Michael Ashdown
Somerville College
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REMEDIES FOR BREACH OF TRUST

1. PRELIMINARY ISSUES

- A wider range of possible responses to a breach of trust is available than merely compensation for loss.

A. Multiple parties

- Trustees
- Third party assistants and recipients of trust property

B. Personal and proprietary remedies

- Personal liability
- Recovery of trust property or its substitute
  - Unique property
  - Bankruptcy of the trustee
  - Bankruptcy of the third-party recipient

2. AN OVERVIEW OF REMEDIES FOR BREACH OF TRUST

A. The problem

- Dave is a trustee. The assets in the trust fund are 1000 shares in Widget plc, and a valuable vase. Dave's brother Boris encourages Dave to sell the Widget shares and to buy shares in Gadget plc. Boris is a shareholder in Gadget and hopes that this will increase the value of his own shares.
- Dave is the only trustee, and he isn't quite sure what he is supposed to do as trustee. So he meets with Olivia, his solicitor. Dave and Olivia discuss what they should do with the trust, and decide:
  1. To sell the shares in Widget plc and buy shares in Gadget plc with the proceeds.
  2. To give the vase to Miriam as a gift.
- Each of these transactions is a breach of trust. The trustee is allowed to invest in Widget shares but not Gadget shares. The trustee is not allowed to give the vase to Miriam.
- The sale of the Widget shares raised £100,000. The Gadget shares which were bought with this money haven't done very well, and are now worth £20,000.
- Miriam has sold the vase to Roger for £30,000. She gave £10,000 of this to charity, and bought a new car with the remaining £20,000.

B. The issues

(1) Personal claims against a trustee

- Dave's personal liability
- Defences – consent, s61 Trustee Act 1925, exemption clause

(2) Proprietary claims

- Possible claims to the vase and to Miriam's new car

(3) Personal claims against third parties

- Trusteeship *de son tort*
- Dishonest assistance
- Knowing receipt

3. PERSONAL CLAIMS AGAINST TRUSTEES

A. Types of breach

- Misapplication of trust property
- Failure to acquire or make profit
- Profit stripping

B. Remedying a breach: account

- R Chambers, 'Liability' in P Birks and A Pretto (eds), *Breach of Trust* (Hart Publishing, Oxford 2002)
- Simply ordering a payment of money is not an adequate substitute for performance.

- *Target Holdings Ltd v Redferns* [1996] AC 421 (HL) 434 (Lord Browne-Wilkinson): "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."

(1) Information

- *Re Londonderry's Settlement* [1965] 1 Ch 918 (CA)
- *Schmidt v Rosewood Trust Ltd* [2003] UKPC 26, [2003] 2 AC 709
- *Chaine-Nickson v Bank of Ireland* [1976] IR 393 (High Court, Ireland)
- A beneficiary will almost always be entitled to see the trust accounts, and the document which created the trust – usually a deed or a will.

(2) Taking the account

- Trustees have to provide a record of all trust transactions, and have to be able to justify each one. They have to pay whatever is found to be due.

(3) The accounting process

- *Re Wrightson* [1908] 1 Ch 789 (Ch) (Warrington J): breach of trust must be proven by the beneficiaries

(4) Falsification

- Falsification creates an arithmetical shortfall in the trust fund which the trustees must make up.
- Interest is payable on the shortfall: "this is on the notional ground that the money so applied was in fact the trustee's own money and that he has retained the misapplied trust money in his own hands and used it for his own purposes." *Wallersteiner v Moir (No 2)* [1975] QB 373 (CA) 397 (Buckley LJ).

(5) Surcharging

- Beneficiaries must prove "wilful default".
- *Armitage v Nurse* [1998] Ch 241 (CA) 252 (Millett LJ): "A trustee is said to be accountable on the footing of wilful default when he is accountable not only for money which he has in fact received but also for money which he could with reasonable diligence have received. It is sufficient that the trustee has been guilty of a want of ordinary prudence"
- Amount of surcharge is "fair compensation": *Nestle v National Westminster Bank Plc* [1993] 1 WLR 1260 (CA) 1269 (Dillon LJ)

(6) Profits made by trustees misapplying the trust fund

- PJ Millett, 'Equity's place in the law of commerce' (2008) 114 LQR 214
- "He must account for what he has done with the trust money, not merely for what he has properly done with it." (2008) 114 LQR 214, 226.
- "Where the beneficiary accepts the unauthorised investment, he is often said to affirm or adopt the transaction. That is not wholly accurate. The beneficiary has a right to elect, but it is merely a right to decide whether to complain or not." (2008) 114 LQR 214, 226.

- *Sinclair Investments (UK) Ltd v Versailles Trade Finance Ltd* [2011] EWCA Civ 347, [2011] 3 WLR 1153
- Cp *Lister v Stubbs* (1890) 45 Ch D 1, *A-G of Hong Kong v Reid* [1993] AC 713

C. Some particular problems

(1) Off-setting profits and losses

- *Dimes v Scott* (1828) 4 Russ 195
- *Bartlett v Barclays Bank Trust Co Ltd (No 1)* [1990] Ch 515 (Ch) 538 (Brightman LJ): "The general rule … is that where a trustee is liable in respect of distinct breaches of trust, one of which has resulted in a loss and the other in a gain, he is not entitled to set off the gain against the loss, unless they arise in the same transaction"

  "The Guildford development stemmed from exactly the same policy and … exemplified the same folly as the Old Bailey project. Part of the profit was in fact used to finance the Old Bailey disaster. By sheer luck the gamble paid off handsomely, on capital account. I think it would be unjust to deprive the bank of this element of salvage in the course of assessing the cost of the shipwreck."

(2) Causation

TRADITIONAL PRINCIPLES

- If the trustee invests in unauthorised investments, or puts the fund in the possession of somewhat not authorised to have it, and a loss is suffered to the fund, then he "will be liable to make it good, however unexpected the result, however little likely to arise from the course adopted, and however free such conduct may have been from any improper motive. Thus, if he omit to sell property when it ought to be sold, and it be afterwards lost without any fault of his, he is liable…": *Clough v Bond* (1828) 3 My & Cr 490, 496 (Lord Cottenham LC).

TARGET HOLDINGS LTD V REDFERNS

- *Target Holdings Ltd v Redferns* [1996] AC 421 (HL)

Lord Browne-Wilkinson's judgment

- *Target Holdings Ltd v Redferns* [1996] AC 421 (HL) 432:
  "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… 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."

- "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…." [1996] AC 421 (HL) 434.
- "Target obtained exactly what it would have obtained had no breach occurred, i.e. a valid security for the sum advanced." [1996] AC 421 (HL) 440.

- *Harris v Kent* [2007] EWHC 463 (Ch) [130] (Briggs J): Compensation is the primary remedy "unless there is good reason to require the reconstitution of the fund, rather than the simple short-cut of compensating the beneficiary".
- *Knight v Haynes Duffell, Kentish & Co* [2003] EWCA Civ 223 (Aldous LJ).

Lord Millett's criticism

- PJ Millett, 'Equity's place in the law of commerce' (2008) 114 LQR 214
- *Target Holdings Ltd v Redferns* [1996] AC 421 (HL) 435 (Lord Browne-Wilkinson):
  "it is important, if the trust is not to be rendered commercially useless, to distinguish between the basic principles of trust law and those specialist rules developed in relation to traditional trusts which are applicable only to such trusts and the rationale of which has no application to trusts of quite a different kind."

- Family trusts vs commercial trusts
- Why "but for causation" – but not other common law causation or remoteness rules?
- Applying accounting principles to *Target Holdings Ltd v Redferns*.

- *Murad v Al-Saraj* [2005] EWCA Civ 95
- J Edelman, 'Money Awards of the Cost of Performance' (2010) 4 J Eq 122, 127-30.

(3) Equitable compensation

- The principal remedy for a breach of trust is the taking of the account, and falsifying or surcharging that account.
- Beneficiary may suffer a loss caused by trustee's breach of duty, where there is no corresponding diminution of the trust fund

- *Nocton v Lord Ashburton* [1914] AC 932 (HL): Equitable compensation where there is no trust.
- *Target Holdings Ltd v Redferns* [1996] AC 421 (HL): Equitable compensation as a remedial short-cut.
- *Sinclair Investments (UK) Ltd v Versailles Trade Finance Ltd* [2011] EWCA Civ 347, [2011] 3 WLR 1153

(4) Breach of the duty of care

- *Bristol and West Building Society v Mothew* [1998] Ch 1 (CA) 17 (Millett LJ):
  "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."

- *Henderson v Merrett Syndicates Ltd* [1995] 2 AC 145 (HL) 205 (Lord Browne-Wilkinson):
  "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 for or advise others."

- J Getzler, 'Duty of Care' in P Birks and A Pretto (eds), *Breach of Trust* (Hart Publishing, Oxford 2002)

4. DEFENCES

A. Consent

- If a beneficiary agrees to the trustee committing a breach of trust, the beneficiary can't then bring a claim for breach of trust.
- Does a beneficiary have to know that what he is consenting to is a breach of trust?
- When will the apparent consent of a beneficiary not protect the trustee – what could invalidate apparent consent?

(1) Re Pauling's Settlement Trusts

- *Re Pauling's Settlement Trusts* [1962] 1 WLR 86 (Ch) (Wilberforce J)

- *Walker v Symonds* (1818) 3 Swans 1, 64 (Lord Eldon LC):
  "It is established by all the cases, that if the cestui que trust joins with the trustees in that which is a breach of trust, knowing the circumstances, such a cestui que trust can never complain of such a breach of trust. I go further, and agree that either concurrence in the act, or acquiescence without original concurrence, will release the trustees: but that is only a general rule, and the court must inquire into the circumstances which induced concurrence or acquiescence; recollecting in the conduct of that inquiry, how important it is on the one hand, to secure the property of the cestui que trust; and on the other, not to deter men from undertaking trusts for the performance of which they seldom obtain either satisfaction or gratitude."

- *Re Pauling's Settlement Trusts* [1962] 1 WLR 86 (Ch) 108 (Wilberforce J):
  "the court has to consider all the circumstances in which the concurrence of the cestui que trust was given with a view to seeing whether it is fair and equitable that, having given his concurrence, he should afterwards turn round and sue the trustees: that, subject to this, it is not necessary that he should know that what he is concurring in is a breach of trust, provided that he fully understands what he is concurring in, and that it is not necessary that he should himself have directly benefited by the breach of trust."

(2) Knowledge of the breach of trust

- J Payne, 'Consent' in P Birks and A Pretto (eds), *Breach of Trust* (Hart Publishing, Oxford 2002) 305:
  "The preferable view is not to regard Wilberforce J's specific knowledge test as a universal test but instead to concentrate on the general principle which he sets down in *Re Pauling*, ie, to take all the facts into account when determining whether the beneficiary should be denied a remedy. This could well mean that in a given fact situation it will only be fair and equitable to deny the beneficiary a claim against the trustee if the beneficiary did appreciate the legal consequences of his or her consent." (p305)

- *Holder v Holder* [1968] Ch 353 (CA)

(3) Vitiated consent

- Full age and capacity
- Undue influence - *Re Pauling's Settlement Trusts* [1962] 1 WLR 86 (Ch)
- Other vitiating factors: duress, misrepresentation, mistake?

- Unfairness: *Chellaram v Chellaram (No 2)* [2002] EWHC 632 (Ch), [2002] 3 All ER 17 [187] (Lawrence Collins J)

B. Section 61, Trustee Act 1925

- If it appears to the court that a trustee, whether appointed by the court or otherwise, is or may be personally liable for any breach of trust, whether the transaction alleged to be a breach of trust occurred before or after the commencement of this Act, but has acted honestly and reasonably, and ought fairly to be excused for the breach of trust and for omitting to obtain the directions of the court in the matter in which he committed such breach, then the court may relieve him either wholly or partly from personal liability for the same.

- *Re Turner* [1897] 1 Ch 536 (Ch) 542 (Byrne J): "I think that the section relied on is meant to be acted upon freely and fairly in the exercise of judicial discretion".

(1) Carelessness

- *Re Turner* [1897] 1 Ch 536 (Ch) (Byrne J)
- *Speight v Gaunt* (1883) 22 Ch D 727 (CA) 739 (Jessel MR): "a trustee ought to conduct the business of the trust in the same manner that an ordinary prudent man of business would conduct his own"
- Judicial Trustees Act 1896, s3 – materially identical to Trustee Act 1925, s61.
- *Lloyds TSB Bank plc v Makandan & Uddin* [2012] 2 All ER 884 at [60]-[61]
- Strict liability vs duty of care

(2) Legal advice

- *Marsden v Regan* [1954] 1 WLR 423 (CA) 434-435 (Evershed MR): "The mere fact that you take a solicitor's advice, natural and prudent though such a course be, will not automatically result in relief being given."

- *Perrins v Bellamy* [1899] 1 Ch 797 (CA) 801: Lindley MR called the breach "a most judicious breach of trust" and said that "there is not one trustee in a thousand, or one business man in a thousand, who would not have done likewise."

- *Re Allsop* [1914] 1 Ch 1 (CA) 13 (Cozens-Hardy MR): "He cannot be considered to have acted reasonably if he has neglected to obtain skilled advice."

- *Davis v Hutchings* [1907] 1 Ch 356

(3) Ought fairly to be excused

- *National Trustees Company of Australasia v General Finance Company of Australasia* [1905] AC 373 (PC) (Sir Ford North)
- *Marsden v Regan* [1954] 1 WLR 423 (CA) 435 (Evershed MR): "essentially a matter within the discretion of the judge".

C. Exemption clauses

- Duty modification
- Extended powers
- Liability exclusion

- Law Commission, 'Trustee Exemption Clauses' (Law Com No 301 Cm 6874, 2006). NB part two (current law).

(1) Duty modification

LORD TEMPLEMAN'S JUDGMENT IN HAYIM V CITIBANK NA

- *Hayim v Citibank NA* [1987] AC 730 (PC)
- Clause ten: "At the time of my death I may be the owner of a residence in Hong Kong. If either of my brother, Albert Joseph Hayim, and my sister, Maisie Ruby Abraham, shall survive me, then I direct that my executor and trustee shall have no responsibility or duty with respect to such property … and my executor's and trustee's only duty and responsibility with respect thereto shall arise … upon the death of the survivor of my said brother and my said sister, whichever shall first occur…."

- *Hayim v Citibank NA* [1987] AC 730 (PC) 744 (Lord Templeman):
  Citibank "was entitled to consider the beneficiaries but owed no duty to the beneficiaries under the American will to consider them or decide in their favour and accordingly as against those beneficiaries the first defendant committed no breach of trust. If the first defendant made a decision to direct the sale of the house to be postponed in the interests of Albert and Maisie this was a decision which the first defendant was entitled to make by clause 10 of the American will":

NOTABLE FEATURES OF THE PRIVY COUNCIL'S APPROACH

Autonomy

- *Hayim v Citibank NA* [1987] AC 730 (PC) 744 (Lord Templeman):
  "It is of course unusual for a testator to relieve the trustee of his will of any responsibility or duty in respect of trust property, but a testator may do as he pleases and in the present case the provisions of clause 10 are explicable and understandable."

Construction

- *Hayim v Citibank NA* [1987] AC 730 (PC) 745 (Lord Templeman):
  The "inevitable conclusion is that clause 10 was intended to enable the first defendant to decide that although Albert and Maisie were not beneficially interested in the house nevertheless Albert and Maisie should be allowed to remain in the house."
- Gives effect to the testator's purpose

No breach of trust

- *Hayim v Citibank NA* [1987] AC 730 (PC) 746 (Lord Templeman):
  Clause 10 "authorised the first defendant to make a decision that the sale of the house should be postponed without regard to the interests of the beneficiaries … The first defendant did not commit a breach of the trusts of the American will by directing the second defendant to postpone sale."

EVALUATION

- Permissive approach
- Commercial trusts – NB Law Commission, 'Trustee Exemption Clauses' (Law Com No 301 Cm 6874, 2006) pp47-58 and Appendix D.
- Family trusts
- Pension trusts

THE "IRREDUCIBLE CORE"

- A trustee with no duties is not a trustee. But what are the minimum duties required for a valid trust?
- *Hayim v Citibank NA* [1987] AC 730 (PC)
- D Hayton, 'The Irreducible Core Content of Trusteeship' in A Oakley (ed) *Trends in Contemporary Trust Law* (Clarendon Press, Oxford 1996)
- Accountability + ?

PROHIBITION CLAUSES

(2) Extended powers

- Permits the trustees to do something they otherwise couldn't.
- But it might still be a breach of trust to do what the clause permits.

(3) Liability exclusion

- *Armitage v Nurse* [1998] Ch 241 (CA)
- Clause 15: "No trustee shall be liable for any loss or damage which may happen to Paula's fund or any part thereof or the income thereof at any time or from any cause whatsoever unless such loss or damage shall be caused by his own actual fraud….".

MILLETT LJ'S JUDGMENT

- Trustee only liable for loss caused by "his own actual fraud" (*Armitage v Nurse* [1998] Ch 241 (CA) 250).

- *Armitage v Nurse* [1998] Ch 241 (CA) 251 (Millett LJ):
  Fraud "connotes at the minimum an intention on the part of the trustee to pursue a particular course of action, either knowing that it is contrary to the interests of the beneficiaries or being recklessly indifferent whether it is contrary or not."

- *Armitage v Nurse* [1998] Ch 241 (CA) 251 (Millett LJ):
- "In my judgment clause 15 exempts the trustee from liability for loss or damage to the trust property no matter how indolent, imprudent, lacking in diligence, negligent or wilful he may have been, so long as he has not acted dishonestly."

IRREDUCIBLE CORE OF OBLIGATIONS

- *Armitage v Nurse* [1998] Ch 241 (CA) 253-254 (Millett LJ):
  "I accept the submission made on behalf of Paula that there is an irreducible core of obligations owed by the trustees to the beneficiaries and enforceable by them which is fundamental to the concept of a trust. If the beneficiaries have no rights enforceable against the trustees there are no trusts. But I do not accept the further submission that these core obligations include the duties of skill and care, prudence and diligence. The duty of the trustees to perform the trusts honestly and in good faith for the benefit of the beneficiaries is the minimum necessary to give substance to the trusts, but in my opinion it is sufficient." (253-254)

- *Hayim v Citibank NA* [1987] AC 730 (PC)
- J Penner, 'Exemptions' in P Birks and A Pretto (eds), *Breach of Trust* (Hart Publishing, Oxford 2002)
- Core duties vs standard of performance

CANNOT EXPLOIT THE EXEMPTION CLAUSE

- *Armitage v Nurse* [1998] Ch 241 (CA) 254 (Millett LJ):
  "a trustee who relied on the presence of a trustee exemption clause to justify what he proposed to do would thereby lose its protection: he would be acting recklessly".

THE CURRENT LAW

- *Bogg v Raper* (1998-1999) 1 ITELR 267 (CA)
- *Wight v Olswang* (1998-99) 1 ITELR 783 (CA) (Peter Gibson LJ): "there can be no doubt that the trustee claiming exemption will not have his liability excluded unless he comes clearly within the exemption, and that he cannot do if there is ambiguity created by the two inconsistent clauses."

- *Barraclough v Mell* [2005] EWHC 3387 (Ch), [2006] WTLR 203
- *Baker v JE Clark & Co (Transport) UK Ltd* [2006] EWCA Civ 464, [2006] PLR 131

- *Spread Trustee v Hutcheson* [2012] 1 All ER 251 at [46]-[63]

5. PROPRIETARY CLAIMS

A. Preliminaries to a proprietary claim

- *Chase Manhattan Bank NA v Israel-British Bank (London) Ltd* [1981] Ch 105 (Ch) 120 (Goulding J): "the equitable remedy of tracing"
- The three stage process: proprietary base and fiduciary relationship; tracing and following; claiming.

- *Foskett v McKeown* [2001] 1 AC 102 (HL) 128 (Lord Millett):
  Tracing is "is merely the process by which a claimant demonstrates what has happened to his property, identifies its proceeds and the persons who have handled or received them, and justifies his claim that the proceeds can properly be regarded as representing his property."

- *Foskett v McKeown* [2001] 1 AC 102 (HL) 128 (Lord Millett):
  "He will normally be able to maintain the same claim to the substituted asset as he could have maintained to the original asset…. The successful completion of a tracing exercise may be preliminary to a personal claim… or a proprietary one"

(1) Advantages of equity

- Common law tracing rules: cannot trace through mixed funds, proprietary remedies not generally available.
- Equitable tracing rules: can trace through mixed funds, can obtain the return of specific property

(2) Fiduciary relationship

- *Re Hallett's Estate* (1879-80) LR 13 Ch D 696
- *Boscawen v Bajwa* [1996] 1 WLR 328 (CA) 335 (Lord Millett): "It is still a prerequisite of the right to trace in equity that there must be a fiduciary relationship"
- *Agip (Africa) Ltd v Jackson* [1991] Ch 547 (CA)

- *Foskett v McKeown* [2001] 1 AC 102 (HL) 128 (Lord Millett):
  "There is certainly no logical justification for allowing any distinction between [the common law and equitable tracing rules] 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."

- *Compagnie Noga D'Importation Et D'Exportation SA v Australia and New Zealand Banking Group Ltd* [2005] EWHC 225 (Comm) [16] (Langley J)
- *Shalson v Russo* [2003] EWHC 1637 (Ch), [2005] Ch 281 [104] (Rimer J)
- *Campden Hill Ltd v Chakrani* [2005] EWHC 911 (Ch) [74] (Hart J): "the Claimant must first establish a fiduciary relationship arising either from a division of the legal and beneficial ownership in the monies sought to be traced or from the very nature of the relationship."
- L Smith, *The law of tracing* (Clarendon Press, Oxford 1997)

(3) Equitable proprietary base

- A claimant who wants to assert an equitable proprietary claim needs to start out with an equitable proprietary interest.
- *Re Goldcorp Exchange Ltd* [1995] 1 AC 74 (PC) 99 (Lord Mustill):
  The court would not "call into existence a proprietary interest" in the Goldcorp company's gold bullion, just because the company had breached a contract which concerned the bullion.

- A trust beneficiary will always have a sufficient proprietary base to bring an equitable proprietary claim
- *Chase Manhattan Bank NA v Israel-British Bank (London) Ltd* [1981] Ch 105 (Ch)
- L Smith, *The law of tracing* (Clarendon Press, Oxford 1997) 340-347

B. Following and tracing

(1) Following

- L Smith, *The law of tracing* (Clarendon Press, Oxford 1997) 67-70, 104-115.
- Locating the trust property itself.
- When following must end:
  - destruction
  - accession
  - specification

(2) Simple substitutions

- Tracing (not following)
- Concerned with value

(3) Mixed funds

BANK ACCOUNTS

- Contractual debt between banker and customer.
- A series of debts, or a single debt.
- *Clayton's case* (1815) 1 Mer 572

TRUSTEE AND BENEFICIARIES

- Particularly concerned with assets acquired using payments out of the mixed fund.

Applying Clayton's case to trusts

- *Clayton's case* (1815) 1 Mer 572
- *Pennell v Deffell* (1853) 4 De G M & G
- Bank account appears externally as a mixed fund, not a series of debts.
- *Clayton's case* produces arbitrary results.

Re Hallett's Estate

- *Re Hallett's Estate* (1879-80) LR 13 Ch D 696, 728 (Jessel MR)
  "where a man does an act which may be rightfully performed, he cannot say that that act was intentionally and in fact done wrongly. … When we come to apply that principle to the case of a trustee who has blended trust moneys with his own, it seems to me perfectly plain that he cannot be heard to say that he took away the trust money when he had a right to take away his own money."

- *Re Hallett's Estate* (1879-80) LR 13 Ch D 696, 728 (Jessel MR): "a very convenient rule"
- The "presumption of honesty".

Re Oatway

- *Re Oatway* [1903] 2 Ch 356 (Ch) 360 (Joyce J):
  "when the private money of the trustee and that which he held in a fiduciary capacity have been mixed in the same banking account, from which various payments have from time to time been made, then, in order to determine to whom any remaining balance or any investment that may have been paid for out of the account ought to be deemed to belong, the trustee must be debited with all the sums that have been withdrawn and applied to his own use so as to be no longer recoverable, and the trust money in like manner be debited with any sums taken out and duly invested in the names of the proper trustees."

- Tension between *Re Hallett's Estate* and *Re Oatway*

A pragmatic approach

- In each case the court has rejected the previous rule because it would advantage the trustee at the expense of the beneficiaries.

- L Smith, *The law of tracing* (Clarendon Press, Oxford 1997) 199:
  "The basic principle is that a contributor can assert her interest in any part of the mixture; and against a wrongdoing contributor, she need not concede the same ability. … once the claimant's value is traced into a bank account, she has the option of asserting that her contribution subsists in the account even if subsequent withdrawals are made. Alternative, if she prefers, she can assert that it is traceable into a sum withdrawn, or into part of a sum withdrawn. If the balance remaining in the account is inadequate, she can even assert that part of her value remains in it, and part of it was withdrawn."

- JE Penner, *The law of trusts* (Core text series, 6th edn OUP, Oxford 2008) 344:
  The outcome of these cases is "to give the beneficiary the right to control the bookkeeping of the bank account to his advantage, to 'cherry-pick' the valuable expenditures"

- *Foskett v McKeown* [2001] 1 AC 102 (HL) 132 (Lord Millett)
  "the interests of the wrongdoer who was responsible for the mixing and those who derive title under him otherwise than for value are subordinated to those of innocent contributors. As against the wrongdoer and his successors, the beneficiary is entitled to locate his contribution in any part of the mixture and to subordinate their claims to share in the mixture until his own contribution has been satisfied."

- *Sinclair Investments (UK) Ltd v Versailles Trade Finance Ltd* [2011] EWCA Civ 347, [2011] 3 WLR 1153 [138] (Lord Neuberger MR): "Where he has mixed the funds held on trust with his own funds, the onus should be on the fiduciary to establish that part, and what part, of the mixed fund is his property."

- *Shalson v Russo* [2003] EWHC 1637 (Ch), [2005] Ch 281 [144] (Rimer J)
  "The justice of this ['cherry-picking'] is that, if the beneficiary is not entitled to do this, the wrongdoing trustee may be left with all the cherries and the victim with nothing."

- *Turner v Jacob* [2006] EWHC 1317 (Ch) [102] (Patten J):
  "It seems to me that in a case (such as the present) where the trustee maintains in the account an amount equal to the remaining trust fund, the beneficiary's right to trace is limited to that fund."

Justifying "cherry-picking"

- Beneficiaries can take advantage of the uncertainty caused by the mixing to assert the most valuable possible claim.
- More difficult when the dispute is between proprietary claimants and a trustee's unsecured creditors.
- Does "cherry-picking" identify the beneficiaries' property?

- L Smith, *The law of tracing* (Clarendon Press, Oxford 1997) 158:
  The claimant's right to "cherry-pick" "derives from the principle that if a defendant is guilty of a wrongful interference with property, all reasonable inferences will be drawn against the defendant in valuing the property".

- *Armory v Delamirie* (1795) 1 Str 505 (Pratt CJ)
- Bankruptcy does not give the creditors a better right to the bankrupt's property than he himself had – even if the bankrupt was a "wrongdoer" and the creditors are "innocent".

- Beneficiaries are entitled to prevent the trustee mixing trust money with his own money. Creditors have no such entitlement.

LOWEST INTERMEDIATE BALANCE

- *James Roscoe (Bolton) Ltd v Winder* [1915] 1 Ch 62 (Ch)
- "Lowest intermediate balance" rule

- *James Roscoe (Bolton) Ltd v Winder* [1915] 1 Ch 62 (Ch) 69 (Sargant J):
- "it is impossible to attribute to him that by the mere payment into the account of further moneys, which to a large extent he subsequently used for purposes of his own, he intended to clothe those moneys with a trust in favour of the plaintiffs."

- L Smith, *The law of tracing* (Clarendon Press, Oxford 1997) 303-305.

INNOCENT CONTRIBUTORS

- Neither party is a "wrongdoer". Each must be treated equally.

First in, first out

- *Re Stenning* [1895] 2 Ch 433 (Ch) 436 (North J):
  "According to In re Hallett's Estate, the rule in Clayton's Case applies as between two cestuis que trust, whose money the trustee has paid into his own account at his bankers, and therefore this balance consisted of those trust moneys which had been most recently paid in."

Alternative methods

- *Barlow Clowes International Ltd v Vaughan* [1992] 4 All ER 22 (CA) 33 (Dillon LJ):
  "the decisions of this court, in my judgment, establish and recognise a general rule of practice that *Clayton's Case* is to be applied when several beneficiaries' moneys have been blended in one bank account and there is a deficiency. It is not, in my judgment, for this court to reject that long-established general practice." (33)

- *Barlow Clowes International Ltd v Vaughan* [1992] 4 All ER 22 (CA) 42 (Woolf LJ):
  "the use of the rule is a matter of convenience and if its application in particular circumstances would be impracticable or result in injustice between the investors it will not be applied if there is a preferable alternative."

- Proportionate sharing and the "North American" method.
- T is a trustee. He has a bank account containing £1000 of his own money. In breach of trust, he pays money from separate trusts for A, B and C into his own bank account. First T pays in £600 from A's trust. Then T pays in £400 from B's trust. Then T spends £1400 on a holiday. Finally, T pays in £200 of C's money. This leaves a balance in the account of £800.

Comparing the possibilities

- Reflecting the parties' intentions.

- *Barlow Clowes International Ltd v Vaughan* [1992] 4 All ER 22 (CA) 42 (Woolf LJ):
  "If the North American solution is practical this would probably have advantages over the pari passu solution. However, the complications of applying the North American solution in this case make [proportionate sharing] the most satisfactory." (42)

Innocent non-contributors

- *Foskett v McKeown* [2001] 1 AC 102 (HL) 132 (Lord Millett):
  "It is not enough that those defending the claim are innocent of any wrongdoing if they are not themselves contributors but… are volunteers who derive title under the wrongdoer otherwise than for value. On ordinary principles such persons are in no better position than the wrongdoer, and are liable to suffer the same subordination of their interests to those of the claimant as the wrongdoer would have been." (132)

(4) Debts and overdrafts

THE PROBLEM WITH DEBTS

- When the trustee pays off the debt, he doesn't receive anything in exchange – the debt is simply extinguished.
- *Bishopsgate Investment Management Ltd v Homan* [1995] Ch 211 (CA) 221 (Leggatt LJ):
  "there can be no equitable remedy against an asset acquired before misappropriation of money takes place, since ex hypothesi it cannot be followed into something which existed and so had been acquired before the money was received and therefore without its aid." (221)

- *Re Goldcorp Exchange Ltd* [1995] 1 AC 74 (PC) 105 (Lord Mustill):
  "the moneys said to be impressed with the trust were paid into an overdrawn account and thereupon ceased to exist"
- *Customers of BA Peters Plc v* Moriarty [2008] EWCA Civ 1604

INTENTION

- *Bishopsgate Investment Management Ltd v Homan* [1995] Ch 211 (CA)
  - Trustee bought an asset using the overdraft, intending at the time to repay the overdraft using trust money.
  - Trust money was used to pay down an overdraft with a view to making the overdraft available to buy some particular asset.

- Tracing has nothing to do with intention.

- If the trustee pays back the overdraft with trust money, then uses the overdraft to buy an asset, that asset is not bought with the beneficiaries' value. It is bought with the bank's value: L Smith, *The law of tracing* (Clarendon Press, Oxford 1997) 146-152.

"BACKWARDS" TRACING

- L Smith, 'Tracing into the payment of a debt' (1995) 54 CLJ 290

- Purchase on Credit
- Sale of goods
- Vendor's perspective

- L Smith, 'Tracing into the payment of a debt' (1995) 54 CLJ 290, 294:
  "the debt is a red herring in the tracing exercise; it is just the means by which the price is paid, with some delay. But the price is paid for the asset bought, and so the price is traceable into that asset."

- *Foskett v McKeown* [2001] 1 AC 102 (HL)

- M Conaglen, 'Difficulties with Backwards Tracing' (2011) 127 LQR 432
- Criticisms of Smith's analysis
  - Authority
  - Policy

C. Claiming

(1) Beneficial ownership or equitable charge

- Proportionate beneficial ownership of the traceable proceeds – advantageous if the property has increased in value.

- Charge over the traceable proceeds to secure repayment of the money misappropriated from the trust fund – advantageous if the property has fallen in value.

(2) Simple substitution by trustee

- *Foskett v McKeown* [2001] 1 AC 102 (HL) 130 (Lord Millett): "The trustee cannot be permitted to keep any profit resulting from his misappropriation for himself"

- Falsification and tracing
- *Foskett v McKeown* [2001] 1 AC 102 (HL) 130 (Lord Millett):
  the beneficiaries are entitled "to bring a personal claim against the trustee for breach of trust and enforce an equitable lien or charge on the proceeds to secure restoration of the trust fund."
- Adoption of the transaction as a secured loan: JE Penner, *The law of trusts* (Core text series, 6th edn OUP, Oxford 2008) 354.

(3) Simple substitution by innocent third party

- Innocent non-contributor
- No personal obligation

- Beneficial ownership or charge to secure repayment by trustee (not by the third party)
- Adoption of the transaction as placement of the trust property with a custodian trustee: JE Penner, *The law of trusts* (Core text series, 6th edn OUP, Oxford 2008) 355-356.

(4) Mixed funds: trustee and beneficiaries

- *Re Hallett's Estate* (1879-80) LR 13 Ch D 696, 709 (Jessel MR)
  "where a trustee has mixed the money with his own… the cestui que trust , or beneficial owner, can no longer elect to take the property, because it is no longer bought with the trust-money simply and purely, but with a mixed fund. He is, however, still entitled to a charge on the property purchased, for the amount of the trust-money laid out in the purchase"

FOSKETT V MCKEOWN

- The leading case: *Foskett v McKeown* [2001] 1 AC 102 (HL)
- Beneficiaries want proportionate ownership of the £1 million death benefit – approximately £400,000.
- Children want to limit the beneficiaries to a charge to secure repayment of the misappropriated trust money – approximately £20,000, plus interest.

Court of Appeal judgments

- Scott V-C: analogy with improvement or maintenance of existing property.
- Lord Millett: This creates a capricious distinction based on who paid which premium.

- Hobhouse LJ: causation argument – use of the trust fund to pay the later premiums made no difference to the outcome.
- Lord Millett: attribution, not causation.

- *Foskett v McKeown* [2001] 1 AC 102 (HL) 137 (Lord Millett):
  "The question is not whether the same death benefit would have been payable if the last premium or last few premiums had not been paid. It is whether the death benefit is attributable to all the premiums or only to some of them. The answer is that death benefit is attributable to all of them because it represents the proceeds of realising the policy, and the policy in turn represents the product of all the premiums."

Arguments in the House of Lords

- The children are innocent of any wrongdoing, and would have stopped their father misappropriating trust money if they had known of it.

- Based on the rejected causation approach of Hobhouse LJ.
- Being an innocent volunteer is not a defence.

- Not "fair and equitable" to give the beneficiaries a share of the £1 million.
- *Foskett v McKeown* [2001] 1 AC 102 (HL) 120 (Lord Hope - dissenting): "it must be divided between the competitors in such proportions as can be shown to be equitable."

- *Foskett v McKeown* [2001] 1 AC 102 (HL) 109 (Lord Browne-Wilkinson):
  "This case does not depend on whether it is fair, just and reasonable to give the purchasers an interest as a result of which the court in its discretion provides a remedy. It is a case of hard-nosed property rights."

- If the beneficiaries can claim £400,000 of the death benefit they will be unjustly enriched by an undeserved windfall.
  Simply an aspect of property ownership – like a landowner discovering oil under his land.

(5) Mixed funds: innocent contributors

- It is not permissible to subordinate the interests of one contributor to the interests of another contributor.

PROPORTIONATE BENEFICIAL OWNERSHIP ONLY

- No contributor entitled to a charge, as this would give them priority over the other contributors. All must be beneficial co-owners.

- *Foskett v McKeown* [2001] 1 AC 102 (HL) 132 (Lord Millett):
  "Innocent contributors … must be treated equally inter se. Where the beneficiary's claim is in competition with the claims of other innocent contributors, there is no basis upon which any of the claims can be subordinated to any of the others. Where the fund is deficient, the beneficiary is not entitled to enforce a lien for his contributions; all must share rateably in the fund."

THE EXCEPTIONAL RULE IN RE TILLEY'S WILL TRUSTS

- *Re Tilley's Will Trusts* [1967] Ch 1179 (Ch) (Ungoed-Thomas J)
- Since the trustee could have made the purchase without using trust money at all, and so did not rely on using the trust money to acquire the property, the beneficiaries should only be entitled to a charge.

- Brian innocently receives £100 of trust money and puts it in his bank account, which already contains £100. He withdraws £1 and uses it to buy a lottery ticket, and wins £1 million.
- The orthodox view is that the beneficiaries are entitled to half the lottery winnings.

- D Hayton, 'Overview' in P Birks and A Pretto (eds), *Breach of Trust* (Hart Publishing, Oxford 2002) 391-392:
  The innocent contributor "would have exclusively used her own money, if she had known the purchasing pool of money was tainted with trust money, then [the innocent contributor] should exclusively be owner of the lottery ticket winnings…."

- The problem with this approach is that it seems to deny that the beneficiary can trace into the lottery ticket purchase at all, and to do based on a causation argument. If this is right, then the beneficiary should have no proprietary remedy at all: JE Penner, *The law of trusts* (Core text series, 6th edn OUP, Oxford 2008) 359-360.

- *Foskett v McKeown* [2001] 1 AC 102 (HL)
- *Bishopsgate Investment Management Ltd v Homan* [1995] Ch 211 (CA)

(6) Multiple claims

- Continuing beneficial interest in exchange products, subject to rule against double recovery
- Power to vest beneficial interest in particular property.

(7) Claiming without tracing into a particular asset

- *Space Investments Ltd v Canadian Imperial Bank of Commerce Trust Co (Bahamas) Ltd* [1986] 1 WLR 1072 (PC) 1074 (Lord Templeman):
  The beneficiaries would be entitled: "to trace the trust money to all the assets of the bank and to recover the trust money by the exercise of an equitable charge over all the assets of the bank."

- *Re Goldcorp Exchange Ltd* [1995] 1 AC 74 (PC) 109 (Lord Mustill):
  "In the case of a bank which employs all borrowed moneys as a mixed fund for the purpose of lending out money or making investments, any trust money unlawfully borrowed by a bank trustee may be said to be latent in the property acquired by the bank and the court may impose an equitable lien on that property for the recovery of the trust money."

- *Bishopsgate Investment Management Ltd v Homan* [1995] Ch 211 (CA) 222 (Leggatt LJ):
  "That decision is authority for no wider proposition than that, where a bank trustee wrongly deposits money with itself, the trustee can trace into all the bank's credit balances."

D. Defences

(1) Bona fide purchase

- Bona fide purchase of a legal interest for value without notice of a pre-existing equitable interest.
- A property law defence based on the historic jurisdiction of the Court of Chancery.
- Only effective against *following* not *tracing*.
- L Smith, *The law of tracing* (Clarendon Press, Oxford 1997) 386-396.
- *Sinclair Investments (UK) Ltd v Versailles Trade Finance Ltd* [2011] EWCA Civ 347, [2011] 3 WLR 1153 [102]-[108]: no automatic knowledge of legal consequences from knowledge of facts

(2) Change of position

- Accepted as a defence to personal liability in unjust enrichment.
- *Lipkin Gorman v Karpnale Ltd* [1991] 2 AC 548 (HL)

- Knowing receipt
- L Smith, *The law of tracing* (Clarendon Press, Oxford 1997) 383-386.

E. Justifying proprietary claims

UNJUST ENRICHMENT

- L Smith, *The law of tracing* (Clarendon Press, Oxford 1997) 293-296, 299-303.

PERSISTENT PROPERTY RIGHTS

- *Foskett v McKeown* [2001] 1 AC 102 (HL) 127 (Lord Millett):
  "The transmission of a claimant's property rights from one asset to its traceable proceeds is part of our law of property, not of the law of unjust enrichment. There is no "unjust factor" to justify restitution (unless "want of title" be one, which makes the point). The claimant succeeds if at all by virtue of his own title, not to reverse unjust enrichment."
- P Birks, *Unjust enrichment* (Clarendon law series, 2nd edn OUP, Oxford 2005) 34-36.

6. THIRD PARTIES

- Personal remedies, not proprietary
- *Barnes v Addy* (1873) LR 9 Ch App 244 (Court of Appeal in Chancery): liability as a "constructive trustee". But this disguises the differences between different types of liability.

- Three possibilities:
  - Trusteeship *de son tort*;
  - Dishonest assistance;
  - Knowing receipt.

A. Trusteeship *de son tort*

(1) The scope of the liability

- *Mara v Browne* [1896] 1 Ch 199 (CA)

- *Mara v Browne* [1896] 1 Ch 199 (CA) 209 (Smith LJ)
  "Now, what constitutes a trustee de son tort? It appears to me if one, not being a trustee and not having authority from a trustee, takes upon himself to intermeddle with trust matters or to do acts characteristic of the office of trustee, he may thereby make himself what is called in law a trustee of his own wrong— i.e., a trustee de son tort, or, as it is also termed, a constructive trustee."

- *Mara v Browne* [1896] 1 Ch 199 (CA) 207 (Lord Herschell LC)
  "Hugh Browne was certainly not purporting or intending to act as trustee, nor was he supposed by any one to be so acting. He purported to act throughout as solicitor, and was understood by all parties to be so acting."

- *Mara v Browne* [1896] 1 Ch 199 (CA) 213 (Rigby LJ)
  "Hugh Browne in all that he did during the interval acted in the capacity of solicitor for one of the two trustees, whose directions as to investments were accepted or acted on by the other."

- Intermeddling
- Not just the abstract quality of what was done – but *why* the third party acted as he did

(2) The role of agents

- *Williams-Ashman v Price and Williams* [1942] Ch 219 (Ch) 228 (Bennett J)
  An honest agent in possession of trust money is only liable as a trustee de son tort if he intermeddles by doing "acts characteristic of a trustee and outside the duties of an agent".
- The scope of the liability is itself defined by the scope of the agency.

(3) The purpose of the liability

- Ensures that beneficiaries have adequate remedies against purported trustees – invalidity of appointment is not a sufficient defence
- A trustee *de son tort* assumes the obligations of trusteeship *voluntarily* by deliberate intermeddling.
- Wider policy of holding people to responsibilities they voluntarily assume: *Hedley Byrne v Heller & Partners Ltd* [1964] AC 465 (HL)

- An agent, such as a solicitor, voluntarily assumes only that role – a solicitor acting for the trustees undertakes to act properly as solicitor, not to act as a trustee.
- The law should facilitate the proper use of agents and advisors by trustees to enhance the standard of trust management.

(4) Possession of trust assets

- *Re Barney* [1892] 2 Ch 265 (Ch) 273 (Kekewich J)
  "A trustee, properly so called, must, according to my view, have property committed to his charge."

- Based on the idea of the trustee *de son tort* as a constructive trustee. But not founded in principle.
- Trustees might defer to the decisions of a third party who never has control of the trust property itself: S Gardner, *An introduction to the law of trusts* (Clarendon law series, 2nd edn OUP, Oxford 2003) 279.

B. Dishonest assistance

(1) The nature of the liability

- Wider than trusteeship *de son tort*.

PRIMARY OR SECONDARY LIABILITY

- Secondary liability – equivalent to accessory liability in criminal law, or the tort of inducing breach of contract.
- Equitable wrong – primary liability for the assistant's own wrongful conduct

PURPOSE OF IMPOSING LIABILITY ON THIRD PARTIES

- *Royal Brunei Airlines Sdn Bhd v Tan* [1995] 2 AC 378 (PC) 386-387 (Lord Nicholls)
- Deterring outside interference with an ongoing legal relationship, and compensating the beneficiaries when deterrence fails.

(2) Primary breach of trust

- A primary breach of trust is essential if dishonest assistance is a form of secondary liability.

TYPES OF PRIMARY BREACH: INNOCENT AND FRAUDULENT

- *Barnes v Addy* (1873) LR 9 Ch App 244 (Court of Appeal in Chancery) 251 (Lord Selborne LC)
  A third party is liable as a constructive trustee for "participating in any fraudulent conduct of the trustee to the injury of the *cestui que trust*."

- Fraudulent breach requirement is finally rejected in *Royal Brunei Airlines Sdn Bhd v Tan* [1995] 2 AC 378 (PC).

DISHONEST ASSISTANT WITHOUT A PRIMARY BREACH

- S Gardner, 'Knowing assistance and knowing receipt: taking stock ' (1996) 112 LQR 56, 68.
- Tension between secondary liability and equitable wrong.
- Spectrum of assistant wrongdoing; at one extreme the assistant so successfully dupes the trustee that the trustee commits no breach of trust. Should the assistant then escape liability too?

- An equivalent problem in the criminal law: *R v Cogan* [1976] QB 217 (CA).
- The criminal law solution: to deny the need for established primary liability to support secondary liability.

- But the third party will always be subject to the trustee's claim in respect of his wrongful conduct – and the trustee must enforce the claim in the beneficiaries' interests. So do the beneficiaries need a direct claim against the third party?

(3) Assistance

- C Mitchell, 'Assistance' in P Birks and A Pretto (eds), *Breach of Trust* (Hart Publishing, Oxford 2002) 171:
  "There are of course as many ways to facilitate the commission of a primary breach as the human imagination can contrive".

- Third party liable for both *assisting* and *procuring* a breach of trust: *Royal Brunei Airlines Sdn Bhd v Tan* [1995] 2 AC 378 (PC) 384.

- Minimal causal requirement: *Baden v Société Générale Pour Favoriser le Developpement du Commerce et de L'industrie en France S.A* [1993] 1 WLR 509 (Ch) 574-575 (Peter Gibson J).
- Passive acquiescence not sufficient: *Brinks Ltd v Abu-Saleh (No 3)* The Times 23 October 1995 (Ch) (Rimer J)

- *Royal Brunei Airlines Sdn Bhd v Tan* [1995] 2 AC 378 (PC) 389 (Lord Nicholls):
  "honesty and its counterpart dishonesty are mostly concerned with advertent conduct".
- *Fitzalan-Howard* v Hibbert [2009] EWHC 2855 (QB) (Tomlinson J).

(4) Dishonesty

- "Assistance" is extremely wide. So the fault requirement must be correspondingly discriminating.

ALTERNATIVES TO FAULT

- No assistance liability at all.
- *Royal Brunei Airlines Sdn Bhd v Tan* [1995] 2 AC 378 (PC) 386-387: beneficiaries' entitlement to non-interference

- Strict liability.
- *Royal Brunei Airlines Sdn Bhd v Tan* [1995] 2 AC 378 (PC) 387 (Lord Nicholls):
  "everyday business would become impossible if third parties were to be held liable for *unknowingly* interfering in the due performance of such personal obligations"

STANDARDS OF FAULT

Negligence

- *Royal Brunei Airlines Sdn Bhd v Tan* [1995] 2 AC 378 (PC) 391 (Lord Nicholls):
  A third party assistant would be liable "if he procures or assists in a breach of trust of which he would have become aware had he exercised reasonable diligence"

- Obligations of care and skill should be voluntarily undertaken, or imposed only for compelling reasons.
- *Royal Brunei Airlines Sdn Bhd v Tan* [1995] 2 AC 378 (PC) 392 (Lord Nicholls):
  "beneficiaries cannot reasonably expect that all the world dealing with their trustees should owe them a duty to take care lest the trustees are behaving dishonestly."

- S Gardner, 'Knowing assistance and knowing receipt: taking stock ' (1996) 112 LQR 56, 78-84.
  - Banks, solicitors etc do already have onerous obligations in relation to potential money laundering.
  - Welfarist perspective – brings about insurance of potential losses, and ultimately benefits the beneficiaries.
  - Agents and advisors would have an incentive to police the activities of trustees.

- The risk of improper trustee behaviour is inherent to the trust structure. The beneficiaries assume that risk, in return for the benefits of independent management or wealth structuring. They cannot retain those benefits whilst shifting the associated risk onto third parties.

Unconscionability

- "Unconscionability" has no clear meaning.

Dishonesty

- *Royal Brunei Airlines Sdn Bhd v Tan* [1995] 2 AC 378 (PC) 389 (Lord Nicholls):
  Definition of dishonesty: "simply not acting as an honest person would in the circumstances."

- *Royal Brunei Airlines Sdn Bhd v Tan* [1995] 2 AC 378 (PC) 389 (Lord Nicholls):
  This is an objective standard. There is a subjective element, in that "it is a description of a type of conduct assessed in the light of what a person actually knew at the time, as distinct from what a reasonable person would have known or appreciated."

- *Royal Brunei Airlines Sdn Bhd v Tan* [1995] 2 AC 378 (PC) 391 (Lord Nicholls).
  "when called upon to decide whether a person was acting honestly, a court will look at all the circumstances known to the third party at the time. The court will also have regard to personal attributes of the third party, such as his experience and intelligence, and the reason why he acted as he did."

- *Royal Brunei Airlines Sdn Bhd v Tan* [1995] 2 AC 378 (PC) 389 (Lord Nicholls).
  But "these subjective characteristics of honesty do not mean that individuals are free to set their own standards of honesty in particular circumstances. The standard of what constitutes honest conduct is not subjective. Honesty is not an optional scale...."

SUBJECTIVE AND OBJECTIVE STANDARDS

- *Twinsectra Ltd v Yardley* [2002] UKHL 12, [2002] 2 AC 164 (Lord Hutton)
- Combined objective and subjective test: the defendant's conduct must be dishonest by the standards of ordinary people, and the defendant must realise that ordinary people would think his conduct dishonest.

- *Twinsectra Ltd v Yardley* [2002] UKHL 12, [2002] 2 AC 164 [35] (Lord Hutton):
  "A finding by a judge that a defendant has been dishonest is a grave finding, and it is particularly grave against a professional man, such as a solicitor."

- *Barlow Clowes International Ltd v Eurotrust International Ltd* [2005] UKPC 37, [2006] 1 WLR 1476 [16] (Lord Hoffmann):
  ""consciousness that one is transgressing ordinary standards of honest behaviour" was in their Lordships' view intended to require consciousness of those elements of the transaction which make participation transgress ordinary standards of honest behaviour. It did not also require him to have thought about what those standards were."

- A clear misrepresentation of *Twinsectra* – but it produces the right result.
- The problem of *stare decisis*: *Abou-Rahmah v Abacha* [2005] EWHC 2662 (QB), [2006] 1 All ER (Comm) 247 [40]-[52] (Treacy J).
- *Abou-Rahmah v Abacha* [2006] EWCA Civ 1492.

- *Aerostar Maintenance International Ltd v Wilson* [2010] EWHC 2032 (Ch).
- *Al Khudairi v Abbey Brokers Ltd* [2010] EWHC 1486 (Ch).

AWARENESS OF THE BREACH OF TRUST

- *Agip (Africa) Ltd v Jackson* [1990] Ch 265 (Ch) 295 (Millett J):
  "is no answer for a man charged with having knowingly assisted in a fraudulent and dishonest scheme to say that he thought that it was "only" a breach of exchange control or "only" a case of tax evasion. It is not necessary that he should have been aware of the precise nature of the fraud or even of the identity of its victim. A man who consciously assists others by making arrangements which he knows are calculated to conceal what is happening from a third party, takes the risk that they are part of a fraud practised on that party."

- *Barlow Clowes International Ltd v Eurotrust International Ltd* [2005] UKPC 37, [2006] 1 WLR 1476 [28] (Lord Hoffmann):
  "Someone can know, and can certainly suspect, that he is assisting in a misappropriation of money without knowing that the money is held on trust or what a trust means…."

C. Knowing receipt

(1) The nature of the liability

- Purely personal liability – but easy to confuse with proprietary claims
- Liability to pay back what was *received* not just what is *retained*. Traditionally fault-based.
- Tension between property-oriented receipt-based view of knowing receipt, and knowing receipt as an equitable wrong based on fault.
- Custodial duties: C Mitchell and S Watterson, 'Remedies for Knowing Receipt' in C Mitchell (ed) Constructive and Resulting Trusts (Hart Publishing, Oxford 2010)

(2) Receipt

TRACEABLE PROCEEDS

- *El Ajou v Dollar Land Holdings plc* [1994] 2 All ER 685 (CA) 700 (Hoffmann LJ):
  "This is a claim to enforce a constructive trust on the basis of knowing receipt. For this purpose the plaintiff must show … the beneficial receipt by the defendant of assets which are traceable as representing the assets of the plaintiff" (700)

MINISTERIAL RECEIPT

- *Agip (Africa) Ltd v Jackson* [1990] Ch 265 (Ch) 291 (Millett J):
  Liability in knowing receipt attaches to someone who "receives for his own benefit trust property transferred to him in breach of trust. He is liable as a constructive trustee…."

- *Agip (Africa) Ltd v Jackson* [1990] Ch 265 (Ch) 292 (Millett J):
  "In paying or collecting money for a customer the bank acts only as his agent. It is otherwise, however, if the collecting bank uses the money to reduce or discharge the customer's overdraft. In doing so it receives the money for its own benefit."

- Apparent immunity for professional agents – why?
- S Gardner, *An introduction to the law of trusts* (Clarendon law series, 2nd edn OUP, Oxford 2003) 284:
  "like certain aspects of the law on dishonest assistance and trusteeship *de son tort*, the immunity reflects a project of protecting 'professional agents'."

- Agents and advisors should not be required to look too closely at what their customers and clients are doing – they should be entitled to assume that their customers are honest.
- This is justified by the vital need for these agency and advisory services.

(3) Fault requirement

RE MONTAGU'S ST

- *Re Montagu's Settlement Trusts* [1987] Ch 264 (Ch) (Sir Robert Megarry V-C).

Receipt vs assistance

- Dishonesty imports notions of active conduct – and receipt can be passive.
- Focus on knowledge rather than dishonesty.

Types of knowledge

- *Baden v Société Générale Pour Favoriser le Developpement du Commerce et de L'industrie en France S.A* [1993] 1 WLR 509 (Ch) 575-576 (Peter Gibson J):

  "i) actual knowledge; (ii) wilfully shutting one's eyes to the obvious; (iii) wilfully and recklessly failing to make such inquiries as an honest and reasonable man would make; (iv) knowledge of circumstances which would indicate the facts to an honest and reasonable man; (v) knowledge of circumstances which would put an honest and reasonable man on inquiry."

- Knowledge is a means of ascertaining whether the recipient's conscience is affected.
- "Notice" doesn't affect conscience, but "knowledge" does.
- *Sinclair Investments (UK) Ltd v Versailles Trade Finance Ltd* [2011] EWCA Civ 347, [2011] 3 WLR 1153 [102]-[108]: no automatic knowledge of legal consequences from knowledge of facts

BCCI V AKINDELE

- *Agip (Africa) Ltd v Jackson* [1990] Ch 265 (Ch) 291 (Millett J):
  "the person who receives for his own benefit trust property transferred to him in breach of trust. He is liable as a constructive trustee if he received it with notice, actual or constructive, that it was trust property and that the transfer to him was a breach of trust…."

- *Bank of Credit and Commerce International (Overseas) Ltd v Akindele* [2001] Ch 437 (CA) 455 (Nourse LJ):

  "What then, in the context of knowing receipt, is the purpose to be served by a categorisation of knowledge?"

  "It can only be to enable the court to determine whether… "[the recipient's] conscience is sufficiently affected for it to be right to bind him by the obligations of a constructive trustee". But, if that is the purpose, there is no need for categorisation. All that is necessary is that the recipient's state of knowledge should be such as to make it unconscionable for him to retain the benefit of the receipt."

  "For these reasons I have come to the view that, just as there is now a single test of dishonesty for knowing assistance, so ought there to be a single test of knowledge for knowing receipt. The recipient's state of knowledge must be such as to make it unconscionable for him to retain the benefit of the receipt. A test in that form, though it cannot, any more than any other, avoid difficulties of application, ought to avoid those of definition and allocation to which the previous categorisations have led."

UNCONSCIONABLE RECEIPT?

- *Royal Brunei Airlines Sdn Bhd v Tan* [1995] 2 AC 378 (PC) 392 (Lord Nicholls):
  "unconscionable is not a word in everyday use by non-lawyers. If it is to be used in this context, and if it is to be the touchstone for liability as an accessory, it is essential to be clear on what, *in this context*, unconscionable *means* . If unconscionable means no more than dishonesty, then dishonesty is the preferable label. If unconscionable means something different, it must be said that it is not clear what that something different is. Either way, therefore, the term is better avoided in this context."

- Judges will continue to make decisions based on actual knowledge or constructive notice, but they will do so in order to pronounce on unconscionability. As a result their reasoning will be less transparent.

(4) Unjust enrichment

COMMON LAW: UNJUST ENRICHMENT AND CHANGE OF POSITION

- *Lipkin Gorman v Karpnale* Ltd [1991] 2 AC 548 (HL).
- Strict liability for unjust enrichment.
- Vigorous defence of *good faith change of position* prevents hardship to the recipient.

RECEIPT LIABILITY IN EQUITY

- Lord Nicholls, 'Knowing Receipt: The Need for a New Landmark' in W Cornish and others (eds), *Restitution, Past, Present and Future: Essays in Honour of Gareth Jones* (Hart Publishing, Oxford 1998).
- P Birks, 'Receipt' in P Birks and A Pretto (eds), *Breach of Trust* (Hart Publishing, Oxford 2002).

- Unjust enrichment and knowing receipt can run in parallel, as they serve different functions.

Receipt-based: unjust enrichment

- Restitution from an innocent recipient reverses the misapplication of trust money.
- Change of position defence prevents hardship to the recipient.

Wrong-based: knowing (dishonest) receipt

- A knowing recipient is a wrongdoing recipient.
- A wrongdoer should have to restore precisely what he received – and has no change of position defence.

OPPOSITION TO UNJUST ENRICHMENT LIABILITY

Commercial unworkability

- *Bank of Credit and Commerce International (Overseas) Ltd v Akindele* [2001] Ch 437 (CA) 456 (Nourse LJ):
  Concern that once it was shown that trust property had been misappropriated "the burden should shift to the recipient to defend the receipt either by a change of position or perhaps in some other way."

- A potentially onerous obligation – but severely mitigated by the operation of change of position.

Farah v Say-Dee

- *Farah Constructions Pty Ltd v Say-Dee Pty Ltd* [2007] HCA 22 (High Court of Australia).

- Majority adopts an anti-unjust enrichment approach

  1. Unhistorical
     But unjust enrichment was only recently recognised, so its absence from the older case law is inevitable.

2. Identification of an unjust factor
   There is a technical unjust enrichment problem with identifying an appropriate unjust factor. But the law of unjust enrichment is still developing. On some views, no specific unjust factor is required: *Pettkus v Becker* [1980] 2 SCR 834 (Supreme Court of Canada); P Birks, *Unjust enrichment* (Clarendon law series, 2nd edn OUP, Oxford 2005) chs 5, 6.

3. Injustice
   "Where is the injustice? … Say-Dee did not explain how there was any justice in permitting restitution against a defendant who received trust property without notice of that fact." [155].
   This is a denial of the justice of unjust enrichment as an independent cause of action – which is contrary to orthodox principle, and must be taken to have been rejected by the House of Lords in *Lipkin Gorman v Karpnale Ltd* [1991] 2 AC 548 (HL).

Custodial liability

- C Mitchell and S Watterson, 'Remedies for Knowing Receipt' in C Mitchell (ed) Constructive and Resulting Trusts (Hart Publishing, Oxford 2010)

FUTURE PROSPECTS

- The law will develop slowly and incrementally in this field, not least because of the practical difficulties of getting an appropriate test case before the House of Lords.

- P Birks, 'Receipt' in P Birks and A Pretto (eds), *Breach of Trust* (Hart Publishing, Oxford 2002) 239:
  "authority cannot militate indefinitely against reason, and there is no rational argument for depriving the equitable owner of the claim in unjust enrichment based on strict liability"

- C Mitchell and S Watterson, 'Remedies for Knowing Receipt' in C Mitchell (ed) Constructive and Resulting Trusts (Hart Publishing, Oxford 2010) 156:
  "Before they recognise a concurrent strict liability in unjust enrichment, however, we believe that the English courts should reflect on the nature of the remedies to which claimants would then become entitled, and recognise that these would be different from the remedies to which claimants are currently entitled under the law of knowing receipt."

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