the Court has no jurisdiction to give, and will not give, its sanction to the performance by trustees of acts with reference to the trust estate which are not, on the face of the instrument creating the trust, authorized by its terms . . . But in the management of a trust estate, and especially where that estate consists of a business or shares in a mercantile company, it not infrequently happens that some peculiar state of circumstances arises for which provision is not expressly made by the trust instrument, and which renders it most desirable, and it may be even essential, for the benefit of the estate and in the interest of all the cestuis que trust, that certain acts should be done by the trustees which in ordinary circumstances they would have no power to do . . . By way merely of illustration, we may take the case where a testator has declared that some property of his shall be sold at a particular time after his death, and then, owing to unforeseen change of circumstances since the testator's death, when the time for sale arrives it is found that to sell at that precise time would be ruinous to the estate, and that it is necessary or right to postpone the sale for a short time in order to effect a proper sale: in such a case the Court would have jurisdiction to authorize, and would authorize, the trustees to postpone the sale for a reasonable time . . .

Occasionally the courts have varied the terms of a trust to allow remuneration for the exceptional work of a trustee. This is discussed at length by Fox LJ in *In Re Duke of Norfolk's Settlement Trust* [1982] Ch 61, although this case was concerned predominantly with the question of whether the court had the jurisdiction to sanction an increase in the remuneration permitted by the trust instrument. Nevertheless, in general, the courts' powers to vary the terms of a trust are limited, and the courts have been extremely reluctant to extend this authority.

EXTRACT

Re Duke of Norfolk's Settlement Trust [1982] Ch 61

Case facts

Here, the trust instrument permitted the trustees to receive remuneration for their work. The question for the court therefore was whether the court could sanction an increase in that amount. In the High Court, Walton J had dismissed the application on the basis that the court could only allow remuneration for the exceptional work of an individual trustee who had provided a benefit to the trust that surpassed all expectations.

Fox LJ

There is, in my judgment, no doubt that the court has an inherent jurisdiction to authorise payment of remuneration to trustees. Danckwerts J. in *In re Masters, decd.* [1953] 1 W.L.R. 81 and Upjohn J. in *In re Worthington, decd.* [1954] 1 W.L.R. 526 accept that. The older authorities lead me to the same conclusion. In *Marshall v. Holloway*, 2 Swan. 432, Lord Eldon L.C. himself authorised remuneration for both past and future services . . .

The question is the extent of that jurisdiction. There can, in my view, be no doubt that there is an inherent jurisdiction, upon the appointment of a trustee, to direct that he be remunerated . . . In the present case, however, what is sought is the increase of remuneration authorised by the trust instrument . . . If it be the law, as I think it clearly is, that the court has inherent jurisdiction on the appointment of a trustee to authorise payment of remuneration to him, is there any reason why the court should not have jurisdiction to increase the remuneration already allowed by the trust investment?

Two reasons are suggested. First, it is said that a trustee's right to remuneration under an express provision of the settlement is based upon a contract between the settlor and the trustee which the trustee is not entitled to avoid; the benefit of that contract is to be regarded as settled by the trust instrument for the benefit of the beneficiaries. I find that analysis artificial. It may have some appearance of reality in relation to a trustee who, at the request of the settlor, agrees to act before the settlement is executed and approves the terms of the settlement. But very frequently executors and trustees of wills know nothing of the terms of the will until the testator is dead; sometimes in the case of corporate trustees such as banks, they have not even been asked by the testator whether they will act. It is difficult to see with whom, in such cases, the trustees are to be taken as contracting. The appointment of a trustee by the court also gives rise to problems as to the identity of the contracting party.

The position, it seems to me, is this. Trust property is held by the trustees upon the trusts and subject to the powers conferred by the trust instrument and by law. One of those powers is the power to the trustee to charge remuneration. That gives the trustee certain rights which equity will enforce in administering the trust. How far those rights can properly be regarded as beneficial interests I will consider later. But it seems to me to be quite unreal to regard them as contractual. So far as they derive from any order of the court they simply arise from the court's jurisdiction and so far as they derive from the trust instrument itself they derive from the settlor's power to direct how his property should be dealt with . . .

I come to the second objection. It is said that the right to remuneration is a beneficial interest in the trust property and can only be varied by an order under the Variation of Trusts Act 1958 or, in accordance with the principles established in *Chapman v. Chapman* [1954] A.C. 429, under a compromise of a dispute as to beneficial interests or by way of salvage.

I do not doubt that, to some extent, the right of a trustee to remuneration is to be regarded as a beneficial interest. Thus, in *In re Pooley* (1888) 40 Ch.D. 1 it was held that a trustee who was an attesting witness of a will was not entitled to claim remuneration under the express provisions of the will because section 15 of the Wills Act 1837 precluded an attesting witness from claiming benefits under the will; the benefit of the remuneration clause was, in effect, a legacy. Again in *In re Thorley* [1891] 2 Ch. 613 trustees were entitled to £250 per annum each under the provisions of the will while they carried on the testator's business. It was held that these benefits were legacies and subject to legacy duty. And in *In re White* [1898] 2 Ch. 217 the benefits given by a trustee remuneration clause were treated as bounty.

In In re Thorley and In re White there were substantial reasons of policy why the remuneration should be treated as a beneficial interest. It would not be acceptable that a testator should be able to confer upon trustees such benefits as he might choose, in the guise of remuneration, to the disadvantage of creditors and in avoidance of death duties . . . But accepting that a trustee's right to remuneration may for certain purposes be treated as a beneficial interest in the trust property, I do not think that it comes within the principle laid down in *Chapman v. Chapman* [1954] A.C. 429 as to the general inability of the court under its inherent jurisdiction to vary beneficial interests . . . *Chapman v. Chapman*, it seems to me, was concerned with the power of the court to authorise variations in beneficial interests as such. The present problem is different. It is concerned not with beneficial interests as such, but with the administration of the trust fund. When the court authorises payment of remuneration to a trustee under its inherent jurisdiction it is, I think, exercising its ancient jurisdiction to secure the competent administration of the trust property just as it has done when it appoints or removes a trustee under its inherent jurisdiction. The result, in my view, is that there is nothing in the principles stated in *Chapman v. Chapman* which is inconsistent with the existence of an inherent jurisdiction in the court to increase the remuneration payable to trustees under the trust instrument.

In my view, therefore, neither of the two objections which have been raised as to existence of such a jurisdiction is well founded.

There remains the question whether, upon principle and authority, we can properly infer that the jurisdiction does exist.

As to principle, it seems to me that if the court has jurisdiction, as it has, upon the appointment of a trustee to authorise remuneration though no such power exists in the trust instrument, there is no logical reason why the court should not have power to increase the remuneration given by the instrument. In many cases the latter may involve a smaller interference with the provisions of the trust instrument than the former. Further, the law has not stopped short at authorising remuneration to a trustee only if he seeks the authority at the time when he accepts the trusts. That, in my view, appears from the observations of Lord Langdale M.R. in *Bainbrigge* v. *Blair*, 8 Beav. 588, and from *In re Masters, decd.* [1953] 1 W.L.R. 81 in which it is clear that Danckwerts J. would have been prepared to make the order which he did (and which authorised payment of remuneration to an administrator who had taken a grant some years previously) under the inherent jurisdiction.

I appreciate that the ambit of the court's inherent jurisdiction in any sphere may, for historical reasons, be irrational and that logical extensions are not necessarily permissible. But I think that it is the basis of the jurisdiction that one has to consider. The basis, in my view, in relation to a trustee's remuneration is the good administration of trusts . . . If the increase of remuneration be beneficial to the trust administration, I do not see any objection to that in principle.

As to authority, I do not find in the English authorities any decision which positively excludes any inherent jurisdiction to increase remuneration, unless it be *Robinson v. Pett*, 3 P.Wms. 249.

But that was a case of a renouncing executor who was expressly given a legacy for his trouble if he did renounce. Lord Talbot L.C. said that he was unable to give him any more. I do not think *Robinson v. Pett* really touches the present case . . . I conclude that the court has an inherent jurisdiction to authorise the payment of remuneration of trustees and that that jurisdiction extends to increasing the remuneration authorised by the trust instrument. In exercising that jurisdiction the court has to balance two influences which are to some extent in conflict. The first is that the office of trustee is, as such, gratuitous; the court will accordingly be careful to protect the interests of the beneficiaries against claims by the trustees. The second is that it is of great importance to the beneficiaries that the trust should be well administered. If therefore the court concludes, having regard to the nature of the trust, the experience and skill of a particular trustee and to the amounts which he seeks to charge when compared with what other trustees might require to be paid for their services and to all the other circumstances of the case, that it would be in the interests of the beneficiaries to increase the remuneration, then the court may properly do so.

Having regard to the view which I take as to the inherent jurisdiction, it is not necessary to consider the extent of the court's jurisdiction under section 57 of the Trustee Act 1925 or otherwise.

I would allow the appeal, and make the declaration sought by the amended summons so far as it relates to the inherent jurisdiction. The matter should, I think, be remitted to the Chancery Division to enable the trustees to make such application and upon such further evidence as they think fit.

Although the courts therefore have some scope to vary trusts, the judgment in *Chapman v Chapman* has been seen to inhibit the variation of trusts unduly. Prior to this case, the courts had exercised their inherent jurisdiction to vary trusts in a fairly liberal fashion. In the aftermath of *Chapman v Chapman*, a number of trusts were rendered worthless or nearly worthless because of the amount of tax payable because the court refused to allow trusts to be varied. Accordingly, in 1958, the Variation of Trusts Act 1958[6] was enacted. This Act allows the court to approve a variation of a trust on behalf of those who cannot give approval on their own account. Section 1(1) identifies those persons.

EXTRACT

Variation of Trusts Act 1958, s.1(1)

1 Jurisdiction of courts to vary trusts

(1) Where property, whether real or personal, is held on trusts arising, whether before or after the passing of this Act, under any will, settlement or other disposition, the court may if it thinks fit by order approve on behalf of –

(a) any person having, directly or indirectly, an interest, whether vested or contingent, under the trusts who by reason of infancy or other incapacity is incapable of assenting, or

(b) any person (whether ascertained or not) who may become entitled, directly or indirectly, to an interest under the trusts as being at a future date or on the happening of a future event a person of any specified description or a member of any specified

[6] (1958 c.53).

class of persons, so however that this paragraph shall not include any person who would be of that description, or a member of that class, as the case may be, if the said date had fallen or the said event had happened at the date of the application to the court, or

(c) any person unborn, or

(d) any person in respect of any discretionary interest of his under protective trusts where the interest of the principal beneficiary has not failed or determined,

any arrangement (by whomsoever proposed, and whether or not there is any other person beneficially int sted who is capable of assenting thereto) varying or revoking all or any of the trusts, or enlarging the powers of the trustees of managing or administering any of the property subject to the trusts:

Provided that except by virtue of paragraph (d) of this subsection the court shall not approve an arrangement on behalf of any person unless the carrying out thereof would be for the benefit of that person.

The effect of the Variation of Trusts Act 1958 is to reformulate the concept of the courts' powers. Under the Act the court does not actually vary the trust, it merely gives its approval to a variation proposed by the trustees. However, the court may only consent to the variation of a trust where it is for the benefit of the person for whom consent is being given. However, where consent is required from the court under s.1(1)(d) there is no requirement that the variation will benefit those persons, although this does not mean that their interests may be disregarded entirely.[7]

Otherwise, the Act permits the court to consent to any variation or even to the termination of the trust, and the court takes a broad view of what is meant by the term 'benefit'. Thus, the court may permit a modification of the trustees' powers and their powers to invest, and will even approve variations where there may be some element of risk, provided that it is a risk that an adult beneficiary of full capacity would be prepared to take. An example may be seen in the case of *Re Cohen's Settlement Trusts* [1959] 3 All ER 523, where the proposed variation to a trust was likely to be advantageous to the testator's infant grandchildren, on whose behalf the court's consent was sought. However, this advantage would be eliminated if the children's mother died before the testator's 80-year-old widow. The court considered that although it was possible for a person young enough to be the mother of infant children to die before an 80 year old, an adult beneficiary would be likely to accept that small risk, and the court was therefore willing to consent to the variation.

A variation may be approved of even if one of its objectives is to reduce the amount of tax that would otherwise become payable. Accordingly, although the application to vary the trust was rejected in the case of *Chapman v Chapman*, the courts were willing to consent to the variation on behalf of those who could not give consent once the Variation of Trusts Act 1958 had come into force.[8]

Furthermore, the benefit conferred by the variation need not be financial – it may be that the variation of the trust will confer some educational or social benefit. In the case of *Re Holt's Settlement Trust* [1969] 1 Ch 100, a trust was created which granted a life interest to one Patricia Wilson, and the remainder to go to her children when they reached the age of 21. Mrs Wilson wished to vary the trust, by surrendering her life interest, but delaying her children's entitlement until they reached the age of 30. She argued that

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[7] See Wilberforce J in *Re Burney's Settlement Trusts* 1 All ER 856 at p.858.

[8] *Re Chapman's Settlement Trusts (No 2)* [1959] 2 All ER 47.

the income they would receive from the trust would be too substantial for them at the age of 21. Megarry J concurred, explaining:

> I can deal with the merits of this application quite shortly. It seems to me that, subject to one reservation, the arrangement proposed is for the benefit of each of the beneficiaries contemplated by section 1 (1) of the Act of 1958. The financial detriment to the children is that the absolute vesting of their interests will be postponed from age 21 to age 30. As against that, they will obtain very substantial financial benefits, both in the acceleration of their interests in a moiety of the trust fund and in the savings of estate duty to be expected in a case such as this. Where the advantages of the scheme are overwhelming, any detailed evaluation, or 'balance-sheet' of advantages and disadvantages, seems to me to be unnecessary; but I can imagine cases under the Act where it may be important that an attempt should be made to put in evidence a detailed evaluation of the financial and other consequences of the changes proposed to be made, so that it may be seen whether on balance there is a sufficient advantage to satisfy the proviso to section 1 (1). But this is not such a case, and I say no more about it. I should, however, state that I fully concur in the view taken by Mrs. Wilson that, speaking in general terms, it is most important that young children 'should be reasonably advanced in a career and settled in life before they are in receipt of an income sufficient to make them independent of the need to work.' The word 'benefit' in the proviso to section 1 (1) is, I think, plainly not confined to financial benefit, but may extend to moral or social benefit, as is shown by *In re T.'s Settlement Trusts* [[1964] Ch 158].

On the other hand in *In Re Weston's Settlements* [1969] 1 Ch 223, the Court of Appeal declined to authorise the variation of a trust that would see it, for the reason of avoiding tax, administered from Jersey. Lord Denning MR explained:

> There is one reported case in which a scheme on these lines was approved. It was *In re Seale's Marriage Settlement* [[1961] Ch 574]. In that case husband and wife married in 1931 . . . They had three children who appear to have been born in England. But when the children were quite small the family emigrated to Canada. The children were brought up as Canadians and were likely to continue to live in Canada . . . It was obviously advantageous for the settlement to be turned from an English settlement into a Canadian settlement . . . Those advising Mr. Weston ask the court to approve a similar scheme here. The judge refused. He said that this was a 'cheap exercise in tax avoidance' which he ought not to sanction: but he hoped that the case would be taken to the Court of Appeal so as to have the views of this court . . . Two propositions are clear: (i) In exercising its discretion, the function of the court is to protect those who cannot protect themselves. It must do what is truly for their benefit. (ii) It can give its consent to a scheme to avoid death duties or other taxes. Nearly every variation that has come before the court has tax avoidance for its principal object: and no one has ever suggested that this is undesirable or contrary to public policy. But I think it necessary to add this third proposition: (iii) The court should not consider merely the financial benefit to the infants or unborn children, but also their educational and social benefit. There are many things in life more worth while than money. One of these things is to be brought up in this our England, which is still 'the envy of less happier lands.' I do not believe it is for the benefit of children to be uprooted from England and transported to another country simply to avoid tax. It was very different with the children of the Seale family, which Buckley J. considered. That family had emigrated to Canada many years before, with no thought of tax avoidance, and had brought up the children there as Canadians. It was very proper that the trust should be transferred to

Canada. But here the family had only been in Jersey three months when they presented this scheme to the court. The inference is irresistible: the underlying purpose was to go there in order to avoid tax. I do not think that this will be all to the good for the children. I should imagine that, even if they had stayed in this country, they would have had a very considerable fortune at their disposal, even after paying tax. The only thing that Jersey can do for them is to give them an even greater fortune. Many a child has been ruined by being given too much. The avoidance of tax may be lawful, but it is not yet a virtue. The Court of Chancery should not encourage or support it – it should not give its approval to it – if by so doing it would imperil the true welfare of the children, already born or yet to be born. There is one thing more. I cannot help wondering how long these young people will stay in Jersey. It may be to their financial interest at present to make their home there permanently. But will they remain there once the capital gains are safely in hand, clear of tax? They may well change their minds and come back to enjoy their untaxed gains. Is such a prospect really for the benefit of the children? Are they to be wanderers over the face of the earth, moving from this country to that, according to where they can best avoid tax? I cannot believe that to be right. Children are like trees: they grow stronger with firm roots. The long and short of it is, as the judge said, that the exodus of this family to Jersey is done to avoid British taxation. Having made great wealth here, they want to quit without paying the taxes and duties which are imposed on those who stay. So be it. If it really be for the benefit of the children, let it be done. Let them go, taking their money with them. But, if it be not truly for their benefit, the court should not countenance it. It should not give the scheme its blessing. The judge refused his approval. So would I. I would dismiss this appeal.

Variation of Trusts Act 1958

Section 1(1)(a)

Sui juris beneficiaries (i.e. adult beneficiaries with full capacity) are able to approve any variation of a trust, and the court's role therefore is merely to represent the interests of those who are unable to consent to a variation of the trust, and to give consent on their behalf. The persons on whose behalf the court is able to give consent include those who are existing beneficiaries of the trust (s.1(1)(a)) but also those who may acquire an interest in the trust in the future. For example, Tess creates a trust for the benefit of her husband Benny, with a proviso that if Benny should die, the fund should pass to her infant son Tom. Tom is not a beneficiary under the trust at this point – he will only inherit if Benny dies during Tom's lifetime – if Benny does not do so, then Tom obtains no entitlement to the fund. Nevertheless, if the trustees were to apply to vary the trust, they could approve a variation on behalf of Tom even where his interest is merely contingent. Accordingly, s.1(1)(a) permits the court to approve a variation of a trust on behalf of any person having, directly or indirectly, an interest, whether vested or contingent, under the trusts but who by reason of minority or other incapacity is incapable of assenting.

Accordingly, if Sam writes a will leaving £100,000 to his wife Jane, or in the event of her death before him, to his five-year-old granddaughter Kate, the trustees may decide to vary this trust so as to permit Kate to inherit the fund, even if Jane survives Sam. Jane could consent to this variation of her own volition, as it may be a way of avoiding inheritance tax being payable on the fund on both Sam and Jane's deaths. Kate cannot consent to the variation however because she is under the age of 18. Accordingly, s.1(1)(a) would permit the court to give consent to the variation on Kate's behalf.

Section 1(1)(b)

Section 1(1)(b) of the Variation of Trusts Act allows for the court to approve a variation on behalf of, for example, a person who may be appointed or nominated at some point in the future, but who has not yet been specifically identified. For example, if John writes a will leaving his estate to his daughter Mary for her lifetime, with a proviso that she may nominate who is to be entitled to the trust fund on her death, a court would have to approve any variation of the trust on behalf of the unknown person whom Mary may nominate in the future, whether that person is a child or an adult.

The case of *Knocker v Youle* [1986] 2 All ER 914 however indicates that the court cannot approve a variation of a trust under s.1(1)(b) if the beneficiaries have been identified and will inherit even if a number of contingencies must occur before that can happen. Here, the settlor created a trust for the benefit of his daughter for her lifetime, with a proviso that she should nominate who should be entitled to the trust fund on her death. If she failed to nominate a beneficiary, the fund would be held on trust for the settlor's wife for her lifetime or until she remarried, and thereafter it was to be distributed between the settlor's sisters and their children. The daughter sought to vary the trust, and sought the court's approval under s.1(1)(b) on behalf of the settlor's sisters' children, many of whom were adults. Warner J concluded that the sisters' children were not future beneficiaries for the purposes of the Act – their interest in the trust was in fact current, albeit contingent both upon the settlor's daughter dying before nominating beneficiaries, and upon the younger beneficiaries reaching the age of 21. Riddall considers this to be extremely problematic, in that he argues that excluding the scope of the courts to approve a variation of a trust on behalf of those whose interests are contingent leaves a significant lacuna in the law, in that the court may approve a variation on behalf of beneficiaries who are not *sui juris* whose interest is contingent, but it cannot approve a variation on behalf of those who are capable adults but who have nevertheless not been fully ascertained (as in the case where the discretion to select beneficiaries is limited to a specific class of persons). Because such persons are not yet beneficiaries under the trust, they cannot, however, give consent to the variation on their own account. Furthermore, Riddall also poses the question of who *is* envisaged by s.1(1)(b) if the section does not include those with a current but contingent interest in the trust fund.

EXTRACT

Riddall, J.G. (1987) 'Does it or doesn't it? Contingent interests and the Variation of Trusts Act 1958' *Conveyancer and Property Lawyer* 144

The decision of the learned judge that paragraph (b) does not cover a person with contingent interest presents a number of difficulties. One is that the interpretation would appear not to be in accord with the intention of the legislature in the restriction it places on the persons on whose behalf consent may be given. This, of course, may present difficulties in practice, but the matter need not detain us here since if this is what the statute enacts, then, unless there is an amendment, there is no more to be said.

A second difficulty is concerned with determining the consequences of the decision. If the section covers only persons who have no interest in trust property whatsoever, just whom does it cover? What about objects under a power of appointment? They have no interest in the trust property, and they may, i.e. on the exercise of the power, become entitled to an interest. So the section would seem to cover such objects of a power. But can we really say that an object of a

pure power is a person who may become entitled as being at a future date or on the happening of a future event a person of any specified description or a member of any specified class of persons? It is true that on the happening of a future event, the exercise of the power in his favour, he becomes entitled to any interest. But does he become entitled as being a person of any specified description, or a member of any specified class of persons? Surely not. He is a member of the class (i.e. of objects) from the outset. (He becomes entitled as being the person to whom the donee's finger points.) Perhaps the meaning of the paragraph can be interpreted so as to include an object of a pure power but, it must surely be admitted, the wording has to be strained almost to breaking point to achieve this result.

Can we think of anyone else who would be covered? How about a gift in remainder to 'such members of the X Gliding Club as shall be living at my death'? Approval could be given by existing members on their own behalf. But what of all the people in the world who are living at the date of the application to the court and who might join the Club between that date and A's death? Do these people have a contingent interest? It is suggested that they do. The gift is for an ascertainable class. The gift vests when a specified condition precedent is satisfied. It is therefore a contingent gift. If Warner J.'s interpretation of 1(1)(b) is correct, the class we have postulated does not provide an example of persons on whose behalf consent can be given under the paragraph. (It is true that if the class did come within the paragraph, the proviso would prevent consent from being given, but that is not the point at issue.) Presumably section 1(1)(b) must cover someone, but if not someone with a contingent interest, who?

Another difficulty arises from the fact that if Warner J.'s interpretation of the words 'may become entitled . . . to an interest' as excluding a person with a contingent interest is correct, then it becomes hard to reconcile the main provision of 1(1)(b) with the proviso. The proviso includes a person who would be of a certain description if a certain event had happened. It is arguable that such a person cannot but be regarded as having a contingent interest. But if this is so the effect is that section 1(1)(b) does not cover any person who has either a vested or a contingent interest, except for certain ones who do have a contingent interest. (The two parts are inconsistent: no houses are green, except for houses that are green.)

Another difficulty stems from the fact that if the first ground for Warner J.'s decision is correct then the decisions in *Re Suffert's Settlement* [[1961] Ch 1] and *Re Moncrief's Settlement Trusts* [[1962] 3 All ER 838], decisions which were accepted as correct in *Knocker v. Youle* [[1986] 2 All ER 914], must have been decided on the wrong grounds. In Suffert the gift was for D for life, with remainder to D's children or, if she had none, to appointees under D's will, with a gift over in default to the person who would be D's next of kin if she died intestate and unmarried. D was 61 and unmarried. If she died unmarried her next of kin would be three cousins. D and one of the cousins applied to the court for a variation of the trust which would have divided the trust fund between D and the three cousins. The court (Buckley J.) held that it could not give consent on behalf of the two cousins who were not a party to the application since each of these cousins was a person who would be of that description [D's next of kin] . . . if the said . . . event [D's death] had happened at the date of the application to the court. The corollary is that if they had not been excluded by the proviso they would have been covered by the principal provision of the section. But they could only be so covered if, according to Warner J. in *Knocker v. Youle*, they had had no interest, vested or contingent, in the property. But did they have no interest? It is submitted that D's next of kin did have a contingent interest – contingent, it is true, on D having no children, and on D not exercising the power, and on being alive at D's death, and liable to a diminution in entitlement in the event of an increase in the class of next of kin, but nevertheless a contingent interest. But if the cousins had, as we suggest, a contingent interest then the proper ground for Buckley J.'s decision should have been, not that they were excluded by the proviso but that, having an interest in the property, they were not covered by paragraph 1(1)(b) at all.

The same argument can be advanced with regard to Moncrief. In that case consent was given on behalf of four next of kin, since they were not excluded by the proviso. But these cousins, it is contended, had, like the cousins in Suffert, a contingent interest in the property and so, if Warner J. is correct, should have been treated as not being covered by section 1(1)(b).

In *Re Bristol's Settled Estates* [[1964] 3 All ER 939] approval was given on behalf of certain beneficiaries under a discretionary trust. Assuming that, as is submitted is the case, beneficiaries under a discretionary trust do have at least some interest, then, if Warner J.'s contention is correct, the court had no jurisdiction to approve the variation.

The more we delve, the more we must be driven to ask, can the exclusion of persons having a contingent interest from the coverage of 1(1)(b) be correct? After all, if we were asked what kind of interest was held by a person who would become entitled on the happening of a future event, our immediate answer would have to be that such person held a contingent interest.

As was seen above, the impetus was the judgment in *Chapman v Chapman*, which was a case where the objective behind the variation was to limit the amount of estate duty (a form of tax) that would become payable. The impact of the Variation of Trusts Act 1958 has been to permit trusts to be varied in a way that allows the amount of tax to be limited – the trust is varied in a way that means that the principal beneficiaries are those who may be lower rate tax payers or those who are more likely to live long enough to ensure that the tax burden is proportionally reduced. McCall therefore explains that following the enactment of the Variation of Trusts Act 1958, its main usage was as a way of minimising the tax burden:

> In the early days the jurisdiction gave rise to a virtual production line of cases of fixed trusts where, for example, the capital beneficiaries were not of full age or there was a possibility that further issue might be born but the aim was to avoid estate duty and to convert the life tenant's low income (net of tax) into a capital sum. Such partitions involved consideration of actuarial and so-called 'drop-dead' values, term and possibly issue risk insurance; but they followed a standard pattern.[9]

On the other hand, he explains that the scope of the Act is much broader than that. For example, it may be used to defer a child's entitlement until they are older, rather than permitting the child to become entitled to the fund in its entirety on reaching the age of 18. Similarly, in the case of a discretionary trust, such as a trust that exists for the purposes of awarding a prize to a successful student, it may be that the trust instrument limits the amount of time for which the trustees may invest the income from the trust fund before identifying a suitable beneficiary and distributing the fund. A variation of the trust may permit the trustees to invest the income for a longer period so that the fund increases in value, with the result that a larger sum may be distributed to an eligible beneficiary. Nevertheless, McCall emphasises that the advantages of the Variation of Trusts Act 1958 are not confined to family trusts:

> But the joy of the Act is essentially that where there is a problem there ought to be a solution, and the adviser can treat it like an intellectual exercise in which there must be a benefit if there can be a solution. A case in point was a trust which had a very substantial fund of shares in a public company and an interest in the possession of that company; it resisted attempts to conquer it for 20 years or more, but in the end succumbed to one of the most ingenious species of schemes within the Act, where the structure of fiscally wasteful equitable interests is replaced by a share structure

[9] McCall, C. (1996) 'Variations of Trusts: Some Observations' 389 *Private Client Business* 389 at pp.395–396.

> which reflects the equitable interests in terms of benefits secured by the issue of different classes of share to the different classes of beneficiaries. Naturally, that sort of engineering does not arise in any save the most exceptional case, but it shows the width of the jurisdiction that if such a scheme is beneficial there is every reason to suppose that it will be approved.[10]

Section 1(1)(c)

Section 1(1)(c) permits a court to vary a trust on behalf of persons unborn. Persons unborn may be capable of being beneficiaries under s.1(1)(a) or s.1(1)(b). However, the court does not approve the variation under either of these sections because s.1(1)(c) includes not only those who are *en ventre sa mère* (conceived but not yet born) but also includes those who do not yet exist at all. Therefore if Mary were to create a trust in favour of her grandchildren, it may not be known yet who those grandchildren might be. Accordingly, a court would have to consent to a variation of the trust in favour of any future grandchildren Mary might have.

Section 1(1)(d)

The fourth category of persons on whose behalf a variation of trusts may be approved is:

> any person in respect of any discretionary interest of his under protective trusts where the interest of the principal beneficiary has not failed or determined.

This fourth category is very precise in its scope. Firstly, the trust must be of a specific character, namely a protective trust. A protective trust would be a trust that confers a life interest on a beneficiary, or alternatively provides a trust for the benefit of a beneficiary until a specified event occurs. For example, a protective trust might be made for the benefit of one's spouse during their lifetime but would expire if the testator and their spouse divorced. However, if the protective trust fails during the period specified by the trustee, or the beneficiary does something that means that he or she is no longer entitled to receive the income from the trust, the trustees have the discretion either to continue to give the income from the trust to the beneficiary, or alternatively to give the income to the beneficiary's spouse or civil partner, the beneficiary's children, or any remoter issue of the beneficiary (grandchildren, great-grandchildren or other direct descendants). If the trustees wish to vary such a trust before it has failed or been brought to an end, then the court's consent will be required in relation to those in whose favour the court may exercise its discretion.

Accordingly, if Alf creates a protective trust for the benefit of his wife Barbara for her lifetime, the trustees will have the discretion to give the income from the trust to Barbara's children, Clare and Daniel, if the trust fails or if Barbara does something that means that she is no longer eligible to receive the income from the trust. During Barbara's lifetime, the court will need to give consent to any variation of the trust on Alf (if he is still alive), Barbara, Clare and Daniel's behalf. As with s.1(1)(b), it is irrelevant whether Clare and Daniel are children or adults – the court's consent to the variation is required because their interest in the trust fund is contingent upon the exercise of the trustees' discretion during Barbara's lifetime. In other words they are not guaranteed to be beneficiaries under the trust – they will only benefit from the trust *if* the trustees exercise their discretion in their favour, and it is because of this uncertainty that the court must approve the variation – the spouse and children cannot approve a variation to something to which they are not certain of being entitled. In the case of *Re Poole's Settlements' Trusts* [1959] 2 All ER 340 for example, it was the fact that the settlor and the beneficiary's marriage was dissolved that caused the trustees' direction to become operative.

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[10] Ibid., p.396.

Sections 53 and s57

Another way in which the courts' inherent jurisdiction has been relegated to a principle that is rarely used is seen in the form of the Trustee Act 1925. Again the court's role is to approve the trustees' proposals rather than to vary the terms of the trust. Section 57 confers a general power upon the court to sanction a variation of the trust to allow for the sale, mortgage, lease or investment of the trust property where that would be expedient, but where it is not permitted by the trust instrument.

EXTRACT

Trustee Act 1925, s.57

57 Power of court to authorise dealings with trust property

(1) Where in the management or administration of any property vested in trustees, any sale, lease, mortgage, surrender, release, or other disposition, or any purchase, investment, acquisition, expenditure, or other transaction, is in the opinion of the court expedient, but the same cannot be effected by reason of the absence of any power for that purpose vested in the trustees by the trust instrument, if any, or by law, the court may by order confer upon the trustees, either generally or in any particular instance, the necessary power for the purpose, on such terms, and subject to such provisions and conditions, if any, as the court may think fit and may direct in what manner any money authorised to be expended, and the costs of any transaction, are to be paid or borne as between capital and income.

(2) The court may, from time to time, rescind or vary any order made under this section, or may make any new or further order.

(3) An application to the court under this section may be made by the trustees, or by any of them, or by any person beneficially interested under the trust.

(4) This section does not apply to trustees of a settlement for the purposes of the Settled Land Act 1925.

Section 53 of the same Act fulfils a broadly similar purpose in that it permits the court to sanction a variation of the trust in favour of a minor. Accordingly, where it is necessary to use the income or the capital from the trust for the purposes of the education or maintenance of a person who is under the age of 18 s.53 will permit the trust to be varied in order to fulfil that objective.

EXTRACT

Trustee Act 1925, s.53

Vesting orders in relation to infant's beneficial interest

Where an infant is beneficially entitled to any property the court may, with a view to the application of the capital or income thereof for the maintenance, education, or benefit of the infant, make an order –

(a) appointing a person to convey such property; or

(b) in the case of stock, or a thing in action, vesting in any person the right to transfer or call for a transfer of such stock, or to receive the dividends or income thereof, or to sue for and recover such thing in action, upon such terms as the court may think fit.

Variation on grounds of public policy

The final ground upon which a trust will be varied is if the settlor's directions are illegal. The leading authority in this respect is the case of *Re Beard* [1908] 1 Ch 383, where the trust was subject to a condition that prevented the beneficiaries from inheriting if they entered the army or the navy. It was held that this condition was contrary to public policy. Swinfen-Eady J concluded that this was contrary to public good and the welfare of the State. Accordingly, the condition was omitted, and the beneficiaries became absolutely entitled to the trust fund. By the same principle, the court will not vary or consent to a variation of a trust if to do so would be illegal or contrary to public policy.[11]

The advantage of the scope to vary the terms of a trust is that it allows the trustees to take into account factors that the settlor had not considered, or changes in circumstances. As has been demonstrated, the objective of saving tax is an important consideration, especially in light of the trustees' duty to maximise the gain for the trust. However, other practical considerations, such as the requirements of the beneficiaries and the day-to-day administration of the trust may also be important considerations. The law therefore operates on two premises – firstly, the issue of necessity being something that justifies the variation, and secondly, the desires of the trustees and the beneficiaries, and the variation of a trust is justified broadly on one of these two grounds.

Chapter summary

This chapter may be useful for assignments and assessments on:

- The trustee's powers and duties
- The grounds upon which a trust may be varied.

Further reading

Goldsworth, J.G. (1996) 'Conditions for variation of a trust: distinctions between a variation and the application of *Saunders v Vautier* principle' 3(1) *Trusts and Trustees* 8.

Hughes, R. (2012) 'Intestacy: Variation of trusts' 2(1) *Elder Law Journal* 16.

Matthews, P. (2006) 'The comparative importance of the rule in *Saunders v Vautier*' 122 *Law Quarterly Review* 266.

McCall, C. (1996) 'Variation of trusts: some observations' *Private Client Business* 389.

Mullan, R. (2007) 'Variations of trusts' 11(2) *Personal Tax Planning Review* 15.

Summers, J. and Brice, R. (2007) 'What constitutes benefit?' 87 *Trusts and Estates Law and Tax Journal* 15.

[11] *In Re Michelham's Will Trusts* [1964] Ch 550.

24

The termination of trusts

Chapter outline

This chapter will cover the different mechanisms by which a trust may be terminated, namely:

- Transfer of the trust property to the beneficiary
- Transfer at the beneficiary's behest.

Introduction

Although the trust is an extremely important and useful tool, it is, necessarily, more restrictive than absolute ownership. Under a trust, the trustee is able to deal with the trust property, but can derive no benefit from it, and the beneficiary may benefit from the trust property but cannot sell it, give it away or destroy it in the manner in which he or she chooses. Therefore, ultimately, the preferable situation is for a person to own property for his or her own benefit. Accordingly, a trust will eventually come to an end, and this chapter covers the different mechanisms by which this will occur.

Termination by transfer of the trust property to the entitled beneficiary

A trust will come to an end when the trust property is transferred to the beneficiary, i.e. when the trust has been fulfilled and the beneficiary becomes the new legal owner of the property. This is most readily demonstrated in situations such as a will. On the testator's death, the executor and trustee of the will become the legal owner of the deceased's assets. The executor and trustee will then distribute those assets to the eligible beneficiaries. Once this has occurred, the trust has come to an end and the trustee has no further obligation.

Termination at the beneficiary's behest

If all the beneficiaries under a trust are over the age of 18, and have the necessary mental capacity, they may terminate a trust. This is irrespective of any specification to the contrary contained in the trust instrument. Therefore, for example, if the trust instrument specifies that the beneficiaries are not entitled to the trust property until they reach the age of 21, once the beneficiaries have reached the age of 18, they can terminate the trust. This is known as the rule in *Saunders v Vautier* (1841) Cr & Ph 240.

EXTRACT

Saunders v Vautier (1841) Cr & Ph 240

Case facts

The testator left his entire estate to his great-nephew, specifying that the great-nephew would become entitled to the trust property when he reached the age of 25.

Lord Cottenham LC

It is argued that the testator's great-nephew, Daniel Wright Vautier, does not take a vested interest in the East India stock before his age of twenty-five, because there is no gift but in the direction to transfer the stock to him at that age. But is that so? There is an immediate gift of the East India stock; it is to be separated from the estate and vested in trustees; and the question is whether the great-nephew is not the *cestui qua* trust of that stock. It is immaterial that these trustees are also executors; they hold the East India stock as trustees, and that trust is to accumulate the income till the great-nephew attains twenty-five, and then to transfer and pay the stock and accumulated interest to him, his executors, administrators or assigns. There is no gift over; and the East India stock either belongs to the great-nephew or will fall into the

residue in the event of his dying under twenty-five. I am clearly of opinion that he is entitled to it. If the gift were within the rule, there would be circumstances to take it out of its operation. There is not only the gift of the intermediate interest, indicative, as Sir John Leach observes in *Vawdry v Geddes* [(1830) 39 ER 78] of an intention to make an immediate gift because, for the purpose of the interest, there must be an immediate separation of the legacy from the bulk of the estate; but a positive direction to separate the legacy from the estate, and to hold it on trust for the legatee when he shall attain twenty-five . . . Sir William Grant, in *Hanson v Graham* [(1801) 31 ER 1030] justifies it on grounds, most of which apply to this case, particularly that the fund was given to trustees till the legatee should attain a certain age and that it should then be transferred to him; from which and other circumstances he thought it was to be inferred, that the fund was intended wholly for the benefit of the legatee, although the testator intended that the enjoyment of it should be postponed till his age of twenty-four. Such, I think, was clearly the intention of the gift in this case. It was observed that the transfer is to be made to the great-nephew, his executors, administrators or assigns. It is true that the addition of those words does not prevent the lapse of a legacy by the death of the legatee in the lifetime of the testator, but they are not to be overlooked when the question is whether the legacy became vested before the age specified; because, if it were necessary that the legatee should live till that age to be entitled to the legacy, then there would be no question about his representatives at that time.

In order for a trust to be terminated, all the beneficiaries must consent. Therefore if one of the beneficiaries does not or cannot consent, then the trust cannot be terminated. Nevertheless, one or more beneficiaries may apply to the trustees in order to effect the partial termination of the trust in the sense that they may apply for the portion of the trust fund to which they are entitled. Where the trust consists of personalty (i.e. chattels or money) this will usually be granted, as the beneficiary is able to receive his or her entitlement without this having a detrimental effect on the other beneficiaries – as shown in the case of *Re Sandeman's Will Trusts* [1937] 1 All ER 368.

EXTRACT

Re Sandeman's Will Trusts [1937] 1 All ER 368

Case facts

The testator left half his estate to the claimants, and the other half in trust for his daughter for her lifetime, and to her children after their mother's death. The claimants requested for the trustees to divide the estate and transfer their half to them. The claimants argued that the interests of the trust as a whole were best served if the trust property were not divided.

Clauson J

The plaintiffs, as I have said, are absolutely entitled to half the estate . . . there is no practical difficulty, as the matter now stands, in dividing up the estate. There is no difficulty in dividing the preferred ordinary and the preferred shares into two halves, leaving one half in the hands of the trustees upon trust for Mrs Hordern and her family, the other half of the shares going to the plaintiffs, who are absolutely entitled to it. In those circumstances, it is settled law that, prima facie, the plaintiffs are entitled to have those shares transferred to them. Prima facie, that is so. But the court will not order that transfer to be made if there is some good ground to the contrary.

The court has, I think, been rather careful never to define in precise terms exactly what would be good ground to the contrary. All I have to do in this case is to ascertain whether, on the facts now before me, there is some good ground for ignoring the plaintiffs' prima facie right to have half of the shares transferred to them.

In the will, there is a provision that the trustees are not to sell the shares in this particular company unless, in their discretion, they think it desirable so to do; and they are to be at liberty to retain the shares as an investment. It is suggested-at least, I think it is suggested-that I can spell out of that power in the will an express direction to the trustees, or at all events a power in them, to refuse to transfer part of the trust property to a beneficiary who is absolutely entitled to that part of the trust property, provided that the part of the trust property in question is the shares in this particular company. That does not seem to me to be the true construction of the will. The clause to which I have been referred seems to me to deal with the question of the sale of the shares. Although it has been suggested by counsel that the transfer of shares to a beneficiary in some sense is equivalent to a sale, because it parts those shares from the estate, I do not take the view that it need be a sale at all. It is a recognition, on the part of the trustees, of the title of a man to something which belongs to him. In my view, on the construction of this will, the clauses contained in it, to which my attention has been drawn, have no bearing upon the problem which I have to consider. However, that is a question of construction; and it may be that my view is not quite right as regards that. So I will confine myself now to considering whether there is anything, either in the will or in the circumstances, which justifies me in refusing to allow effect to be given to what the Court of Appeal, in *Re Marshall* [[1914] 1 Ch 192], has determined in these circumstances to be the prima facie right of the plaintiffs, namely, to have the shares which belong to them transferred to them.

It is suggested that I am entitled to ignore that right for this reason. It is said that, if these shares are left in the hands of the trustees, the effect of that will be that the trustees can have control of the company, as against the holders of the remaining shares, in connection with any resolution which they may think desirable to have passed at a general meeting. That is perfectly true, but it is to be remembered that the trustees can do that only having regard to the interests of their beneficiaries. If you have two sets of beneficiaries equally concerned in the trust, and those two sets of beneficiaries take differing views as to the course which the trustees ought to take, the court will certainly see that those trustees, before exercising their power of voting, pay due regard to the wishes of those two sets of beneficiaries. It is foolish to say that the trustees, having shares in their name, have anything in the nature of an independent right to deal with voting power of the shares. However that may be, there is no fact, at the present moment, which seems to show that the interests of anybody concerned in the trust will be in the slightest degree prejudiced by the proper division being made-in other words, by the shares to which the plaintiffs are entitled being handed over to them.

I can conceive that there might be circumstances – they would have to be very special – which would justify the court in refusing to give effect to the plaintiffs' rights; but I cannot find, on the evidence before me, anything to suggest that such circumstances exist in this case. I have no reason to suppose that either the trustees, on the one hand, or the plaintiffs, when they become transferees of their shares, on the other hand, will exercise their voting power otherwise than perfectly bone fide; and I cannot see that any harm will be done to anybody by giving effect to the prima facie right of the plaintiffs to have their shares, and the voting power on their shares, in their own control.

If that is the right view on the facts, whether my view of the construction of the will is right or not, it is quite plain that the plaintiffs' rights must be given effect to; and they must have their half of the shares in question transferred to them. . . .

Therefore if Bob is entitled to a 25 per cent share of a £100,000 trust fund, he may apply to the trustees for his share (£25,000) even though the other beneficiaries require that the trust be continued. However, where the trust property consists of land,[1] or where giving the beneficiary his or her entitlement would affect the other beneficiaries to their detriment, the beneficiary cannot insist on the transfer of the trust property to him or her – confirmed in the case of *Lloyds Bank plc v Duker* [1987] 3 All ER 193. Therefore, in Bob's situation, if the trust fund is invested in a long-term investment where there would be penalties if the investment was terminated before the agreed date, Bob could not insist on receiving his share, as doing so would prejudice the entitlements of the other beneficiaries. The law on this issue is summarised by Walton J in the case of *Stephenson (Inspector of Taxes) v Barclays Bank Trust Co Ltd* [1975] 1 All ER 625, who explains:

> Now it is trite law that the persons who between them hold the entirety of the beneficial interests in any particular trust fund are as a body entitled to direct the trustees how that trust fund is to be dealt with, and this is obviously the legal territory from which that definition derives. However . . . I think it may be desirable to state what I conceive to be certain elementary principles. (1) In a case where the persons who between them hold the entirety of the beneficial interests in any particular trust fund are all sui juris and acting together ('the beneficial interest holders'), they are entitled to direct the trustees how the trust fund may be dealt with. (2) This does not mean, however, that they can at one and the same time override the preexisting trusts and keep them in existence . . . (3) Nor, I think, are the beneficial interest holders entitled to direct the trustees as to the particular investment they should make of the trust fund. I think this follows for the same reasons as the above . . . So much for the rights of the beneficial interest holders collectively. When the situation is that a single person who is sui juris has an absolutely vested beneficial interest in a share of the trust fund, his rights are not, I think, quite as extensive as those of the beneficial interest holders as a body. In general, he is entitled to have transferred to him (subject, of course, always to the same rights of the trustees as I have already mentioned above) an aliquot share of each and every asset of the trust fund which presents no difficulty so far as division is concerned. This will apply to such items as cash, money at the bank or an unsecured loan, stock exchange securities and the like. However, as regards land, certainly, in all cases, as regards shares in a private company in very special circumstance . . . and possibly . . . mortgage debts . . . the situation is not so simple, and even a person with a vested interest in possession in an aliquot share of the trust fund may have to wait until the land is sold, and so forth, before being able to call on the trustees as of right to account to him for his share of the assets.

In *Stephenson*, the testator wrote a will. The terms of the will required the trustees to invest the trust fund in such a way as to generate enough income to give his wife and daughters an annuity each. Any surplus generated by the investment, as well as the capital fund, was to be divided between the testator's grandchildren provided that they attained the age of 21. By 1969, all the beneficiaries had become entitled to the trust fund, and the trustees therefore arranged to calculate how much of the fund was needed to pay the annuities to the testator's daughters (his wife having died) and then arranged to pay the remainder to the testator's two grandsons. Essentially, this meant that the annuities were paid by the grandsons, rather than by the trust, and brought to an end the daughters' claim to the testator's estate.

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[1] *Re Marshall, Marshall v Marshall* [1914] 1 Ch 192 at 199.

Nevertheless, although the aim was to transfer the remainder to the testator's grandsons, thus bringing the trust to an end entirely, this did not occur immediately, and therefore the trustees continued to hold the trust fund for the benefit of the two adult grandsons. However the trustees were nevertheless liable to pay capital gains tax on the fund on the basis that even though the trust fund had not been distributed, the grandsons were absolutely entitled to it.

Although the principle is generally exercised in relation to private trusts, it is nevertheless possible for a charity to direct that a trust be terminated. Accordingly, in *Wharton v Masterman* [1895] AC 186, the testator left the residue of his estate to various people entitled to an annuity, and after all of them had died, the fund was to be divided between four specific charities which could require that the funds to which they were entitled were transferred to them. One exception to this rule is where the trust is for the benefit of charity generally. Although this is a valid declaration of the objects of the trust (being a partial exception to the three certainties rule), a charity could not direct that the fund is transferred to it, as they have no entitlement to the trust fund until the trustees have identified how the settlor's charitable intention is to be fulfilled – a matter that is confirmed in the case of *Re Jefferies* [1936] 2 All ER 626. Nevertheless, this does not preclude the beneficiaries under a discretionary trust from requiring that the trust property is transferred to them, as the case of *In Re Smith* [1928] Ch 915. The testator in this case gave the trustees a discretion to use part of the residuary estate to pay for the maintenance and support of a lady named Mrs Aspinall or her children. Mrs Aspinall and her two adult children mortgaged their equitable interest to the defendants. The trustee therefore required the court's advice regarding whether he was obliged to pay the entire fund to the mortgage lender, or whether he was entitled to exercise his discretion to use the fund for the maintenance or support of Mrs Aspinall. Romer J concluded:

> The question I have to determine is whether the Legal and General Assurance Company are now entitled to call upon the trustees to pay the whole of the income to them. It will be observed from what I have said that the whole of this share is now held by the trustees upon trusts under which they are bound to apply the whole income and eventually pay over or apply the whole capital to Mrs. Aspinall and the three children or some or one of them . . . Mrs. Aspinall, the two surviving children and the representatives of the deceased child are between them entitled to the whole fund. In those circumstances it appears to me, notwithstanding the discretion which is reposed in the trustees, under which discretion they could select one or more of the people I have mentioned as recipients of the income, and might apply part of the capital for the benefit of Mrs. Aspinall and so take it away from the children, that the four of them, if they were all living, could come to the Court and say to the trustees: 'Hand over the fund to us' . . . What is the principle? As I understand it, it is this. Where there is a trust under which trustees have a discretion as to applying the whole or part of a fund to or for the benefit of a particular person, that particular person cannot come to the trustees, and demand the fund; for the whole fund has not been given to him but only so much as the trustees think fit to let him have. But when the trustees have no discretion as to the amount of the fund to be applied, the fact that the trustees have a discretion as to the method in which the whole of the fund shall be applied for the benefit of the particular person does not prevent that particular person from coming and saying: 'Hand over the fund to me' . . . Now this third case arises. What is to happen where the trustees have a discretion whether they will apply the whole or only a portion of the fund for the benefit of one person, but are obliged to apply the rest of the fund, so far as not applied for the benefit of the first named person, to or for the benefit of

> a second named person? There, two people together are the sole objects of the discretionary trust and, between them, are entitled to have the whole fund applied to them or for their benefit. It has been laid down by the Court of Appeal in the case to which I have referred that, in such a case as that you treat all the people put together just as though they formed one person, for whose benefit the trustees were directed to apply the whole of a particular fund.

While this rule would apply in relation to a discretionary trust where there is a small class of beneficiaries who, between them, are somehow entitled to the fund in its entirety – as is seen in the case of *In Re Smith*, it may be more difficult to conceive how it may be applied in relation to a wider discretionary trust where there is no certainty regarding which person would be given the fund. For example, if a trust fund confers a discretion on the part of the trustees at a university to award a prize to the law student who obtains the highest examination mark in Equity and the Law of Trusts, but with a discretion to withhold the prize if no student obtains a first class mark, it may be more difficult to argue that the class of beneficiaries could apply to the trustees for distribution of the fund.

Unlike the situation in *In Re Smith* [1928] Ch 915, the beneficiaries are not ascertained until such time as the trustees exercise their discretion and select a beneficiary or beneficiaries. In *In Re Smith* on the other hand, the discretion related more specifically to when the beneficiaries would become entitled rather than who the beneficiaries were. It remains to be seen therefore how the rule would apply to discretionary trusts where the trustees are given the discretion to select beneficiaries from a wider class. The author's suspicion is that the law in this type of situation is likely to follow the approach taken in *Re Jefferies* – a view that is shared by Parkinson:[2]

> A more substantial argument for reconsideration arises however, when one considers the nature of discretionary trusts. It is clear that beneficiaries under a discretionary trust do not gain proprietary interests. That may be so in terms of individual proprietary rights, but can it be said that the beneficial estate vests in the named beneficiaries collectively?
>
> One way of answering this is to inquire whether the rule in *Saunders v. Vautier* [[1835-42] All ER Rep 58] will apply to allow the beneficiaries of the discretionary trust if all adult and *sui juris*, to call for the legal estate to be vested in them. This has been applied in the context of discretionary trusts, in the circumstances where the class of beneficiaries was closed, and there was no power to accumulate income. However, there will be many other discretionary trusts where such a rule could not practically have any operation. A prominent example is the trust which was involved in the Baden litigation. *In McPhail v. Doulton* [[1971] AC 424], consideration was given to the validity of a discretionary trust which listed the beneficiaries as officers, employees and ex-officers or employees of a certain company, together with their relatives and dependants. In the subsequent case, *Re Baden's Deed Trusts (No. 2)* [[1973] Ch 9] the Court of Appeal, by majority, held that relatives meant 'descendants from a common ancestor'. Such a definition would include an enormous number of people who are distantly related to employees or ex-employees of the company. It would be impossible to say where the beneficial interest lay in the *Baden* trust. Of course, one might assert as a matter of dogma that the beneficial estate vests collectively in the group of potential beneficiaries even if they could never be ascertained, but it is difficult to see what practical reality this could have.

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[2] Parkinson, P. (2002) 'Reconceptualising the Express Trust' 61 *Cambridge Law Journal* 657 at p.660.

The rule in *Saunders v. Vautier* can only really have application to a discretionary trust if there is a fixed class, subject to a discretion to choose between members of that class, and the class is closed, or to a discretionary trust which, although initially open, becomes closed by subsequent events. In such a case the beneficiaries should be regarded as collectively holding the equitable estate and therefore able to wind up the trust if they are all adult and *sui juris*. If however, the class is so wide that no list of beneficiaries can sensibly be drawn up, then the rule in *Saunders* v. *Vautier* would not apply. Consequently, the legal estate would vest in the trustees without a symmetrical equitable right vested elsewhere, although the trust would need to be set up in such a way as to avoid perpetuity problems.

Once the trustees have transferred the trust property to the beneficiaries, the trust comes to an end. The trustees have discharged their obligation, and the beneficiary becomes the absolute owner of the property. Of course, they may now declare themselves to be trustees, or transfer the trust property to new trustees, or write a will, or die intestate, and once again, the law of trusts comes into operation.

Trusts being terminated by operation of law

The third way in which a trust may be terminated is through the operation of law. In the case of *Midland Bank v Wyatt* [1997] 1 BCLC 242 for example, a trust was terminated because the court felt that it was a sham that had been created in order to put money beyond the reach of the settlor's creditors. Accordingly, the court took it upon itself to terminate the trust.

EXTRACT

Midland Bank v Wyatt [1997] 1 BCLC 242

Case facts

The claimants made a charging order over the defendant's matrimonial home. The defendant argued that the bank could not do this because he held the property on trust for his wife and daughters.

David Young QC

(1) It is quite clear that at the time of execution of the declaration of trust Mrs Wyatt was not aware of its import or effect. She said in evidence at that time (1987) she would have signed whatever was put in front of her without reading it. This is borne out by the fact that when she came to execute the later declaration of trust on the basis that she and Mr Wyatt were tenants in common with equal shares in Honer House, she knew nothing about the earlier declaration of trust. Also, when first questioned about it she could recall nothing about it, but could remember a draft will in which she and her two daughters were to be provided for in equal shares.

(2) It is equally clear that, once executed, the declaration of trust was placed in the safe in Honer House and not acted upon in any way whatsoever.

  (a) Mr Wyatt continued as though he remained a joint equity owner of Honer House. In his dealings with the bank with Mr Schools, Mr Hunt and Mr Hopper they all believed that he had a joint beneficial interest in the matrimonial home with his wife.

As stated above, his wife, at all relevant times until the deed was drawn to her attention towards the end of August 1991, believed he was a joint beneficial owner of the property.

His daughter Kirsty Wyatt was not told about it until the latter half of 1991. His partner in Fabrics 2000 Ltd, Mr Howick, believed he was the owner of the property, a view that was perpetuated by Mr Wyatt right up until the end (see Mr Wyatt's letter of 17 June 1991).

Neither Mr Barry Minton nor Mrs Bevis, both partners of Rapers, who acted for Mr Wyatt in his separation arrangements and in the refinancing arrangements with Abbey National, were made aware of the earlier declaration of trust divesting Mr Wyatt of his interest in Honer House. Indeed dealings with the Abbey National proceeded on the basis that the Wyatts were the beneficial owners of Honer House.

(b) Mr Wyatt stated in his evidence that he was aware that his powers as trustee under the declaration of trust were to be exercised for the benefit of the beneficiaries, namely Mrs Wyatt and his two daughters.

In spite of this understanding, within six months or so of when he is alleged to have signed the deed he was seeking to borrow £50,000 as a personal loan for his new business, the security for which was to be Honer House.

(c) Mr Wyatt also agreed in evidence that, as regards the then existing home mortgage loan, he continued to pay interest thereon after the execution of the declaration of trust deed as he had before and to claim tax relief thereon.

(3) In short, subsequent to the execution of the trust deed, nothing had changed in Mr Wyatt's behaviour or attitude with regard to his dealings involving Honer House.

I do not believe Mr Wyatt had any intention, when he executed the trust deed, of endowing his children with his interest in Honer House, which at the time was his only real asset. I consider the trust deed was executed by him, not to be acted upon but to be put in the safe for a rainy day. As Mr Wyatt states in his affidavit, it was to be used as a safeguard to protect his family from long-term commercial risk, should he set up his own company. As such, I consider the declaration of trust was not what it purported to be but a pretence, or as it is sometimes referred to, a 'sham'. The fact that Mr Wyatt executed the deed with the benefit of legal advice from Mr Ellis does not, in my view, affect the status of the transaction. It follows that even if the deed was entered into without any dishonest or fraudulent motive, but was entered into on the basis of mistaken advice, in my judgment such a transaction will still be void and therefore an unenforceable transaction if it was not intended to be acted upon but was entered into for some different or ulterior motive. Accordingly I find that the declaration of trust sought to be relied upon by Mr Wyatt is void and unenforceable. As I have already found, the declaration of trust was entered into not with the intention of endowing Kirsty and Olivia Wyatt with Mr Wyatt's interest in Honer House but as a safeguard to protect his family from long-term commercial risk should Mr Wyatt set up his own company, which by June 1987 he was contemplating . . .

As to exactly when the trust deed was entered into, whilst I have no doubt that it was executed by the parties prior to Mr Wyatt's separation from his wife at the end of 1989, there is no clear evidence whether it was executed on the date it bears or some later date. Mr Wyatt was not asked as to when the date was entered on the deed. Mr Pallett had no reason to believe it was not the date he witnessed the signatures, although very fairly he could not confirm that that was the case. Certainly I am not satisfied that it was executed at a date later than the date the deed bears and accordingly on the evidence before me I have concluded that the deed bears the date on which it was executed . . .

As I have already found that Mr Wyatt had no intention of disposing of his interest to benefit his children, it must follow that the real purpose of entering into the declaration of trust was to

screen or protect them against the unknown risks of the new adventure . . . Accordingly, I am also satisfied that the declaration of trust was entered into by Mr Wyatt for the purpose of putting his interest in Honer House out of the reach of any future creditors who might make a claim with respect thereto and, therefore, cannot be relied upon by Mr Wyatt in view of s 423 of the 1986 Act.

It was sought by both Mr Wyatt and Mr Farber, for the second and third defendants, to put the blame on the plaintiff bank in not properly securing the loan in the first place and in not properly considering Mrs Bevis' amendments to Rapers' undertaking to pay over the moneys raised by Mr and Mrs Wyatt from Abbey National. I do not consider such errors by the bank affect the question before me as to the true nature of the deed of declaration.

Outcome

Accordingly, the trust was set aside.

Therefore, trusts can be terminated either by the trustees, once they have fulfilled their obligations to the beneficiaries, or by the beneficiaries. These are the two primary ways by which a trust may be terminated. Nevertheless, there is also the possibility that the settlor can be overridden where the interests of legality and public policy require it.

Chapter summary

This chapter may be useful for assessments and assignments relating to:

- Termination of trusts
- The role of the beneficiaries under the trust
- The nature of the trust.

Further reading

Clutton, O. (1990) 'When trusts can be set aside: Insolvency Act 1986' 4(9) *Trusts and Estates* 72.

Part 5

Tracing

25

Tracing

Chapter outline

This chapter will consider:

- The concepts of following and tracing
- Tracing at common law
- Tracing in equity
- The fusion of common law and equitable tracing.

Introduction

The final aspect of the law of trusts we are going to cover is the law relating to tracing. Although it is commonly dealt with as a form of equitable remedy, strictly speaking, tracing is not actually a remedy. Tracing is a process that enables a claimant to identify who to sue and what the subject of the claim is. Accordingly, tracing is commonly used where a trustee has misappropriated trust property. However, tracing can be used in other situations where there has been a misappropriation of assets, for example theft, and sales by an insolvent company. Nevertheless, its application to situations where trusts have been breached, has expanded the scope of tracing, and has taken tracing beyond the domain of the common law and into the realm of equity. Accordingly, tracing may be seen to be yet another example of equity's capacity to innovate.

Tracing encompasses two elements. These are known as following and tracing.

EXAMPLE

Imagine that Alf owns a ring. Bob steals it and gives it to Claire. Let us say that Bob has sold the ring to Claire. Alf can claim the ring back off Claire under a process called following, because even though she has bought it in good faith from Bob, Bob had no right to sell it to her, and Alf's title defeats Claire's. Essentially, what occurs here is that Alf follows the transfer of the ring from person to person, and then sues the person into whose hands it has fallen.

Alternatively, Alf may claim against anything for which the ring has been exchanged. For example, let us say it has been sold. Rather than following the ring further, it may be possible to make a claim against Bob for the money that Claire has paid for the ring. In other words, what Alf does here is to identify the ways in which the ring has been substituted for other assets, and then claims for those substitutions. This is called tracing.

Tracing is useful where the asset has been acquired by a bona fide purchaser (such as Claire in the example above), whom it is not desirable to sue because they have done nothing wrong. It is also useful where the original asset has been destroyed or has diminished in value, because the claimant is able to claim for the value of the asset when it was stolen rather than its current (diminished) value. The claimant is able to choose whether to claim under the process of following, or whether to claim under the process of tracing. Of course, he or she cannot claim against both potential defendants, as this would mean being compensated twice in relation to the same loss. However, as Lord Millett explains in the case of *Foskett v McKeown* [2001] 1 AC 102 at p.120:

> In practice his choice is often dictated by the circumstances. In the present case the plaintiffs do not seek to follow the money any further once it reached the bank or insurance company, since its identity was lost in the hands of the recipient (which in any case obtained an unassailable title as a bona fide purchaser for value without notice of the plaintiffs' beneficial interest). Instead the plaintiffs have chosen at each stage to trace the money into its proceeds, viz, the debt presently due from the bank to the account holder or the debt prospectively and contingently due from the insurance company to the policy holders.

Tracing at common law

Tracing originated as a common law process. However, common law tracing is only available where the legal owner of an asset has been deprived of it and is only available in three situations. Firstly, tracing is used where the asset is the subject of clean substitutions, in other words where the asset is not mixed with any other assets.[1] Therefore there would be no difficulty with tracing the exchange of a painting for a diamond ring for example, or, more commonly the exchange of an item for money. In such cases, the claimant may claim the substituted product, as confirmed in *FC Jones and Sons v Jones* [1997] Ch 159 where Beldam LJ states (at p.171):

> There is now ample authority for the proposition that a person who can trace his property into its product, provided the product is identifiable as the product of his property, may lay legal claim to that property.

EXTRACT

FC Jones and Sons v Jones [1997] Ch 159

Case facts

FC Jones and Sons was a firm which committed an act of bankruptcy. Soon afterwards however, but before the company was adjudicated bankrupt, the wife of one of the partners paid cheques drawn from the bank account of her husband and one of the other partners in the firm into a commodity brokerage account. This investment made a gain and the trustee in bankruptcy then sought to claim this money as representing part of FC Jones' debts.

Millett LJ

If the cheques had passed the legal title to the defendant but not the beneficial ownership, she would have received the money as constructive trustee and be liable to a proprietary restitutionary claim in equity (sometimes, though inaccurately, described as a tracing claim). The defendant would have been obliged, not merely to account for the £11,700 which she had received, but to hand over the £11,700 in specie to the trustee. Her position would have been no different from that of an express trustee who held the money in trust for the trustee; or from that of Mr. Reid in *Attorney-General for Hong Kong v. Reid* [1994] 1 A.C. 324, whose liability to account for the profits which he made from investing a bribe was based on his obligation to pay it over to his principal as soon as he received it. The existence of any such obligation has been disputed by commentators, but no one disputes that, if the obligation exists, it carries with it the duty to pay over or account for any profits made by the use of the money.

But the defendant was not a constructive trustee. She had no legal title to the money. She had no title to it at all. She was merely in possession; that is to say, in a position to deal with it even though it did not belong to her . . . If she made a profit, how could she have any claim to the profit made by the use of someone else's money? In my judgment she could not. If she were to retain the profit made by the use of the trustee's money, then, in the language of the modern law of restitution, she would be unjustly enriched at the expense of the trustee. If she were a constructive trustee of the money, a court of equity, as a court of conscience, would say that it was unconscionable for her to lay claim to the profit made by the use of her beneficiary's

[1] *Lipkin Gorman v Karpnale* [1991] 2 AC 548.

money. It would, however, be a mistake to suppose that the common law courts disregarded considerations of conscience. Lord Mansfield C.J., who did much to develop the early law of restitution at common law, founded it firmly on the basis of good conscience and unjust enrichment. It would, in my judgment, be absurd if a person with no title at all were in a stronger position to resist a proprietary claim by the true owner than one with a bare legal title. In the present case equity has no role to play. The trustee must bring his claim at common law. It follows that, if he has to trace his money, he must rely on common law tracing rules, and that he has no proprietary remedy. But it does not follow that he has no proprietary claim. His claim is exclusively proprietary. He claims the money because it belongs to him at law or represents profits made by the use of money which belonged to him at law.

Outcome

Accordingly, the Court of Appeal dismissed the appeal.

In *FC Jones v Jones*, the loan was simply traced into that which it had been substituted, and the trustee in bankruptcy was able to claim that which the loan now represented, i.e. the balance in a bank account.

Secondly, common law will allow tracing into a mixed bulk, provided that the mixed bulk is capable of being divided into proportionate shares, as in *Indian Oil Corporation v Greenstone Shipping* [1998] QB 345 which concerned oil in containers that had been mixed with other containers of oil. It was held that it was possible in such situations for tracing to occur by dividing the containers between the parties in a proportionate measure to what was rightfully theirs. Staughton J explains:

> The combined effect of those principles would justify and require that where it is totally unknown how much of the innocent party's goods went into the mixture, the whole should belong to him. But I do not see that they require or justify the same result where it is known how much was contributed by the innocent party, or even what the maximum quantity is that he can have contributed, being something less than the whole. That would not be the only justice that could be done: it would be injustice . . . Seeing that none of the authorities is binding on me, although many are certainly persuasive, I consider that I am free to apply the rule which justice requires. This is that where B wrongfully mixes the goods of A with goods of his own, which are substantially of the same nature and quality, and they cannot in practice be separated, the mixture is held in common and A is entitled to receive out of it a quantity equal to that of his goods which went into the mixture, any doubt as to that quantity being resolved in favour of A. He is also entitled to claim damages from B in respect of any loss he may have suffered, in respect of quality or otherwise, by reason of the admixture.
>
> Whether the same rule would apply when the goods of A and B are not substantially of the same nature and quality must be left to another case. It does not arise here. The claim based on a rule of law that the mixture became the property of the receivers fails.

However, where the property has been mixed in such a way that it is no longer divisible, such as where the property is used to manufacture an entirely new product, common law tracing will fail. This was shown in the case of *Borden Ltd v Scottish Timber Products* [1981] Ch 25 where resin belonging to the claimant was mixed with other materials to make chipboard. However, the claimant was not able to claim the chipboard as his property because the resin was no longer identifiable.

The third situation where common law tracing will succeed is where the claimant may claim the mixed product in its entirety. An example is seen in *Jones v De Marchant* (1916) 28 DLR 561. Here animal skins had been used to make a fur coat. Therefore the coat was

in effect the same asset as the animal skins, even though things (e.g. sewing thread) had been added to the skins to make the coat. Accordingly, tracing was permitted because the misappropriated item was, in substance, the same as the asset in its new format. However, whether tracing will be allowed will depend on the extent to which the claimant's property has been used in the formation of the new product, and therefore tracing is unlikely to be permitted when significant assets belonging to another have been incorporated into the mixture.

Under the common law it is impossible to trace money into a mixed fund, as was confirmed in the case of *Banque Belge pour L'Etranger v Hambrouck* [1921] 1 KB 321, such as the situation where the money that is being traced is put into a bank account alongside existing funds.

EXTRACT

Banque Belge pour L'Etranger v Hambrouck [1921] 1 KB 321

Case facts

The defendant, a bank clerk, perpetrated a fraud by paying cheques, purportedly from his employer, into his own account at the claimant bank. He then paid sums of money to his partner, a Miss Spanoghe, who paid the money into her own account. When the fraud was discovered, the claimants tried to recover their money from Miss Spanoghe's account, and succeeded. Miss Spanoghe appealed.

Scrutton LJ

It is clear, however, that the money actually obtained by Hambrouck was the Bank's money, even if they might debit their payments to the account of another, and the Bank therefore can sue for the money if it was obtained by fraud on them. Secondly, it was said that as Hambrouck paid the stolen money into a bank, he had only a creditor's right to be paid with any money, not the particular money he paid in; so that when he drew some money out of the bank and paid it to Mlle. Spanoghe, he did not make her the recipient of the money he had obtained from the Banque Belge, and therefore an action for money had and received would not lie. It was further said that Mlle. Spanoghe received the money as a gift without notice of any defect in title and that therefore no action would lie against her . . . But both good faith and valuable consideration were necessary, as Lord Mansfield says: 'in case of money stolen, the true owner cannot recover it after it has been paid away fairly and honestly upon a valuable and bona fide consideration'; but before money has passed in currency an action may be brought for the money itself. In the present case, it is clear that this money came to Mlle. Spanoghe either as savings out of housekeeping allowance, or as a gift to a mistress for past or future cohabitation. In the first case she would hold it as agent for Hambrouck; in the second for no consideration that the law recognized. If then the money that came to her was the money of the Banque Belge, she got no title to it, as Hambrouck against the Banque Belge had no title. The defence is that it was not the money of the Banque Belge, for payment into Hambrouck's bank, and his drawing out other money in satisfaction, had changed its identity. I am inclined to think that at common law this would be a good answer to a claim for money had and received, at any rate if the money was mixed in Hambrouck's bank with other money.

Outcome

What was significant in this case however was that the money was not Miss Spanoghe's in the first place. The Court of Appeal therefore ordered that Miss Spanoghe could be required to repay the money.

It is not possible to trace money that has been moved using electronic or telegraphic transfer. It is important that, in order for tracing to occur, the product traced must be identifiable, and this is not the case with intangible assets, as the case of *El Ajou v Dollar Land Holdings* [1993] 3 All ER 717 confirms. Accordingly, tracing at common law is of only very limited application to contemporary situations where the claimant is seeking to trace money that has been misappropriated and transferred through a series of bank accounts.

Tracing in equity

Because of the limitations of tracing at common law (i.e. the fact that it is not available to an equitable owner, and the inability to trace into a mixed fund), the courts developed the concept of tracing in equity. Equitable tracing will be available where a fiduciary duty is owed by the wrongdoer to the claimant – as Fox LJ indicates in *Agip (Africa) v Jackson* [1992] 4 All ER 451 at p.466 where he states:

> It is . . . a prerequisite to the operation of the remedy in equity that there must be a fiduciary relationship which calls the equitable jurisdiction in to being.

A fiduciary relationship will clearly be demonstrated where a beneficiary is attempting to trace trust property that has been misappropriated by the trustee, as Lord Browne-Wilkinson concludes in *Foskett v McKeown* [2001] 1 AC 102 at p.110:

> Where a trustee in breach of trust mixes money in his own bank account with trust moneys, the moneys in the account belong to the trustee personally and to the beneficiaries under the trust rateably according to the amounts respectively provided. On a proper analysis, there are 'no moneys in the account' in the sense of physical cash. Immediately before the improper mixture, the trustee had a chose in action being his right against the bank to demand a payment of the credit balance on his account. Immediately after the mixture, the trustee had the same chose in action (ie the right of action against the bank) but its value reflected in part the amount of the beneficiaries' moneys wrongly paid in. There is no doubt that in such a case of moneys mixed in a bank account the credit balance on the account belongs to the trustee and the beneficiaries rateably according to their respective contributions.

Tracing in equity would also therefore be permitted in other cases where a fiduciary relationship is owed, although in many of these situations, where the claimant is the legal owner of the goods that are the subject of the tracing claim, it may be preferable to trace at common law, simply because the claimant is the legal owner of the goods, and is founding a claim in law rather than equity. That said, as shall be demonstrated, there may be advantages to tracing in equity that are not present in common law tracing claims.

Firstly, the courts have stretched the concept of a fiduciary duty and argue (as in the case *of El Ajou v Dollar Land Holdings* [1993] 3 All ER 717) that where an asset has been misappropriated, the wrongdoer may be said to hold it on a resulting trust basis for the owner. Such cases would allow equitable tracing where there has been embezzlement from a fund,[2] as well as where a person makes unauthorised profits from the investment of property.[3] Money obtained as a result of a factual mistake as well as money obtained

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[2] *Agip (Africa) Ltd v Jackson* [1990] Ch 265.
[3] *A-G for Hong Kong v Reid* [1994] 1 AC 324.

as a result of fraud can all be traced in equity. This makes the wrongdoer a trustee, and therefore owing a fiduciary duty to the true owner. Accordingly, equitable tracing has been used both where the claimant is the legal owner of the asset, and where he is a beneficiary under a trust.

EXTRACT

El Ajou v Dollar Land Holdings [1994] 2 All ER 685

Case facts

An investment manager was bribed to invest the claimants' money in fraudulent share-selling schemes. The proceeds of these schemes were invested in a property development project in London, operated by the defendant. The defendant company's chairman was also an agent of the organisation that had perpetrated the fraud, although it would not be proved that this was known to the defendant. It was also proved that the chairman played no active part in the management of the defendant company. Nevertheless, it was held that el Ajou could trace the fund into the money received by the defendant.

At first instance, Millett J explained that the claimants could trace in equity, although their claim would fail because the defendant did not know of the fraudulent activity.

Millett J

In *Agip (Africa) Ltd v Jackson* [1992] 4 All ER 451 at 466, [1991] Ch 547 at 566 Fox LJ restated the principle, settled by *Re Diplock's Estate, Diplock v Wintle* [1948] 2 All ER 318, [1948] Ch 465, that it is a prerequisite of the right to trace in equity that there must be a fiduciary relationship which calls the equitable jurisdiction into being. This makes it necessary to consider separately the common law and equitable tracing rules. In the present case, it is manifestly impossible to follow the money at common law. The international transfers of money were made electronically; the plaintiff's money was mixed, not merely with the money of other victims or of the fraudsters themselves, but with the money of innocent third parties in the accounts of Valmet Geneva and Valmet Gibraltar, and passed on several occasions through the clearing systems of New York and London; while the back-to-back financing arrangements with Banque Scandinave and Scandinavian Bank would seem to present an insuperable obstacle to the common law, even if it had not lost the trail long before.

As counsel for DLH properly concedes, however, none of these features creates a problem for equity. Nor has the plaintiff any difficulty in satisfying the precondition for equity's intervention. Mr Murad was the plaintiff's fiduciary, and he was bribed to purchase the shares. He committed a gross breach of his fiduciary obligations to the plaintiff, and that is sufficient to enable the plaintiff to invoke the assistance of equity. Other victims, however, were less fortunate. They employed no fiduciary. They were simply swindled. No breach of any fiduciary obligation was involved. It would, of course, be an intolerable reproach to our system of jurisprudence if the plaintiff were the only victim who could trace and recover his money. Neither party before me suggested that this is the case; and I agree with them. But if the other victims of the fraud can trace their money in equity it must be because, having been induced to purchase the shares by false and fraudulent misrepresentations, they are entitled to rescind the transaction and revest the equitable title to the purchase money in themselves, at least to the extent necessary to support an equitable tracing claim: see *Daly v Sydney Stock Exchange Ltd* (1986) 160 CLR 371 at 387–390 per Brennan J. There is thus no distinction between their case and the plaintiff's. They can rescind the purchases for fraud, and he for the bribery of his agent; and each can then invoke the assistance of equity to follow property of which he is the equitable owner. But, if this

is correct, as I think it is, then the trust which is operating in these cases is not some new model remedial constructive trust, but an old-fashioned institutional resulting trust. This may be of relevance in relation to the degree of knowledge required on the part of a subsequent recipient to make him liable.

Subject to two points, counsel for DLH concedes that the plaintiff can successfully trace the money from Amsterdam to London. He submits (1) that the plaintiff has not established that the money which reached the Keristal No 2 account on 12 and 16 May 1986 represented the money which was last seen leaving Gibraltar for Panama on 30 March and 1 April 1986, and (2) that the equitable remedy depends on the continuing subsistence of the plaintiff's equitable title, and cannot be invoked where the money is transferred to recipients in civil law jurisdictions like Switzerland and Panama which do not recognise the trust concept or the notion of equitable ownership.

I reject both submissions.

(1) Tracing through Panama

It is, of course, beyond dispute that the money which was received in the Keristal No 2 account was the Canadians' money. It is, however, true that the plaintiff is unable by direct evidence to identify that money with the money which Mr D'Albis had sent to Panama only a few weeks before. If the question arose in proceedings between the plaintiff and the Canadians, then, in the absence of evidence to the contrary, the court would draw the necessary inference against the latter, for they would be in a position to dispel it. But DLH is not; it is as much in the dark as the plaintiff.

Nevertheless, in my judgment there is sufficient, though only just, to enable the inference to be drawn. One of the two sums received in the Keristal No 2 account was $1,541,432 received on 12 May 1986 from Bank of America. That corresponds closely with the sum of $1,600,000 transferred to Bank of America, Panama on 1 April 1986. In relation to the later transaction, Bank of America may, of course, merely have been acting as a correspondent bank in New York and not as the paying bank; and the closeness of the figures could be a coincidence. It is not much, but it is something; and there is nothing in the opposite scale. The source of the other money received in the Keristal No 2 account is not known, but from the way in which the Canadians appear to have dealt with their affairs, if one sum came from Panama, then the other probably did so, too.

The plaintiff points out that the deposit was paid out of funds held by the second tier Panamanian companies immediately before they were sent to Panama, and submits that it is a reasonable inference that the rest of the money came from the same source. If the Canadians had substantial funds elsewhere to invest in the project, the plaintiff asks, why did they not use them to provide the deposit? There is force in this submission. Against it, DLH points out that, by the time the money was sent to Panama, Roth had already struck the deal with Mr Stern, and the Canadians knew that another £1,030,000 would be needed in London within a few weeks. Why send it to Panama? Far simpler to leave it in Geneva, especially when the Canadians had already decided to use it to support a back-to-back guarantee, as the terms of Mr Ferdman's telex demonstrate. There is force in this observation, too. But, in my judgment, any attempt to weigh the Canadians' motives is too speculative to form the basis of any inference. They may have decided to remove the funds at least temporarily from Geneva in order to conceal from Mr D'Albis that they were transferring their allegiance to a different Swiss fiduciary agent; or they may have decided to launder the money through Panama before making any long-term investment in Europe. Their request to be given five days' notice before coming up with the money is neutral; it may have had more to do with the time needed to arrange the back-to-back guarantee than any additional time needed to bring back funds from Panama.

But the fact remains that there is no evidence that the Canadians had any substantial funds available to them which did not represent proceeds of the fraud. This is acknowledged by counsel for DLH. For the source of the money he points to the $1,4345m received by Zawi and the payments totalling $4,927,000 made by Herron and Wilmington which cannot be accounted for. But it has not been shown that any of these moneys were still at the disposal of the Canadians in May 1986. They had many expenses to meet out of moneys received by Herron and Wilmington (commissions to salesmen, for instance, not already accounted for); and Singer and Goldhar would presumably need to be looked after.

But, in my judgment, this is irrelevant. The money in the accounts of Herron and Wilmington represented proceeds of the fraud. It can be traced in equity from those accounts to the Keristal No 2 account as well as through Zawi or any other intermediate recipient as through the first and second tier Panamanian companies. The victims of a fraud can follow their money in equity through bank accounts where it has been mixed with other moneys because equity treats the money in such accounts as charged with the repayment of their money. If the money in an account subject to such a charge is afterwards paid out of the account and into a number of different accounts, the victims can claim a similar charge over each of the recipient accounts. They are not bound to choose between them. Whatever may be the position as between the victims inter se, as against the wrongdoer his victims are not required to appropriate debits to credits in order to identify the particular account into which their money has been paid. Equity's power to charge a mixed fund with the repayment of trust moneys (a power not shared by the common law) enables the claimants to follow the money, not because it is theirs, but because it is derived from a fund which is treated as if it were subject to a charge in their favour.

Counsel for DLH, however, submits that in the present case the plaintiff is confined by his pleading. In the statement of claim he has alleged that his money was paid to the first and second tier Panamanian companies whence it eventually found its way to the Keristal No 2 account. Accordingly, counsel submits, he cannot now claim to trace it by a different route. But the plaintiff's case has not changed. He still asserts that which he must establish, viz that the money in the Keristal No 2 account was derived from the moneys in the Herron and Wilmington accounts. It is still his case that it reached the Keristal No 2 account via the first and second tier Panamanian companies; but that is not essential to his claim. DLH could not defeat the claim by proving that, although the money in the Keristal No 2 account was derived from the Herron and Wilmington accounts, it had come by a different route. Still less can it defeat the claim by demonstrating that it may possibly have done so.

In my judgment, there is some evidence to support an inference that the money which reached the Keristal No 2 account represented part of the moneys which had been transmitted to Panama by the second tier Panamanian companies some six weeks previously, and the suggestion that it was derived from any other source is pure speculation.

(2) Tracing through civil jurisdictions

Counsel for DLH next submits that the plaintiff's claim, whether personal or proprietary, depends on the continuing subsistence of his equitable title to the money, and cannot be established where the money had passed through the hands of recipients in civil law jurisdictions which do not recognise the concept of equitable ownership. In my judgment, this argument is not open to DLH. Foreign law is a question of fact. It must be pleaded and proved by expert evidence. The court cannot take judicial notice of foreign law, though it be notorious: *Lazard Bros & Co v Midland Bank Ltd* [1933] AC 289 at 297, [1932] All ER Rep 571 at 576. In the absence of evidence, foreign law is presumed to be the same as English law. In the present case no question of foreign law has been pleaded, and no evidence of foreign law has been tendered.

But, even if the argument were open to DLH, I would reject it. In my judgment, it is misconceived. For technical reasons, the plaintiff's claim is brought in equity, where it is of a kind generally described as a case of 'knowing receipt'. This is the counterpart in equity of the common law action for money had and received. Both can be classified as receipt-based restitutionary claims. The law governing such claims is the law of the country where the defendant received the money: see Dicey and Morris *The Conflict of Laws* (11th edn, 1987) r 203(2)(c) and *Chase Manhattan Bank NA v Israel-British Bank (London) Ltd* [1979] 3 All ER 1025, [1981] Ch 105. Whatever money or property DLH received was received by it in England and, accordingly, the plaintiff's claim falls to be governed by English law, including the principles of equity. It is not necessary to consider whether the concept by which equity gives effect to the claim by permitting the plaintiff to trace his money and identify it as his in the hands of the recipient is procedural or substantive, since on either footing it too is governed by English law, either as the *lex fori* or as the law of the restitutionary obligation.

Although equitable rights may found proprietary as well as personal claims, it has long been settled that they are classified as personal rights for the purpose of private international law. The doctrine was stated by *Lord Selborne LC in Ewing v Orr Ewing* (1883) 9 App Cas 34 at 40 as follows:

> 'The Courts of Equity in England are, and always have been, Courts of conscience, operating *in personam* and not *in rem*; and in the exercise of this personal jurisdiction they have always been accustomed to compel the performance of contracts and trusts as to subjects which were not either locally or *ratione domicilii* within their jurisdiction. They have done so as to land, in Scotland, in Ireland, in the Colonies, in foreign countries . . .'

In *Cook Industries Inc v Galliher* [1978] 3 All ER 945, [1979] Ch 439 Templeman J entertained an action in which the plaintiff claimed a declaration that the defendants held a flat in Paris together with its contents in trust for the plaintiff, and made an order compelling the defendants to allow the plaintiff to inspect the flat. The fact that the subject matter of the alleged trust was situate in France, a civil law country, was no bar to the jurisdiction.

DLH is, therefore, answerable to the court's equitable jurisdiction as regards assets situate abroad, even in a civil law country. A fortiori, it is amenable to the court's equitable jurisdiction as regards assets which were formerly in a civil law country but which it has received in England in circumstances which are alleged to render it unconscionable for it to retain them.

DLH's argument is based on the premise that, for the plaintiff to succeed in tracing his money in equity through successive mixed accounts, he must have been in a position to obtain an equitable charge against each successive account. Even if the premise were correct, however, it would not matter where the accounts were maintained. It would be sufficient (and necessary) that the account holders were within the jurisdiction. But, in my judgment, it is not correct. It is not necessary that each successive recipient should have been within the jurisdiction; it is sufficient that the defendant is. This is because the plaintiff's ability to trace his money in equity is dependent on the power of equity to charge a mixed fund with the repayment of trust moneys, not upon any actual exercise of that power. The charge itself is entirely notional. In *Lord Portarlington v Soulby* (1834) 3 My & K 104 at 108, [1824–34] All ER Rep 610 at 612 Lord Brougham LC said:

> 'In truth, nothing can be more unfounded than the doubts of the jurisdiction. That is grounded, like all other jurisdiction of the Court, not upon any pretension to the exercise of judicial and administrative rights abroad, but on the circumstance of the person of the party on whom this order is made being within the power of the Court.'

An English court of equity will compel a defendant who is within the jurisdiction to treat assets in his hands as trust assets if, having regard to their history and his state of knowledge, it would

be unconscionable for him to treat them as his own. Where they have passed through many different hands in many different countries, they may be difficult to trace; but in my judgment neither their temporary repose in a civil law country nor their receipt by intermediate recipients outside the jurisdiction should prevent the court from treating assets in the legal ownership of a defendant within the jurisdiction as trust assets. In the present case, any obligation on the part of DLH to restore to their rightful owner assets which it received in England is governed exclusively by English law, and the equitable tracing rules and the trust concept which underlies them are applicable as part of that law. There is no need to consider any other system of law.

Knowing receipt

The plaintiff seeks a personal remedy based on 'knowing receipt'. As I have previously pointed out, this is the counterpart in equity of the common law claim for money had and received. The latter, at least, is a receipt-based claim to restitution, and the cause of action is complete when the money is received: see *Lipkin Gorman (a firm) v Karpnale Ltd* [1992] 4 All ER 512 at 527, [1991] 2 AC 548 at 572. So, in my judgment, is the former, unless arbitrary and anomalous distinctions between the common law and equitable claims are to be insisted upon. But it is necessary at the outset to identify the assets which DLH received, and the occasions upon which it received them. The plaintiff alleges that DLH received the sum of £270,000 in March 1986, and a further £1,030,000 in June 1986.

In my judgment, however, the position is somewhat more complicated than that. The sum of £270,000 was never received by DLH. It was paid into Grangewoods' client account, and their client at the time must be taken to have been DLH London. DLH London was not a nominee or agent for DLH. As had previously been agreed between Roth and Mr Stern, it was the intended contractual purchaser of the site, and the money was to be used exclusively for the payment of the deposit on exchange of contracts. In my judgment, DLH did not receive the money at all, and DLH London did not receive it beneficially but upon trust to apply it for a specific purpose. DLH London used the money, as it was bound to do, to pay the deposit on the site, and thereby acquired for its own benefit a corresponding interest in the site which it subsequently sold and transferred to DLH. The plaintiff can follow his money through these various transactions, but the relevant asset capable of being identified as having been received by DLH is an interest in the site corresponding to the payment of the deposit.

The sum of £1,030,000 was also paid into Grangewoods' client account, but by then their client had become DLH. The money was disbursed on the instructions and for the benefit of DLH. Only £745,598,4360 was used to pay the money due to the vendor on completion, but this was the result of the arrangements which DLH had made with Regalian. So far as Yulara is concerned, the whole £1,433m must be taken to have been disbursed as agreed between them on the acquisition of a 40% interest in the project. Moreover, in my judgment, on a proper analysis of the transaction between Yulara and DLH, Yulara's money should be treated as having been invested in its share of the project, and not in or towards the acquisition of DLH's share.

The investment proved highly successful. In itself it was not a breach of trust and caused the plaintiff no loss. Had he been able to intervene before the Canadians were bought out, he could have claimed the whole of Yulara's interest in the project; but whatever the extent of DLH's knowledge of the source of Yulara's funds, his claim would have been confined to Yulara's interest in exoneration of that of DLH. In the events which have happened, the plaintiff is in my judgment bound to treat his money as represented by Yulara's interest in the project, and must rely exclusively on the transaction on 16 March 1988 when Yulara's interest was bought out by DLH.

By that date Yulara's interest had (unknown to Yulara) crystallised into a 50% share in a sum of £4,4365m, which it sold to DLH (at an undervalue) for £1,4375m. In [1993] 3 All ER 717 at 739

those circumstances the plaintiff can, in my judgment, either affirm the transaction and claim payment of the purchase price (£1,4375m) for which DLH did not obtain a good receipt or repudiate the transaction and claim an account of its share of 50% of the £4,4365m (£2,325,000).

On electing to repudiate the sale of Yulara's interest, the plaintiff could if he wished have an account of what DLH did with the £4,4365m it received from Regalian, or the balance remaining after payment of the £1,4375m to Yulara, in an attempt to identify it as still in the possession of DLH with a view to asserting a proprietary claim against it to the extent of £2,325,000. The plaintiff has not sought to do so, seeing no advantage in the attempt. DLH is solvent and good for £2,325,000, and there is nothing to be gained by making a proprietary claim.

All this, of course, is dependent on the plaintiff establishing that DLH possessed the requisite degree of knowledge at the time of its purchase of Yulara's interest. DLH claims to be a bona fide purchaser for value without notice. Unfortunately, the nature of the knowledge required is highly controversial, at least where the recipient is a volunteer and the plaintiff brings a personal claim. In *Re Montagu's Settlement Trusts, Duke of Manchester v National Westminster Bank Ltd* [1992] 4 All ER 308 at 330, [1987] Ch 264 at 285 Megarry V-C expressed the view obiter that, in such a case, dishonesty or want of probity involving actual knowledge or wilful blindness is required. In *Agip (Africa) Ltd v Jackson* [1992] 4 All ER 451 at 467, [1991] Ch 547 at 567 Fox LJ expressed the view that dishonesty is not required, and that knowledge of any circumstances which would indicate the facts to an honest and reasonable man, and knowledge of circumstances which would put an honest and reasonable man on inquiry, are sufficient.

That was a case of knowing assistance, not knowing receipt, and it is not clear whether Fox LJ's remarks were intended to apply to the former. But they must at least cover the latter. In *Eagle Trust plc v SBC Securities Ltd* [1992] 4 All ER 488 at 509–510, [1993] 1 WLR 484 at 506–507 Vinelott J based liability firmly on inferred knowledge and not on constructive notice. For my own part, I agree that even where the plaintiff's claim is a proprietary one, and the defendant raises the defence of bona fide purchaser for value without notice, there is no room for the doctrine of constructive notice in the strict conveyancing sense in a factual situation where it is not the custom and practice to make inquiry. But it does not follow that there is no room for an analogous doctrine in a situation in which any honest and reasonable man would have made inquiry. Vinelott J held that knowledge might be inferred if the circumstances were such that an honest and reasonable man would have inferred that the moneys were probably trust moneys and were being misapplied. He left open the question whether a recipient might escape liability if the court was satisfied that, although an honest and reasonable man would have realised this, through foolishness or inexperience he did not in fact suspect it.

That question does not arise in the present case. In the absence of full argument I am content to assume, without deciding, that dishonesty or want of probity involving actual knowledge (whether proved or inferred) is not a precondition of liability; but that a recipient is not expected to be unduly suspicious and is not to be held liable unless he went ahead without further inquiry in circumstances in which an honest and reasonable man would have realised that the money was probably trust money and was being misapplied. That approach is in accordance with the preponderance of judicial authority in this country and New Zealand, and is consistent with an analysis of the underlying trust as a subsisting trust. Moreover, I do not see how it would be possible to develop any logical and coherent system of restitution if there were different requirements in respect of knowledge for the common law claim for money had and received, the personal claim for an account in equity against a knowing recipient and the equitable proprietary claim. In the present case, for example, it would be illogical and undesirable to require the plaintiff to assert a proprietary claim he does not need in order to avoid the burden of having to prove dishonesty or ask the court to infer it.

I turn, therefore, to the allegation that by June 1988, if not before, DLH possessed the necessary degree of knowledge that Yulara's funds represented the proceeds of fraud. DLH is a body corporate, and establishing knowledge on the part of an artificial person involves identifying particular individuals and attributing their knowledge to it. For this purpose, the plaintiff has singled out Mr Ferdman and Mr Stern as persons alleged to have possessed the necessary knowledge at the relevant time.

Outcome

In the Court of Appeal, Lords Nourse, Rose and Hoffmann accepted Millett J's analysis of the principles of tracing, but felt that the claimants did have the requisite level of knowledge that would enable the claimant to recover its assets.

Equitable tracing is also more advantageous to the beneficiary under a trust, who cannot trace at common law because the beneficiary has no entitlement to goods that the common law would recognise. It enables the beneficiary under a trust to trace those assets that a legal owner could trace under common law, such as clean substitutions, and a mixed bulk of tangible goods, where it is possible to grant each claimant a proportionate share of the goods. Therefore, where there has been a breach of trust on the part of a fiduciary, such as a trustee, the beneficiary-claimant is able to recover his or her property from the trustee.

However equitable tracing is also advantageous to both the legal and the equitable owner of property because it is possible to trace into a mixed fund. Where the claimant's money has been mixed with money belonging to the defendant, such as where a trustee has misappropriated the trust fund, the key aim is to maximise the benefit for the claimant. One approach therefore in such situations is to say that where the claimant's money and the defendant's own money is put in the same account, it is presumed that the defendant's money is spent first, leaving the claimant's money intact, as in *Boscawen v Bajwa* [1995] 4 All ER 769 at p.778 where Millett LJ states:

> A trustee will not be allowed to defeat the claim of his beneficiaries by saying that he has resorted to trust money when he could have made use of his own.

A different situation that may arise is where the defendant invests some of the mixed assets and then dissipates the rest. Here it is presumed that the defendant's intention was to preserve the claimant's fund, as with *Re Oatway* [1903] 2 Ch 356, where Joyce J states (p.360):

> when any of the money drawn out has been invested . . . the rest of the balance having afterwards been dissipated by him, he [the defendant] cannot maintain that the investment . . . represents his own money alone, and that what has been spent . . . was the money belonging to the trust. Clearly, the courts' objective in both these situations is to punish the defendant for his carelessness or wrongdoing.

What therefore is the situation where the money that one seeks to trace has been mixed with funds belonging to another innocent person, such as where the wrongdoer is the trustee for two different people? Let us say that he misappropriates two trust funds and places the money in a bank account. In this situation, there are two beneficiaries who are the victims of the defendant's wrongdoing, and evidently, there will be no desire on the part of the courts to punish either of them – both claimants are the victims of another person's wrongdoing. The objective here therefore is to achieve a fair and just result between the claimants. The traditional approach is that adopted in *Clayton's Case* (1816)

1 Mer 572, where it was presumed that money that is paid into a bank account first is also the money that is paid out first. However, this has largely been superseded by the approach taken by the Court of Appeal in *Barlow Clowes v Vaughan* [1992] 2 All ER 22.

This case involved a large number of people who had taken out investment plans with Barlow Clowes. The money invested was misapplied, and the company owed a great deal of money to its investors, but could not repay them what was owed. The court therefore had to consider how to divide the remaining assets between the investors, and decided that the *Clayton's Case* approach would be unjust because newer investors would get all their money back, while those who had invested with the company for many years would be left with nothing. Thus, the court decided that a fairer approach would be to consider that each person's investment had been proportionately reduced over time, so that each individual investor would get some of their money back.

EXTRACT

Barlow Clowes v Vaughan [1992] 4 All ER 22

Case facts

The appellant company went into liquidation owing several millions of pounds to investors. The respondent was appointed to distribute the remaining assets among the investors, and the defendant contended that this should occur on the basis of *Clayton's Case*, i.e. that the earlier investors should be repaid first. The appellant appealed arguing that the distribution should be on a proportionate basis, with all investors being entitled to a proportion of the fund.

Dillon LJ

It is, as I understand it, the view of the Secretary of State that in a case such as this, where so many individual investors contributed their moneys to BCI and its Portfolios 28 and 68 on the same basis, it would be unfair and inequitable if, by the accidents of tracing, a relatively small number of the investors were to be held entitled to the vast bulk of the available assets and moneys, as might result from the application of Clayton's Case. It will be necessary in this judgment to consider both the basis and the fairness of tracing in accordance with the rule in Clayton's Case, and how far this court is bound by previous decisions of this court to adopt that method of distribution.

The argument put by Mr Walker QC for the appellant is that instead of tracing or any application of Clayton's Case the available assets and moneys should be distributed pari passu among all unpaid investors rateably in proportion to the amounts due to them. This is the basis of distribution which-subject to any application which might be made by any individual depositor or shareholder with a view to tracing his own money into any particular asset-was directed by the House of Lords in *Sinclair v Brougham* [1914] AC 398, [1914–15] All ER 622 as between the shareholders in a building society which was being wound up and depositors who had made deposits in an ultra vires banking business which the building society had developed and carried on for many years. It is not in doubt that that basis of distribution ought to be adopted if distribution by tracing in accordance with Clayton's Case is not to be preferred.

We were indeed referred in the course of the argument to a third possible basis of distribution, which was called the 'rolling charge' or 'North American' method. This has been preferred by the Canadian and United States courts to tracing in accordance with Clayton's Case, as more equitable: see for instance the decision of the Ontario Court of Appeal in *Re Ontario Securities Commission and Greymac Credit Corp* (1986) 55 OR (2d) 673. This method goes on the basis

that where funds of several depositors, or sources, have been blended in one account, each debit to the account, unless unequivocally attributable to the moneys of one depositor or source (eg as if an investment was purchased for one), should be attributed to all the depositors so as to reduce all their deposits pro rata, instead of being attributed, as under Clayton's Case, to the earliest deposits in point of time. The reasoning is that if there is an account which has been fed only with trust moneys deposited by a number of individuals, and the account holder misapplies a sum from the account for his own purposes, and that sum is lost, it is fair that the loss should be borne by all the depositors pro rata, rather than that the whole loss should fall first on the depositor who made the earliest deposit in point of time. The complexities of this method would, however, in a case where there are as many depositors as in the present case and even with the benefits of modern computer technology be so great, and the cost would be so high, that no one has sought to urge the court to adopt it, and I would reject it as impracticable in the present case.

Clayton's Case (1816) 1 Mer 572, [1814–23] All ER Rep 1 was not a case of tracing at all, but a case as to the appropriation of payments. Clayton had been a customer of a banking partnership with an account in credit. One of the partners, Devaynes, had died in 1809 and the remaining partners became bankrupt at the end of July 1810. Clayton had had a running account with the bank before and after the death of Devaynes. The debits and credits made after the death of Devaynes were made without specific appropriation and the account had not been broken on the death of Devaynes. Clayton claimed after the bankruptcy to set his drawings on the account after the death of Devaynes against the credits to the account after the death of Devaynes; consequently he claimed to prove against the estate of Devaynes for the balance to his credit in the account at the death of Devaynes, on the footing that the balance had never been satisfied. Those claims were rejected by Grant MR, who said (1 Mer 572 at 608–609, [1814–23] All ER Rep 1 at 6):

> 'But this is the case of a banking account, where all the sums paid in form one blended fund, the parts of which have no longer any distinct existence. Neither banker nor customer ever thinks of saying, this draft is to be placed to the account of the £500 paid in on Monday, and this other to the account of the £500 paid in on Tuesday. There is a fund of £1000 to draw upon, and that is enough. In such a case, there is no room for any other appropriation than that which arises from the order in which the receipts and payments take place, and are carried into the account. Presumably, it is the sum first paid in, that is first drawn out. It is the first item on the debit side of the account, that is discharged, or reduced, by the first item on the credit side. The appropriation is made by the very act of setting the two items against each other. Upon that principle, all accounts current are settled, and particularly cash accounts. When there has been a continuation of dealings, in what way can it be ascertained whether the specific balance due on a given day has, or has not, been discharged, but by examining whether payments to the amount of that balance appear by the account to have been made? You are not to take the account backwards, and strike the balance at the head instead of the foot, of it. A man's banker breaks, owing him, on the whole account, a balance of £1000. It would surprise one to hear the customer say, "I have been fortunate enough to draw out all that I paid in during the last four years; but there is £1000, which I paid in five years ago, that I hold myself never to have drawn out; and, therefore, if I can find any body who was answerable for the debts of the banking-house, such as they stood five years ago, I have a right to say that it is that specific sum which is still due to me, and not the £1000 that I paid in last week." This is exactly the nature of the present claim.'

That rule will apply to the appropriation of payments between any trader and his customer where there is an account current or running account. But it will not apply unless there is a running account – see per Lord Halsbury LC in *Cory Bros & Co Ltd v Turkish Steamship Mecca (owners), The Mecca* [1897] AC 286 at 290–291, [1895–9] All ER Rep 933 at 935–936 and even in

relation to the appropriation of payments it is not, as Lord Halsbury LC said, an invariable rule: '. . . the circumstances of a case may afford ground for inferring that transactions of the parties were not so intended as to come under this general rule . . .'.

One case in which it was held that the nature and circumstances of a fund showed that the parties could not have intended Clayton's Case to be applied when the surplus in the fund fell to be returned to the subscribers is *Re British Red Cross Balkan Fund, British Red Cross Society v Johnson* [1914] 2 Ch 419, [1914–15] All ER Rep 459, a decision of Astbury J. There a fund had been collected by public subscription in 1912 for assisting the sick and wounded in the Balkan war of that time. By 1913 there remained a balance in the fund which was no longer required for the purposes of the fund and it was assumed that the surplus fell to be returned to the subscribers. Astbury J held that Clayton's Case, which would involve the attribution of the first payments out of the fund to the earlier contributions to it was not to be applied; he said ([1914] 2 Ch 419 at 421, [1914–15] All ER Rep 459 at 460): '. . . the rule is obviously inapplicable.'

The actual decision is suspect, since the objects of the fund would seem to have been charitable, and if they were charitable then, as the surplus did not come about through a failure of the charitable objects ab initio, the surplus should have been applied cy-près for other charitable purposes. If however for some reason the fund was not devoted to charity, the decision was plainly right. It was followed, in te case of a winding up of a non-charitable fund, by Cohen J in *Re Hobourn Aero Components Ltd's Air-Raid Distress Fund, Ryan v Forrest* [1945] 2 All ER 711 at 718, [1946] Ch 86 at 97; Cohen J's decision was affirmed by this court, but the only issue on the appeal was whether or not the fund was charitable (see [1946] 1 All ER 501, [1946] Ch 194).

There are many other cases in the books in which the court has been concerned with the distribution of the surplus on the winding up of a non-charitable benevolent fund and no one has suggested that Clayton's Case should be applied . . . I accordingly accept Mr Walker's narrower submission and would hold that Clayton's Case is not to be applied in the distribution of the available assets and moneys.

Mr Walker's wider submission is to the effect that, while the rule in Clayton's Case is valid and useful, subject to the observations in The Mecca, where what is in question is the appropriation of payments as between the parties to a running account, it is illogical and unfair to the earlier contributors to apply the rule as between innocent beneficiaries whose payments to a third party, BCI, have been paid by that third party into a bank account in which, at the end of the day, there are-for whatever reason-not enough moneys left to meet all claims.

Mr Walker submits that it might be more fair to apply the North American method outlined above, but as that is not practicable in the circumstances of this case, the court should fall back on a distribution *pari passu* between all investors in the proportions of the amounts respectively due to them.

For my part, so far as fairness is concerned, I have difficulty in seeing the fairness to a later investor whose contribution was in all likelihood still included in the uninvested moneys in the schedule A accounts, of holding that all those moneys must be shared *pari passu* by all investors early or late if there was no common investment fund. In addition of course the order made by the House of Lords in *Sinclair v Brougham* [1914] AC 398, [1914–15] All ER Rep 622, on which the order which Mr Walker seeks in the present case is modelled, was expressly subject to any tracing application by any individual depositor or shareholder. If the application of Clayton's Case is unfair to early investors *pari passu* distribution among all seems unfair to late investors.

Outcome

The appeal was allowed, and the money was divided proportionately across all the investors.

There are however limits to the scope of tracing in equity. Whereas common law tracing is applicable against anyone who has acquired an asset belonging to the claimant, equitable tracing ceases to be available once the asset or its substitution fall into the hands of a bona fide purchaser for value without notice. If the wrongdoer then becomes insolvent, the claimant who must rely on equitable tracing is left with no remedy. He or she cannot sue the wrongdoer, or a recipient, because they are insolvent, but cannot trace the asset or its substitution either.

Equitable tracing is also ineffective where the asset has been dissipated or has ceased to exist.[4] Therefore if the money is used to purchase a holiday, or is used to repay a debt, or an asset is destroyed, equitable tracing can no longer succeed. Another difficulty in the context of mixed funds is where the claimant's money is mixed with other funds, some of the fund is then dissipated, but other money is later added. Unless the money that is added is intended to replenish the trust fund, it is not possible to use it for the purposes of tracing – as in *James Roscoe (Bolton) Ltd v Winder* [1915] 1 Ch 62.

It is also impossible to trace in equity into unascertained goods. In other words, where goods have not been identified as belonging to the claimant, such as where items are ordered from a company and not been separated out from the larger bulk so that is clear which particular items belong to the claimant, the claimant cannot be said to have any right to the goods, and therefore they cannot be the subject of equitable tracing. This is shown in *Re Goldcorp Exchange Ltd* [1994] 2 All ER 806, where, in the event of the company becoming insolvent it was deemed to be impossible for the claimants to get their money back on items they had ordered. They therefore attempted to claim ownership of the gold bullion they had ordered by virtue of equitable tracing. This too failed because until the gold was separated and identified as belonging to the claimant, they had no right of ownership over it. This is also a problem with money transferred into bank accounts. Because the property is intangible, it is difficult to say that it belongs to the claimant, especially in cases involving multiple transfers from one account to another. Accordingly, in *Westdeutsche Landesbank Girozentrale v Islington LBC* [1996] AC 669, it was held that it was difficult to identify money in a bank account as belonging to the claimant.

However, lack of identification should be distinguished from cases where assets belonging to the claimant have been mixed. Clearly in such cases the claimant can claim ownership, and therefore tracing will succeed. The difficulty with money in bank accounts is that, with the exception of straightforward cases such as *FC Jones v Jones*, where it could be seen that the money in Mrs Jones' account was the same money that had been given as a loan, it is difficult to say that 'that particular money belongs to the claimant'. However, many of the cases referred to have involved money having been moved from one account to another, including accounts that are overdrawn, with the result that it is very easy, in cases of significant duplicity, to make tracing workable – once the money has gone into an overdrawn account, it is no longer property, merely the cancellation of a debt. However, this means that claimants from whom money has been misappropriated are left without any form of redress.

Furthermore, in some cases it will be considered inequitable to trace, as with *Re Diplock* [1948] Ch 465 where an innocent volunteer has used traceable assets to improve his land. It was held that forcing the sale of the land to enable the claimant to recover his money was an unfair use of the principles of equitable tracing.

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[4] *Bishopsgate Investment Management v Homan* [1995] Ch 211.

Other comments on tracing

Tracing can be very useful for the claimant. He is entitled to claim any increase in value in the item traced, as well as its original value. A case that illustrates this is *FC Jones and Sons v Jones* [1996] 3 WLR 703, where FC Jones & Sons had loaned money to Mrs Jones, which she had invested very successfully, making a large profit. However FC Jones was not entitled to lend the money to Mrs Jones because it was bankrupt at the time, and therefore the Official Receiver was able to trace the money and the profit Mrs Jones had made.

Remedies

Where tracing occurs, the claimant is entitled to claim either the original asset or its clean substitution, whereby the defendant becomes a constructive trustee of the asset, until it is transferred to the claimant.

Where the claimant's assets are mixed with those of an innocent person, the claimant is entitled to claim a proportionate share of the fund. Where the claimant's assets are mixed with those of the wrongdoer, the case of *Foskett v McKeown* confirms that the claimant can claim a proportionate share of the mixed asset. The claimant has a choice of either claiming a charge over the property or a lien (pronounced lee-en). Where a charge is selected, the claimant claims the value of the item misappropriated, and may sell the item if the debt is not repaid.

With a lien, the claimant takes possession of the asset, and holds it as a security in respect of the claimant's claim for damages against the defendant. This may be useful where the item itself is of greater value than the payment of damages.

A constructive trust would be appropriate if the asset could not be immediately transferred, such as in the case of land or shares. A charge may be more appropriate if the property decreases in value, as the value of the claim is the value of the debt owed, whereas a lien or a constructive trust may be more advantageous if the property increases in value. A charge or a lien is more appropriate where the property is identifiable and separate (a painting for example) whereas a constructive trust is more appropriate in the case of a mixed fund.

Therefore the asset may be sold if the debt is not repaid. The significance of this is that where the asset has increased in value, it is beneficial for the claimant to claim the asset itself. If on the other hand the asset has decreased in value, the lien represents a better claim, because it will enable the claimant to claim the full value misappropriated.

ACTIVITY

Evaluate the advantages and disadvantages of tracing in equity. What reforms would you make to the law?

This is a fairly typical example of the type of question examiners and assessors ask in relation to tracing.

An approach to the question would be to imagine yourself on the side of those who favour tracing in equity. What would their arguments be? How would they seek to convince someone

of the advantages of tracing in equity? What evidence would they introduce in order to support their argument?

Now consider the opposing point of view. What would those who oppose the concept of tracing in equity argue? Again, consider what evidence they would introduce to support their argument.

Consider also how each side would seek to undermine the other side's arguments.

A common weakness with essays and assessments is to fail to consider that the weaknesses identified in the second part of the essay should inform the suggestions for reform. Accordingly, if you have identified (for example) the inability to trace into the hands of a bona fide purchaser for value without notice as being a weakness of tracing in equity, how would you reform this?

The future of common law and equitable tracing

The overlap between common law and equitable tracing means that some would argue that there is a need for reform of the law, so as to develop a single law of tracing, thus eliminating the distinctions that subsist, arguably unnecessarily, between common law and equitable tracing. In *Foskett v McKeown* [2000] AC 10 at p.127 for example, Lord Millet makes the argument against common law and equitable tracing needing to be separate concepts most unequivocally:

> Given its nature, there is nothing inherently legal or equitable about the tracing exercise. There is thus no sense in maintaining different rules for tracing at law and in equity. One set of tracing rules is enough. The existence of two has never formed part of the law in the United States: see *Scott on Trusts*, 4th ed (1989), section 515, at pp 605–609. There is certainly no logical justification for allowing any distinction between them to produce capricious results in cases of mixed substitutions by insisting on the existence of a fiduciary relationship as a precondition for applying equity's tracing rules. The existence of such a relationship may be relevant to the nature of the claim which the plaintiff can maintain, whether personal or proprietary, but that is a different matter.

Yet, perhaps it is in this argument that the counter-argument is advanced. Perhaps, although there is overlap between common law and equitable tracing regarding what may be traced and how the process occurs; perhaps it is in the distinction between the proprietary claim and the personal claim that the difference is needed. Tracing at common law means that the claimant is able to follow the goods into the hands of anyone who has or had them – the claim is proprietary in that the claimant is entitled to the goods themselves. On the other hand, following in equity will be defeated by the transfer of the goods to a bona fide purchaser for value without notice. The claimant's claim is therefore necessarily personal against the trustee or the person who has acquired the goods either without an element of consideration or whilst having notice of the claimant's entitlement. For this reason, the argument whether there should be further fusion between common law and equity in this area is a debate which continues. Martin for example argues very strongly in favour of a more unified approach to tracing:

EXTRACT

Martin, J.E. (1994) 'Fusion fallacy and confusion' *Conveyancer and Property Lawyer* 13

Personal liability in equity can attach to persons who have received trust property for their own benefit or who have knowingly assisted in a fraudulent breach of trust. It is now generally settled in England that dishonesty is required for 'knowing assistance.' Earlier authorities regarding constructive knowledge as sufficient have been rejected. To regard negligence as the basis of liability subverts the principles of equity and sidesteps the tort rule against liability for negligently causing economic loss. Negligence should play no greater part here than in the mortgage cases discussed earlier. The negligence approach has recently been favoured in New Zealand by Thomas J., who referred to 'This happy mingling of law and equity.' Wylie J., rejecting this view, has emphasised that negligence is a different cause of action based on different principles and having a different historical background: 'We have not yet reached the stage where the conventional ingredients of causes of action can be ignored for the purpose of enabling the courts to arrive at some ill-defined and undisciplined objective of being fair.'

In the case of liability for 'knowing receipt,' the weight of authority supports the view that constructive knowledge suffices, although the point is not settled. This is an area where the courts should strive to achieve a coherent doctrine by reflecting on the position at common law where a volunteer is liable for money had and received without regard to his state of knowledge, subject to the defence of change of position. An innocent volunteer who retains the property is, of course, liable to a tracing action. The personal action in equity, being restitutionary, should be based not on fault but on the fact of receipt. After all, innocent volunteers who receive the property of another in the administration of an estate are personally liable. Now that the defence of change of position has been recognised, there is no reason why an innocent volunteer should not be liable in equity to an equitable owner, just as he is liable at common law to a legal owner, without regard to his state of knowledge. Any other view leads to the unjust enrichment of the volunteer.

Sir Peter Millett has taken some extra-judicial steps in this direction. He returned to the theme in *El Ajou v. Dollar Land Holdings plc* [[1994] 2 All ER 685], considering that as both the common law action for money had and received and the action in equity were receipt-based, the rules should be similar 'unless arbitrary and anomalous distinctions between the common law and equitable claims are to be insisted on.' Rejecting any requirement of actual knowledge, he continued:

'I do not see how it would be possible to develop any logical and coherent system of restitution if there were different requirements in respect of knowledge for the common law claim for money had and received, the personal claim for an account in equity against a knowing recipient and the equitable proprietary claim. In the present case, for example, it would be illogical and undesirable to require the plaintiff to assert a proprietary claim he does not need in order to avoid the burden of having to prove dishonesty or ask the court to infer it.'

The difficulty is that, by requiring constructive knowledge for the claim in equity against a recipient of trust property, we have not yet achieved a logical and coherent doctrine. As the equity principles are not yet settled, there is no reason why the courts should not look to the common law to achieve a rational principle and avoid the anomalies referred to by Millett J. This could be done without attributing the result to a 'fusion' of law and equity.

The differences between the tracing rules at law and in equity are well known. They have not escaped criticism. Equity for example, requires a fiduciary relationship, while the common law cannot trace into a mixed fund. Millett J. in *Agip (Africa) Ltd. v. Jackson* [[1991] Ch 547] called for

the development of a unified restitutionary remedy to replace the common law and equitable rules. The Court of Appeal in that case was more conservative, taking a traditional view of tracing. The House of Lords in *Lipkin Gorman v. Karpnale Ltd.* [[1991] 2 AC 548] envisaged that the acceptance of the defence of change of position would encourage a more consistent approach to tracing, in which common defences would be recognised whether the claim proceeded at law or in equity. The point to be made here is the same as in relation to 'knowing receipt,' discussed above. There is no ground for asserting that the legal and equitable origins of the tracing rules should now be disregarded. The task of the courts is to develop the rules in a coherent way so that there are no anomalous distinctions between the rights of legal and equitable owners. It is evident that they intend to do so.

Villiers also argues very strongly in favour of a more unified approach:

EXTRACT

Villiers, T. (1999) 'Progress towards a coherent law of tracing: will common law catch up with equity?' 7(1) *Journal of International Trust and Corporate Planning* 51

Jones v Jones [[1997] Ch 159] is the first case where the common law has been used successfully to claim the profit from traced assets. The possibility of such a claim seems to have been well within the scope of previous authorities. Hence *Jones* does not represent any radical new development. The means by which Millett LJ justified the claim for profits do merit consideration, however. His Lordship relied on general restitutionary principles. Were Mrs Jones to be able to keep the profits from the scheme she would be unjustly enriched at the expense of the trustee. He also relied, however, on technical tracing rules. He emphasised that tracing was neither a cause of action nor a remedy but merely a process by which assets were identified after a series of substitutions.

Millett LJ acknowledged that the whole edifice of the common law tracing was built on uncertain foundations. The case in which the common law's ability to trace was first seemingly upheld was *Taylor v Plumer* [[1997] Ch 159]. His Lordship held that the principles considered in *Taylor* were actually those of equity, albeit that the case was decided on by the common law court. However, in his Lordship's view this did not undermine the line of authority or the common law principles for which *Taylor* was later taken to stand. To draw such a conclusion would, it was averred, be to misunderstand the way in English doctrine of stare decisis works: 'It would be more consistent with the doctrine to say that in recognising claims to substituted assets, equity must have been taken to have followed the law even though the law was not declared until later.' In essence, a long established error makes good law.

Conclusion

The facts of *Jones v Jones* have been described as freakish, since extensive dealings were made with the funds but no mixing took place at any point. The practical impact of the case is limited because the Court of Appeal did not, at any point, question that principle that the common law cannot trace through a mixed fund. Unless overturned, this principle will continue to provide a significant brake on the development and the expansion of common law tracing. Its inevitable effect is that equity will continue to offer far more effective and wide ranging tracing rights than the common law.

Watts on the other hand is more cautious, and argues that there continues to be a distinct role for tracing in equity in cases where it would be unconscionable not to allow the claimant to trace. This maintains the distinction that exists between tracing being available as of right, and tracing being based on the equitable notions of fairness and good conscience. Therefore in the same way as an equitable remedy is only available where it is just and convenient, a similar approach might be taken in some situations in relation to equity. In other words, equitable tracing would be available where a claimant is not ordinarily entitled to trace, but where the unconscionability of the defendant justifies it, then tracing will be allowed.

EXTRACT

Watts, P. (1990) 'Tracing at common law and in equity' 106 *Law Quarterly Review* 550

The second case, *Elders Pastoral Ltd. v. Bank of New Zealand* [1989] 2 N.Z.L.R. 180, involved the bank's claim, as mortgagee, to transfer its security interest from the original secured assets to the proceeds of their disposition, in priority to the claim of an agent of the mortgagor which was holding the proceeds. The mortgaged assets were farm animals that had been sold by the mortgagor through the appellant stock agent, which then asserted a right to off-set the proceeds against debts the mortgagor owed it on other accounts. The court upheld the claim of the bank.

The decision would not have been particularly significant had the mortgage expressly extended to the proceeds of sale of the stock. Nor would the case have made new law had the mortgage sufficiently clearly prohibited the sale of the stock, which the court held it did not do. There is authority to support the proposition that a mortgagee can claim in equity the proceeds of an unauthorized disposition of the mortgaged assets (see *Re Miles* (1989) 85 A.L.R. 216; *Canadian Imperial Bank of Commerce v. Kernel Farms Ltd.* (1984) 6 D.L.R. (4th) 384, aff'g (1983) 138 D.L.R. (3d) 128; and *Siebe Gorman & Co. Ltd. v. Barclays Bank Ltd.* [1979] 2 Lloyd's Rep. 142 at p. 156). If there is a legal mortgage the plaintiff may also have actions in conversion and money had and received. As it happened, although the mortgage contained a clause requiring the mortgagor to pay the proceeds from any sale of stock to the bank (cf. the clause in *Siebe Gorman*), the court did not hold that this clause created either an express trust or charge over the proceeds, or an assignment of the rights to payment by purchasers of the stock. Instead, Cooke P., with whom Richardson J. agreed, imposed a constructive trust in respect of the proceeds because it would have been against conscience for the mortgagor and the agent to withhold the proceeds from the bank. In so holding, Cooke P. pointed out (at p. 185) that contract was not the only way in which equitable rights can arise. His Honour quoted and approved a lengthy passage in Goff and Jones, The Law of Restitution (3rd ed.) at p. 77 which suggests (relying on *Sinclair v. Brougham* [1914] A.C. 398, *Chase Manhattan Bank N.A. v. Israel-British Bank (London) Ltd.* [1981] Ch. 105 and *Neste Oy v. Lloyd's Bank Plc. (The Tiiskeri)* [1983] 2 Lloyd's Rep. 658) that unconscionability is the key to establishing a right to trace in equity and not the presence of a fiduciary relationship as has traditionally been thought. The other member of the court. Somers J., considered that the relevant provision in the mortgage did create a fiduciary relationship between the parties in respect of the proceeds, but he also approved the passage in Goff and Jones.

The dropping of a fiduciary requirement from the right to trace is to be welcomed, although it has to be admitted that its replacement with unconscionability can only be the starting point for further analysis (as is shown by the controversy surrounding Chase Manhattan – see

A. Tettenborn, [1980] C.L.J. 272, and G. Jones, [1980] C.L.J. 275). However, with respect, it is submitted that there ought not to be room for the imposition by operation of law of a trust based on unconscionability where there is a valid contract between the same parties which does not provide for such an interest. This was the position in the Elders case, and, though with more difficulty, in The Tiiskeri as well. So, if it was not able to find that the bank had stipulated that its mortgage applied to the proceeds of sale of the stock, the court ought not to have nursed the bank by giving it the extended security to the prejudice of others not party to the contract. On the other hand, the finding by Somers J. that a fiduciary relationship was intended to be created by the contract might have supported a right to trace (see *Palette Shoes Pty, Ltd. v. Krohn* (1937) 58 C.L.R. 1; *Romalpa*; and *Len Vidgen Ski & Leisure Ltd. v. Timaru Marine Supplies (1982) Ltd.* [1986] 1 N.Z.L.R. 349. Cf. E. Pfeiffer *Weinkellerei-Weinenkauf GmbH & Co. v. Arbuthnot Factors Ltd.* [1988] 1 W.L.R. 150).

A further difficulty with the *Elders* case concerns the Court's holding (at p. 186 per Cooke P. and at p. 193 per Somers J.) that *Elders* was as equally affected by the constructive trust, or his other fiduciary obligations, as the farmer, on the simple ground that, being the farmer's agent, it could not be in any better position than its principal. No authority was cited. This reasoning appears inconsistent with a leading case on set-off, which happened to involve an agent, *Roxburghe v. Cox* (1881) 17 Ch.D. 520 (C.A.). In the ordinary course, an agent is entitled to set off, in any accounting with its principal, sums owed to it by the principal (see *Bowstead on Agency* (15th ed.) at pp. 246–247), and it appears from *Roxburghe* that that right is no different from that of an ordinary debtor. Such persons generally need to have at least constructive notice of the competing security interest of the third party before losing the right of set-off. The only question is whether it might also be necessary for the agent to show that it had acted in reliance on the receipt or given consideration for the set-off (in other words that it is a bona fide purchaser for value) before receiving notice of the competing security interest. This difficulty has arisen in relation to set-offs and combining of accounts by banks when they receive money as agents for customers the accounts of which are otherwise in debit. The cases not only require some degree of knowledge by banks of the competing equity (see *The Tiiskeri, and Westpac Banking Corp. v. Savin* [1985] 2 N.Z.L.R. 41 (C.A.)), but some also seem to favour the right of the bank to set off irrespective of detriment, though this has been criticised (see *Union Bank of Australia v. Murray-Aynsley* [1898] A.C. 693, criticised by Ellinger, *Modern Banking Law* (1987) at p. 152. Cf. *The Tiiskeri* (at p. 666), and *Barclays Bank Ltd. v. Quistclose Investments Ltd.* [1970] A.C. 567, 582, discussed on this point in Derham, *Set-Off* (1987) at pp. 284–285).

The future development of the law of tracing is therefore an interesting area which includes a number of important issues to be discussed. For this reason it is a popular topic for assignments and examinations, as well as being an interesting area within which to undertake further research, for example as part of an extended project or a dissertation.

Conclusion

What this book has demonstrated is that although equity and the law of trusts is a comparatively straightforward subject in the sense that much of it is concerned with preventing the unjust deprivation by one person of an entitlement to property by another, its flexibility means that it can be used in a vast range of circumstances. It is innovative, and able to be applied to new and different situations. There is also considerable scope for differences of opinion and approach. Because the emphasis is often on finding that the defendant has acted unconscionably, as opposed to acting in contravention of some

direct rule, it is possible to present convincing arguments on both sides for most of the situations represented. It is also a very relevant and very socially pertinent subject. Most people either sought or will seek to acquire property or to share property with another at some point in their lives, sometimes with a clearly established expectation of gain (such as ordering goods from a company), sometimes with no clear expectation of gain, but equally no expectation of being unjustly deprived either. Most of the time one does not enter into these arrangements with an eye to following the formalities of the law. It is all rather too hard-nosed, too callous, too indicative of a lack of trust in our fellow man or woman, and perhaps it is good that it is so. Many commercial and domestic relationships would not survive the protracted negotiations of lawyers present at their inception. On the other hand, when that trust is misplaced, the law needs to intervene. Sometimes it cannot do so, and the loss is attributed to misfortune, and a warning to be wiser in future. Sometimes however, the law realises that it must intervene. Equity, and the concept of the trust is its mechanism for doing so.

Chapter summary

This chapter may be useful for assessments and assignments on:

- Tracing
- Equitable processes and remedies
- The fusion of common law and equity.

Further reading

Baughen, S. (2002) 'Tracing a Future for the Common Law: The Action for Money Had and Received After Foskett McKeown' 31(2) *Common Law World Review* 165.

Burrows, A. (2002) 'We do this at common law but that in equity' 22(1) *Oxford Journal of Legal Studies* 1.

Congalen, M. (2010) 'Difficulties with tracing backwards' 127 *Law Quarterly Review* 432.

Panesar, S. (2012) 'Equitable tracing Part 1' 133 *Trusts and Estates Law and Tax Journal* 17.

Panesar, S. (2012) 'Equitable tracing Part 2' 134 *Trusts and Estates Law and Tax Journal* 23.

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